
EEF and UK Steel Response to Ofgem Open Letter on the RIIO-2 Framework

Due by: 4 September 2017

To: Jonathan Brearley, Senior Partner, Networks at Ofgem (RIIO2@ofgem.gov.uk)

About EEF

EEF, the manufacturers' organisation, is the representative voice of UK manufacturing, with offices in London, Brussels, every English region and Wales. Collectively, we represent 20,000 companies of all sizes, from start-ups to multinationals, across engineering, manufacturing, technology and the wider industrial sector. We directly represent over 5,000 businesses who are members of EEF. Everything we do – from providing essential business support and training to championing manufacturing industry in the UK and the EU – is designed to help British manufacturers compete, innovate and grow.

UK Steel, a division of EEF, is the trade association for the UK steel industry. It represents all the country's steelmakers and a large number of downstream steel processors.

Response to Open Letter

EEF and UK Steel welcome the opportunity to respond to your open letter on the RIIO-2 Framework ahead of the launch of the formal process for the price controls.

The priority for the industrial consumers that EEF and UK Steel represent is achieving internationally competitive industrial energy prices in the UK. Given that the three key parts of the energy bill are wholesale, network and policy costs, the RIIO 2 framework will need to consider how it contributes to the UK's industrial strategy and Conservative manifesto commitment to achieve the lowest energy bills in Europe for domestic and business consumers. This includes achieving UK network costs that are competitive with EU and international counterparts. The future approach to UK network charging must not add to the consistent and significant disparity between UK and EU international industrial electricity prices.

Industrial consumers have faced real issues in engaging with and informing the changes to the energy sector that impact the competitiveness of their businesses, and we therefore welcome the focus in the open letter on improving stakeholder engagement and participation. Whilst energy may not be the 'core business' of many industrial firms, it is crucial to energy intensive industries, whilst access to secure, affordable supplies is consistently cited as a key issue by industrial firms¹.

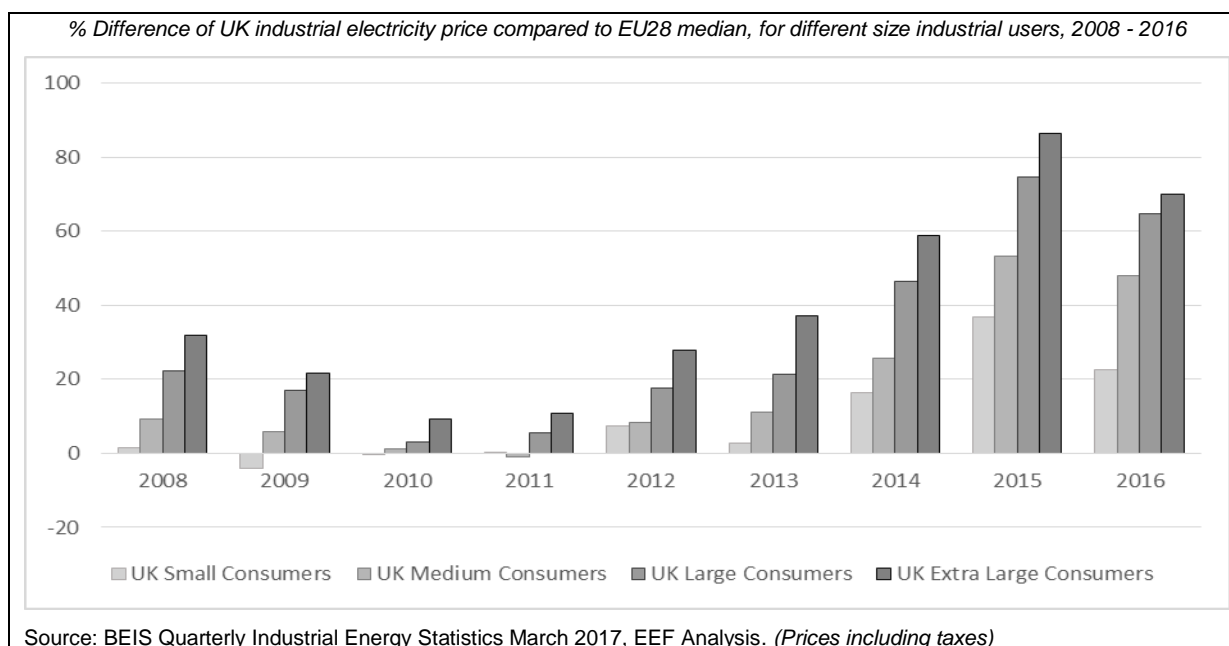
RIIO 2 therefore presents an opportunity to improve transparency and engagement with industrial consumers, who often aren't treated as 'pure consumers' (as seems to be implied in the open letter) or fully represented as 'grid users' in energy sector discussions that directly impact UK industrial firms.

¹ Consistently demonstrated in EEF surveys

The stakeholder engagement and participation proposed by network operators must include meaningful representation from industrial consumers to ensure that ‘fairness’ encompasses supporting the competitiveness of UK firms and achieving the lowest end-cost to all consumers *including* industrial consumers.

What ‘fairness’ means for industrial consumers

Multiple studies and statistics² have recognised that UK industrial firms face amongst that highest electricity prices in Europe and internationally, due to higher costs across the energy bill components of wholesale, policy and network costs. UK industrial electricity prices have increased significantly in the past few years compared to EU competitors.



As a further example, a study by UK Steel during the steel crisis demonstrated that UK electric arc furnaces face a £17/MWh disadvantage compared to German competitors, split roughly equally between wholesale, policy and network costs. It is well demonstrated that high UK electricity costs have affected the competitiveness of the UK steel industry.³

It is therefore imperative that the next price controls are also considered in the context of achieving competitive prices for the UK's industrial base, which accounts for 45% of UK exports⁴.

There are clearly uncertainties in understanding what the energy networks will look like in the 2020's, and challenges on understanding the implications for price controls. For consumers there is an additional challenge: in the volume of change proposed for network charges over the 2020's. This is due to the combination of the new price controls, and large number of changes being proposed by multiple energy industry and Ofgem-led work streams to reform how these costs are recovered from users. This is an unprecedented amount of uncertainty given the long time frames industrial firms often use to ensure an efficient response to energy prices for the coming decade, and the actions they may need to take now.

² For example, BEIS, Eurostat and IEA regularly report data on energy costs that demonstrate how uncompetitive UK industrial energy costs have been and continue to be. <https://www.gov.uk/government/statistical-data-sets/international-industrial-energy-prices>

³ The following UK Steel paper sets out the competitiveness issues caused by high UK electricity costs: <https://www.eef.org.uk/uk-steel/news-blogs-and-publications/publications/2017/mar/energy-costs-and-the-steel-sector-a-uk-steel-briefing>

⁴ EEF Industrial Strategy Policy Digest, August 2017 <https://www.eef.org.uk/campaigning/campaigns-and-issues/current-campaigns/industrial-strategy/industrial-strategy-fact-card>

Ensuring the views of all consumers are considered – from domestic to industrial consumers

We support Ofgem's objective to give consumers, including industrial consumers, a stronger voice in setting outputs, and shaping and assessing business plans. One of the challenges that industrial consumers have faced is that business plans have historically been written in a way that is relevant to the energy industry, but not to the end consumer. One thing in particular that would be useful would be an indication of potential bill impacts for different types of consumer, including types of industrial consumers.

Industrial consumers have been relatively under-represented to date in discussions about network charges (including at industry code modification level), resulting in industrial views not being fully considered in rapidly increasing network costs for many firms. Ofgem's approach to stakeholder engagement through the RIIO-2 price controls is therefore a key opportunity to reverse the lack of industrial consumer representation and lack of understanding of impacts on these consumers seen in the past.

We would welcome the opportunity to discuss further with Ofgem and network operators how the industrial consumer perspective, experience and evidence, and the issues that are most important to these consumers, can be incorporated to deliver fair and transparent decision making for the upcoming price controls.

Developing the right evidence base and transparency of information

To assess what is fair and represents good value for consumers, consumers need better and more transparent data and information about the potential implications for end consumers bills. This can include better impact assessments of individual proposals as suggested above, as well as a more explicit link to UK objectives – primarily the UK's emerging Industrial Strategy, the commitment to deliver affordable energy and clean growth, and roadmap to minimising business energy costs.

As an example the Belgian energy regulator (CREG) has produced annual reports for the past three years on the competitiveness of industrial electricity prices in Belgium against key competitors, and detailed assessment of network charging in different countries. In the 2017 report, CREG concluded that UK industrial electricity prices have been the highest when compared to Belgium, Holland, Germany and France for the past 2 years, including due to higher network costs⁵. These are extremely helpful reports, although not fully reflective of the details of the UK situation⁶.

We encourage Ofgem and Government to work together to conduct similar studies to deliver competitive industrial electricity prices, and understand the cumulative impact of bill components within Ofgem's control (directly and indirectly through the energy industry change proposals it oversees). More widely, there is a need to explicitly consider non-energy sector impacts of proposals, such as adversely impacting the international competitiveness of UK industrial firms, to ensure that regulatory change does not deliver outcomes counter to policy intentions set at a national level, such as the Industrial Strategy.

In protecting the interests of current and future consumers, and promoting fairness, the UK energy sector and network costs cannot be seen in isolation, and must consider the very real impact that network costs have on the competitiveness of UK industries, which provide wider benefits to the UK economy.

⁵ PWC for CREG, *A European comparison of electricity and gas prices for large industrial consumers*, Final Report, 2017 Update, 29 March 2017 http://www.creg.be/sites/default/files/assets/Publications/Studies/2017-PwC_Report_A_European_comparison_of_electricity_and_gas_for_large_industrial_consumers_0.pdf

⁶ EEF would be happy to provide Ofgem with support and evidence to ensure that the UK situation is more accurately reflected in these reports for CREG.

We encourage improved transparency by DNOs of the charging methodologies used to recover their costs (namely the Distribution Charging Methodology Forum (DCMF)). Whilst there may rightly be some issues and information that need to be shared and discussed confidentially by a limited number of parties, documents and meetings related to the DCMF are hidden from the consumers that they impact, limiting the ability of consumers to understand and inform the methodologies that impact their network charges.

More transparency is also needed on the overall costs of the energy networks. EEF, UK Steel and many other industrial sector representatives have long called for an Annual Energy Policy Statement (delivered by BEIS, Ofgem and National Grid). Reporting on network costs as part of such a Statement is crucial, by providing a central source of information on the overall costs of the energy system now and forecast for the future. It would also allow more consistent policy and regulatory intervention, which is currently lacking and increasingly aggravating energy issues for consumers.

Providing a central data source of the investments made by network operators, and costs recovered from categories of consumers (including industrial consumers) would provide much-needed transparency of the impacts of the evolving network and associated costs in the low carbon transition. It would allow consumers an opportunity for more informed discussions about network costs, whether these are fair, and help deliver the consumer outcomes that are most important to different categories of consumers.

Demand Side Response (DSR)

Ofgem is rightly considering how DSR might be catered for within the price controls. However, we note that the open letter refers to both demand side response or storage solutions, or *rolling out energy-efficiency measures*, which defer or avoid the need for costly network enhancements.

Energy efficiency delivers very different outcomes to DSR or storage solutions. DSR and storage are able to respond dynamically and support or strain the system when used, on a minute-by-minute basis. Energy efficiency is potentially a one-off or relatively infrequent investment by another party that the network operator may benefit from. These two issues – flexibility and energy efficiency – therefore need to be treated separately and carefully within the RIIO framework. There may be situations where large demand users invest in energy efficiency to the benefit of the network operators, and further consideration could be given to how to reward consumers who can achieve this benefit for the wider energy system.

Furthermore, thought also needs to be given to whether network operators can invest in storage solutions, and if so, to ensure it is done in a way that does not cause distortions in energy markets.

Stakeholder engagement

EEF and UK Steel are keen to provide evidence and experience to inform the approach of Ofgem and network operators to ensure that future price controls deliver in the interests of all consumers, including industrial consumers, in a fair manner. We would therefore be very keen to meet bilaterally and discuss the issues raised in this paper, and to participate in future workshops, webinars and working groups if possible.

We would also be happy to facilitate opportunities to engage directly with industrial consumers as these important proposals are developed, ahead of and during the public Framework Consultation in early 2018. Given the potentially significant competitiveness impact that these proposals, combined with network charging reforms⁷, may have on

⁷ such as the recently launched Targeted Charging Review and multiple industry code modification proposals in this area

industrial consumers, it is imperative that industrial consumer representatives can participate in working groups to inform these price controls.

FOR FURTHER INFORMATION CONTACT:

Dipali Raniga, Senior Energy & Environment Policy Adviser

Phone: 020 7654 1569

Email: draniga@eef.org.uk

Twitter: [@EEF_Environment](https://twitter.com/EEF_Environment)

Website: www.eef.org.uk
