

Anna Kulhavy  
Ofgem  
107 West Regent Street  
Glasgow G2 2BA.

Regulatory Affairs  
Ground Floor, Lakeside West  
30 The Causeway  
Staines  
Middlesex  
TW18 3BY

25 July 2017.

Dear Anna,

## **Consultation on submissions to the RIIO-ED1 Innovation Roll-out Mechanism window**

Thank you for the opportunity to respond to the above consultation. This is a non-confidential response on behalf of the Centrica Group, excluding Centrica Storage.

A finding of the review of the Low Carbon Networks Fund is benefits worth in excess of £7 billion are to be realised when solutions trialled during those projects supported by the consumer-funded network innovation stimuli are rolled out<sup>1</sup>. It is also estimated that 40% of the benefits will accrue to network operators<sup>2</sup>. As such, we welcome the roll-out of the solutions trialled in order to deliver benefits to consumers and this should be progressed as quickly as possible.

We, however, raise concerns about the Innovation Roll-out Mechanism (IRM) submissions:

- **Information presented in the submissions does not allow stakeholders to fully assess their suitability.**
- **Submissions relate to solutions that could reasonably be expected to be rolled out anyway.**
- **Requests for additional expenditure allowances should be considered in the context of licensee surpluses.**

Also, we recommend:

- **The treatment of outputs delivered and licensee benefits should be clarified.**

### **Information in the submissions does not allow stakeholders to fully assess their suitability:**

In several instances, information that would assist stakeholders to fully assess whether licensee benefits exceed implementation costs during RIIO-ED1 or whether funding has already been provided in the settlement has been redacted or has been presented in insufficient detail.

In some submissions, not all benefits expected to accrue during RIIO-ED1 have been fully quantified, nor has the profile of lifetime benefits accrual been sufficiently detailed. For

---

<sup>1</sup> “The network innovation review: our policy decision”, page 6. (<https://www.ofgem.gov.uk/publications-and-updates/network-innovation-review-our-policy-decision>).

<sup>2</sup> “The network innovation review: our policy decision”, page 7. (<https://www.ofgem.gov.uk/publications-and-updates/network-innovation-review-our-policy-decision>).

example, it is estimated that approximately £54 million of lifetime benefits will accrue from deferred network reinforcement in the *Low Voltage Network Visibility and Control System* submission. However, benefits to accrue from “...reinforcement deferral achieved by utilising granular, time-series data...” during RIIO-ED1 are referred to but have not been quantified.

Similarly, it is expected the *Enhanced Secondary Substation Monitoring* project will have a beneficial impact on customer interruptions but the benefits from avoided CMs and CIs during RIIO-ED1 have been redacted. Expenditure allowances in the RIIO-ED1 settlement for substation monitoring have also been redacted. These omissions and redactions do not allow stakeholders to fully assess the suitability of the proposals against Special Condition 3D.

**Submissions relate to solutions that could reasonably be expected to be rolled out anyway:**

We raise concerns that, generally, submissions have been made to fund the roll-out of solutions that could reasonably be expected to be implemented by licensees as part of business-as-usual (BAU) practice anyway. As an example, an application has been made for funding to implement a digitalised approach to overhead line surveys, as part of the *Holistic Overhead-line Survey Strategy* project. We suggest that the transition to digital solutions should be treated as normal improvement in BAU practice and, as such, we question the eligibility for additional funding.

A variety of active network management solutions were proposed in the licensees' RIIO-ED1 business plans and now typically constitute BAU practice. The *Enhanced Secondary Substation Monitoring* submission, for example, is justified in part based on an increase in volumes compared to those agreed during the RIIO-ED1 price control review. A key component of the RIIO framework is the latitude allowed to network operators to manage expenditure allowances and they should bear commensurate risk. An increase in volumes for solutions that now typically constitute BAU practice should be considered to fall within the scope of the risk network operators are exposed to. The provision of additional allowances for volumes outside of mechanisms specifically designed for that purpose does not represent an appropriate balance of risk and reward between consumers and network operators.

**Requests for additional expenditure allowances should be considered in the context of licensee surpluses:**

The submissions have been made on the basis it is not cost-beneficial for licensees to roll out these projects in RIIO-ED1. The IRM guidance states:

*...Licensees should also explain why, if they have generated a surplus in another area of the business, the IRM is necessary to roll out the proposed solution...*<sup>3</sup>

---

<sup>3</sup> “Electricity Distribution Innovation Roll-out Mechanism submission guidance”, section 3. (<https://www.ofgem.gov.uk/publications-and-updates/application-guidance-electricity-distribution-innovation-roll-out-mechanism-irm>).

The licensees that seek additional funding have, collectively, forecast to under-spend their existing RIIO-ED1 allowances by £941 million<sup>4</sup>. The additional expenditure allowances requested are less than a tenth of the forecast under-spend. The forecast under-spend, along with the benefits expected to accrue to licensees during RIIO-ED1, render the need for additional funding unnecessary.

**The treatment of outputs delivered and licensee benefits should be clarified:**

Clarity should be provided on the treatment of any impact these projects, if funded via the IRM, have on pre-agreed outputs and performance. Particularly, the *Integrated Network Constraint Management for Dumfries and Galloway* project involves investment meant to address constraints on the transmission network. We support the roll-out of 'whole-system' solutions that are expected to deliver long-term benefits to consumers. However, it is necessary that the treatment of both DNO and TO outputs is carefully considered since DNO-led investment could contribute to the delivery of TO outputs.

Benefits to licensees will continue to accrue beyond the end of the current price control period. It is important that licensee benefits and expected efficiencies are explicitly considered when expenditure allowances for the next round of price controls are assessed. It may also be necessary to consider redress measures if the expected outputs are not delivered as the IRM is meant to fund only Proven Innovation.

We hope you find these comments helpful. Answers to the consultation questions are attached. Please do not hesitate to contact me if you have any questions.

Yours sincerely,

Andy Manning  
Director - Network Regulation, Forecasting and Settlements

---

<sup>4</sup> Data taken from Table 2.2 in "RIIO-ED1 Annual Report 2015-16". (<https://www.ofgem.gov.uk/publications-and-updates/riio-electricity-distribution-annual-report-2015-16>)

## Answers to consultation questions

---

**Question 3: Do you consider that any of the roll-outs will allow the licensees to receive commercial benefits within the price control period, ie will the roll-out lead to cost savings and/or incentive rewards, greater than the cost of the roll-out within the price control period?**

In several instances, information that would assist stakeholders to fully assess whether licensee benefits exceed implementation costs during RIIO-ED1 has been redacted or has been presented in insufficient detail.

In some submissions, not all benefits expected to accrue during RIIO-ED1 have been fully quantified, nor has the profile of lifetime benefits accrual been sufficiently detailed. For example, it is estimated that approximately £54 million of lifetime benefits will accrue from deferred network reinforcement in the *Low Voltage Network Visibility and Control System* submission. However, benefits to accrue from "...reinforcement deferral achieved by utilising granular, time-series data..." during RIIO-ED1 are referred to but have not been quantified.

Similarly, it is expected the *Enhanced Secondary Substation Monitoring* project will have a beneficial impact on customer interruptions but the benefits from avoided CMs and CIs during RIIO-ED1 have been redacted. Expenditure allowances in the RIIO-ED1 settlement for substation monitoring have also been redacted. These omissions and redactions do not allow stakeholders to fully assess the suitability of the proposals against Special Condition 3D.

**Question 10: With reference to the IRM licence condition, do you have any significant concerns about funding any of the proposed roll-outs under the IRM? For example, do you consider it is reasonable to expect the licensee to carry out the work anyway as part of business as usual?**

We raise concerns about the provision of additional funding for the proposed roll-outs under the IRM. The IRM licence condition states that projects will not be eligible for funding if benefits expected to accrue to licensees during the current price control exceeds implementation costs. As discussed above, information that would assist stakeholders to fully assess whether licensee benefits exceed implementation costs during RIIO-ED1 has been redacted or has been presented in insufficient detail. Further, the IRM guidance states:

*...Licensees should also explain why, if they have generated a surplus in another area of the business, the IRM is necessary to roll out the proposed solution.<sup>5</sup>*

---

<sup>5</sup> "Electricity Distribution Innovation Roll-out Mechanism submission guidance", section 3. (<https://www.ofgem.gov.uk/publications-and-updates/application-guidance-electricity-distribution-innovation-roll-out-mechanism-irm>).

The licensees that seek additional funding have, collectively, forecast to under-spend their existing RIIO-ED1 allowances by £941 million<sup>6</sup>. The additional expenditure allowances requested are less than a tenth of the forecast under-spend. The forecast under-spend, along with the benefits expected to accrue to licensees during RIIO-ED1, render the need for additional funding unnecessary.

Submissions have been made to fund the roll-out of solutions that could reasonably be expected to be implemented by licensees as part of BAU practice anyway. As an example, an application has been made for funding to implement a digitalised approach to overhead line surveys, as part of the *Holistic Overhead-line Survey Strategy* project. We suggest that the transition to digital solutions should be treated as normal improvement in BAU practice and, as such, we question the eligibility for additional funding.

A variety of active network management solutions were proposed in the licensees' RIIO-ED1 business plans and now typically constitute BAU practice. The *Enhanced Secondary Substation Monitoring* submission, for example, is justified in part based on an increase in volumes compared to those agreed during the RIIO-ED1 price control review. A key component of the RIIO framework is the latitude allowed to network operators to manage expenditure allowances and they should bear commensurate risk. An increase in volumes for solutions that now typically constitute BAU practice should be considered to fall within the scope of the risk network operators are exposed to. The provision of additional allowances for volumes outside of mechanisms specifically designed for that purpose does not represent an appropriate balance of risk and reward between consumers and network operators.

Though not addressed in the IRM licence condition, clarity should be provided on the treatment of any impact these projects have on pre-agreed outputs and performance if funded via the IRM. Particularly, the *Integrated Network Constraint Management for Dumfries and Galloway* project involves investment meant to address constraints on the transmission network. We support the roll-out of 'whole-system' solutions that are expected to deliver long-term benefits to consumers. However, it is necessary that the treatment of both DNO and TO outputs is carefully considered since DNO-led investment could contribute to the delivery of TO outputs.

Benefits to licensees will continue to accrue beyond the end of the current price control period. It is important that licensee benefits and expected efficiencies are explicitly considered when expenditure allowances for the next round of price controls are assessed. It may also be necessary to consider redress measures if the expected outputs are not delivered as the IRM is meant to fund only Proven Innovation.

---

<sup>6</sup> Data taken from Table 2.2 in "RIIO-ED1 Annual Report 2015-16". (<https://www.ofgem.gov.uk/publications-and-updates/riio-electricity-distribution-annual-report-2015-16>)