

RIIO-ED2 Cost Assessment Working Group (CAWG) – 14th May 2020

From: Ofgem

Date: 14th May

Time: 10am to 1pm

Location:
Teleconference

Present

Ofgem
UK Power Networks (UKPN)
Western Power Distribution (WPD)
Northern Powergrid (NPG)
Scottish Power Energy Networks (SPEN)
Electricity North West (ENWL)
Scottish and Southern Energy Networks (SSEN)
Centrica

1. Ofgem presentation on early ED2 forecasts

- 1.1. Ofgem had previously asked network companies to provide early sight of the challenges for ED2 by sharing early forecasts. Ofgem presented slides on the benefits of submitting these early forecasts, stressing that these submissions are not intended to confine DNOs' business plan submissions.
- 1.2. Ofgem added that having early sight of forecasts would aid the development of BPDs, EJP templates and CBA templates, giving an opportunity to spot problems early if they arise. Understanding forecasting assumptions will also be helpful, to ensure that a consistent methodology is applied across DNOs. It could also be helpful to run early cost models. Ofgem also noted that a key benefit of getting early forecasts would be to understanding the scope and materiality of change between ED1 into ED2.
- 1.3. The proposed forecast period would cover the remainder of ED1 and the full ED2 period, and the proposal at present would be to receive submissions from DNOs September 2020. Ofgem stated that the forecasts would not need to include greater granularity than the existing RIGs C1 tables.
- 1.4. DNOs argued that a September submission would be challenging to develop a common approach to forecasting, nor for Ofgem to issue guidance. Ofgem replied that receiving different approaches would be helpful at this stage, that work would help form a better understanding of forecasting assumptions ahead of the business plan submissions.
- 1.5. DNOs questioned whether submitting cost forecasts in a M16 table format would be the most effective way to deliver the benefits of providing early forecast, and asked whether alternative ways could be found. ENWL noted that giving an early view based on scenarios currently being developed could be quite clunky, and that a discrete piece of work could be more appropriate.

- 1.6. Ofgem noted the robust challenge from the DNOs on this proposal, but reiterated the view that this to benefit the process and that Ofgem would continue the discussion with Regulatory Manager.

2. SSEN presentation on early ED2 forecasts

- 2.1. SSEN presented their slides on ED2 forecasts and stated that a similar exercise had been carried out in RIIO-ET2. SPEN noted that each company submitted a range of forecasts to Ofgem and that this would require DNOs to have a common approach – however, this would be difficult to achieve within the current timelines.
- 2.2. Several DNOs noted that CI and CML targets were not known and that this a significant driver for expenditure in the next price control. Therefore, providing views on related costs and volumes would be difficult. SSEN noted that the RIIO-ET2 price control is different to RIIO-ED2 as transmission projects span across multiple price controls.
- 2.3. Ofgem stated that it was hoping to make the process useful for all stakeholders and to ensure transparency. UKPN queried what the rationale was for an absolute number, and suggested that a 'low' and 'high' range could still provide views on uncertainty. UKPN argued that a single number might draw focus on the wrong places and risks leading to misleading results.
- 2.4. UKPN suggested that realistic timelines are required and practicalities need to be considered. UKPN raised that Ofgem should indicate if there is anything that is not required as part of the exercise.
- 2.5. **Action: Ofgem to set out draft timelines for development of this proposal and provide a draft template for discussion**

3. Incremental costs

- 3.1. Ofgem ran through slides on incremental costs. Ofgem defined incremental costs as any costs sitting above the core costs relating to the primary driver. Ofgem asked for views on how these costs should be treated for ED2.
- 3.2. ENWL agreed with the summary. They stated that there had often been a debate about the comparability of unit costs and that it was unclear how losses should be treated. This is being played out in climate change adaptation, where companies are taking incremental positions to cut trees back or to install taller poles. Companies are adopting an additional scheme of work to normal activities that is not captured. Unless these cases are identified and flagged, these costs, which are potentially making activities more efficient in the long term, are not incentivised. There is a question of whether this is a more material issue for ED2, and will feed into BPDT design. There is a risk that there is a CBA that justifies many incremental costs, but this is ignored in the cost assessment process.
- 3.3. NPG stated that the totex mechanism creates an incentive for DNOs to incur incremental costs, even if the benefits are realised in the next price control period. There was a discussion on how incremental costs could be treated in disaggregated models, which DNOs agreed, was of more of a challenge.

- 3.4. Ofgem made the point that if all DNOs are doing a similar thing in one area, e.g. upsizing cables through replacement, and if all DNOs upsize cables and include the incremental cost within their unit cost, then there is no issue of inconsistency. ENWL stated that it is an issue if DNOs come to different conclusions on which incremental costs to include.
- 3.5. It was suggested that DNOs identify areas of the cost base that will have significant incremental costs e.g. areas most relevant to losses activity. NPG suggested that identifying where the incremental cost becomes an issue could be something that is included in the Ofgem guidance for early forecasts. WPD stated that the forecast submissions would need some commentary to explain these costs.
- 3.6. **Action: DNOs to provide feedback on the two questions on slide 17, and on options to treat these costs by 29th May.**

4. Actions, Next Steps, AOB

- 4.1. Ofgem and DNOs discussed pushing back the next CAWG meeting, originally set for 26th May. As the next CAWG meeting will aim to give an overview of the SSMC, pushing back the meeting will allow for a better discussion. Ofgem mentioned that EJPs would also be covered then.
- 4.2. SSEN asked whether the decision on early forecast scenarios would be included in the next CAWG as well. Ofgem replied that clarity would be given after further discussion with Regulatory Managers, due to happen next week.
- 4.3. **Action: Ofgem to provide stakeholders with a new date for the next CAWG.**