

Drax Power Limited

Drax Power Station
Selby
North Yorkshire
YO8 8PH

01757 618381
www.drax.com

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RIIO Team
Network Price Controls
10 South Colonnade,
Canary Wharf,
London.
E14 4PU

RIIO Team,

Drax response to the RIIO-2 Sector Specific Methodology

Drax Group plc (Drax) owns and operates a portfolio of flexible, low carbon and renewable electricity generation assets – providing enough power for the equivalent of more than 8.3 million homes across the UK. The assets include Drax Power Station, based at Selby, North Yorkshire, which is the country's single largest source of renewable electricity. Drax also owns two retail businesses, Haven Power and Opus Energy, which together supply renewable electricity and gas to over 350,000 business premises.

We welcome the opportunity to reply to the RIIO2 Sector Specific Methodology and whilst not answering the detailed questions for each sector we would like to offer the following comments.

Price control framework and change

Drax agrees that Networks and the Electricity System Operator (ESO) are vital facilitators of change within the energy sector. A shorter price control, stronger incentives and a clear focus on promoting effective competition provide a regulatory environment for networks to adapt and facilitate this change. However, we recognise that a negative consequence of these changes is that companies may become averse to plan and contract beyond the five-year time horizon. This could be detrimental to the long-term interests of current and future consumers. We expect that Ofgem will mitigate this potential limitation through the yearly challenge process, scrutinising networks long-term strategic direction and the actions they take within year to secure value for consumers beyond a short-term horizon.

Finance

The Sector Specific Methodology outlines a working assumption of the cost of equity for the companies of 4%. We do not offer comment if this is the right level, though note it is lower than some other regulated industries. We do agree that the Networks need to be appropriately financed and that decisions and changes made now will shape the future cost for consumers. With greater decentralisation, more intermittent power generation and potentially greater demand, the electricity transmission network owner should explore non-build commercial solutions that offer flexibility and value-for-money over several years. Equally for gas networks, demand patterns are generally reducing whilst requirements for flexibility are higher than historical levels. We would be concerned if the financial settlement lead to a narrower definition of acceptable solutions by the networks to meet these challenges. For instance, companies may decide a safer

Drax Group plc.

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outcome for their long-term income is to build infrastructure rather than seek commercial solutions and options for managing change on the networks. It would be an undesirable outcome if the companies were overly risk averse because of the financial settlement.

Whole system

We welcome the clarification of whole system within the context of the price control and agree that currently the narrow focus is appropriate, highlighting the coordination of investment planning and operational delivery across the Electricity and Gas networks. To accompany this, a greater degree of transparency by the networks and system operators with respect to longer term operational and network needs could help to stimulate markets for systems support services.

Complexity and reopeners

Drax supports the introduction of the challenge process and believes this, along with greater market participant engagement by the networks, could lead to greater understanding and develop a more strategic outlook in Network investment and operation. We support appropriate scrutiny within the course of the RII02 period and note that this needs to be proportionate and not lead to unwieldy administrative arrangements.

Electricity System Operator

We note that some parties have identified the proposed ESO Business Planning cycle process as effectively a full two-year price control mechanism. We do not agree with that characterisation though can see the risk that it could be perceived as such if overly complex measures or processes are put in place to support it. On balance we feel the arrangements are proportionate given the ESO is a new entity having legally separated from National Grid but still part of the parent group. As such we believe the process outlined will be a sensible checkpoint to ensure that milestones are met, delivery is on track and the longer-term strategic direction is in place. As highlighted in the consultation there is a clear expectation that the planning cycle should not lead to shorter term thinking by the ESO. Currently the focus is very short term and we would like to see more emphasis beyond five years in the ESO's strategic thinking and plans and encourage Ofgem to consider how it can further enable this within the arrangements.

Innovation

We agree with the decision to more clearly focus innovation funding on supporting the Energy System Transition and replacing the Network Innovation Competition. We believe this clearer strategic focus on the role of funding to promote truly innovative thinking by the companies could bring significant benefits to current and future consumers. We agree with the premise that lower risk innovation such as maintenance and operational changes should be part of BAU activities and that this should be reflected in companies base case revenues.

We trust that you find our views useful. If you have any questions, please don't hesitate to get in touch.

Yours sincerely,

Paul Youngman
Regulation Manager