

Interested parties and
stakeholders

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Date: 17 December 2015

Non Gas Fuel Poor Network Extension Scheme modification direction

We are making changes to the Gas Distribution Networks (GDNs) transporter licences to introduce the Non Gas Fuel Poor Network Extension Scheme (the Scheme) incentive mechanism. The incentive mechanism sets out the fuel poor connection targets the GDNs should deliver during the RIIO-GD1 price control period¹ and encourages them to exceed those connection targets by providing a financial incentive to connect additional eligible fuel poor households.

We published a statutory consultation setting out these changes on 30 October 2015. The responses we received to the statutory consultation are summarised below. We also explain several minor changes to the licence text which accompanied the statutory consultation made in response to comments received from the consultation.

The changes implemented by the modification direction will be incorporated into the GDN's transporter licences on 12 February 2016. This means the Scheme incentive mechanism will apply to the GDNs from 1 April 2016.

Background

The Scheme enables low income vulnerable households to switch to natural gas by helping to fund the cost of connecting to the gas network, where a connection to gas main is the best solution for them. It does so by providing a discount to eligible households against the cost of the gas network connection.

We recently concluded a review of the Scheme which considered if it was aligned with wider Government strategies on heating and fuel poverty, and whether there were any changes we could make to maximise its benefits.²

We made a number of changes to the Scheme based on feedback we received to the review. One of these changes was to establish an incentive mechanism which encourages GDNs to connect additional eligible households over and above those included in the fuel poor connection targets.

¹ RIIO-GD1 is the current price control period (2013-2021). RIIO stands for Revenue = Incentives and Innovation and Outputs.

² A copy of our final decision letter can be found here: <https://www.ofgem.gov.uk/publications-and-updates/fuel-poor-network-extension-scheme-final-decision-document>

The Scheme incentive mechanism

To encourage the GDNs to complete a higher number of connections than were originally approved in their price control targets, we will implement the Scheme incentive mechanism. The modification direction and licence text which accompany this covering letter sets out in full the changes we will make to introduce the Scheme incentive mechanism.

In summary, the GDNs will be required to report on their performance on delivering fuel poor connections. We will then assess if the GDNs have over or under delivered against their fuel poor connections targets using the principles established for the RIIO-GD1 price control period.

The GDNs will either be rewarded or penalised depending on any over or underperformance in delivering fuel poor connections against their connection targets. The GDNs will receive an additional 2.5 per cent reward or penalty of the assessed efficient costs related to the over or under delivery.

The over or under delivery will be offset against any output commitment agreed as part of the next price control period. If the Scheme does not continue beyond RIIO-GD1, we will make the appropriate legacy adjustment at the beginning of the next price control period.

The statutory consultation

Between the 30 October 2015 and 30 November 2015, we consulted on making these changes to the GDNs gas transporter licences. We received three responses to the statutory consultation all from GDN companies.³

The consultation respondents indicated that they were broadly content with the licence changes which would introduce the Scheme incentive mechanism. However, they also suggested a number of changes to the licence text. We explain our views on these suggested changes below.

Two of the consultation respondents, NGGD and NGN, identified incorrect cross referencing within the licence text. This occurred in paragraphs 4J.5 and 4J.7 which included cross references to paragraphs numbered "4I". The cross references should have been numbered "4J". We have corrected this mistake in the licence text included in the modification direction.

NGGD and NGN also suggested other minor text changes to several paragraphs in the licence text. In particular:

- the words "or output commitment" should be inserted into paragraph 4J.4 after the word "allowed revenue"
- minor changes are made to paragraph 4J.5 to improve its readability
- the words "In relation to the Licensee's" are removed from the beginning of paragraph 4J.6
- changes to paragraph 4J.6 are introduced so that the wording for "scheme connection targets" matches that used in Annex A of the licence condition.

We consider these are minor changes to the licence text which are limited to improving its readability. We have therefore incorporated them into the licence text.

SGN considered that the final date to submit the performance report (31 Jul 2021) is not consistent with the start of the next price control period on 1 April 2021. They suggest the date for submitting the performance report should be brought forward to precede the start of the next price control period.

³ The consultation responses are available on our website: <https://www.ofgem.gov.uk/publications-and-updates/fuel-poor-network-extension-scheme-incentive-mechanism-statutory-consultation>

In our view, no adjustments are needed to the performance report submission date. We will use the performance report to assess the Licensees delivery of fuel poor connections and if any adjustments are necessary to the output commitments in the next price control period to take account of under or over delivery of those connection targets. These adjustments will be made as legacy adjustments to the Licensees revenue and output commitments after the next price control period begin. We anticipate this will be undertaken in line with the process used for RIIO-GD1 where legacy adjustments were made in subsequent annual iteration processes.

NGGD requested we should better explain the intent and meaning of paragraph 4J.6. In particular what:

- “in accordance with the RIIO principles” means
- “detailed explanations” consists of in relation to the performance report.

“RIIO principles” is defined in Special Condition 1A of each GDNs gas transporter licence⁴ as “...the principles for the assessment of business plans set out in the document entitled “Decision on strategy for the next gas distribution price control” (Ref 47/11) published on 31 March 2011;”. We consider this definition is sufficient to explain what the term means and further explanatory text is not required in Special Condition 4J.

The words “detailed explanations” are used in their ordinary and normal meaning. They carry no significance beyond indicating that the Licensee should provide us with enough information to form a view on their performance in delivering fuel poor connections. It is incumbent on the Licensee to provide this information to us and justify fully the fuel poor connections they have made. We consider that no additional text is required to define or explain these words.

NGGD also stated that Special Condition 4J does not set out how the Scheme’s incentive mechanism will facilitate the connection of district heating (DH) or Independent Gas Transporter (IGT) connections.

The Scheme’s incentive mechanism does not apply to DH or IGT connections facilitated by the GDNs. The revised targets we put in place for RIIO-GD1 only apply to domestic one-off and community gas connections. This is explained in the decision letter we published in October 2015.⁵ As a result, it will only be single one-off or community gas connections that will count towards the incentive mechanism.

NGN suggested a number of changes to Table 1 which sets out the treatment of under or over delivery of connection targets. These changes included rewording the text in the justified over delivery box to state that if the Scheme continues to the next price control period, any over delivery shall be removed from the relevant output commitment although revenues accruing to the GDN would still be set on the pre-removal commitment.

We have decided not to make this change as it would limit our flexibility to adjust either the Licensee’s future totex amount or output commitments to take account of a justified over delivery of connection targets. We will retain the text we consulted on in the statutory consultation.

NGN suggested text in the justified under delivery box should be amended so that the connection targets shortfall would not be added to the relevant output commitment in the next price control period.

We have decided not to make this change. If the Scheme continues in the next price control period, then any under delivery of the connection targets will be added to the

⁴ Special Condition 1A. Restriction of revenue in respect of the Distribution Network Transportation Activity: definitions

⁵ A link to this document can be found in the footnote above

relevant output commitment. This will make sure that those connections are delivered by the GDN and the amount of fuel poor households who benefit from the Scheme is maximised.

If the Scheme does not continue into the next price control period, we will make a legacy adjustment to take account of the shortfall in fuel poor connections.

NGN also proposed the text in the unjustified under delivery box is amended so that if the Scheme continues in the next price control period, revenues accruing to the GDN would not take into account the addition of under-delivered fuel poor connections from RIIO-GD1. They also proposed text which stated a legacy adjustment will be if the Scheme does not continue into the next price control period.

We have decided not to make these changes. We consider changes to specify what basis the GDN's revenues are set is unnecessary. We also consider the other proposed changes would limit our ability to make legacy adjustments or amend output commitments depending on whether the Scheme continues in the next price control period.

Gas connection definitions

The covering letter that accompanied the statutory consultation set out definitions for Domestic One-off and Community gas connections. These were:

- Domestic One-off connection: A service pipe connection from an existing main to a single household
- Community Connection: A connection to a number of households requiring new mains pipe and service pipes to each individual household.

We explained the definitions would be inserted in the Regulatory Instructions and Guidance (RIGs) document.

NGGD were the only respondent to comment on the definitions. They expressed some concern that the RIGs may not be the most appropriate place for the definitions. However, they said if we do place the definitions in the RIGs we should make sure any future changes are managed appropriately.

We will modify the RIGs to include the definitions set out above. Any future changes to the definitions will be considered with any further modification of the RIGs.

Licence change process

The modification direction published alongside this letter fully explains the licence changes that will be made to the GDN's gas transporter licences. It also includes the wording of the relevant licence text which will be added to each licence. These changes will come into effect on 12 February 2016.

If you have any questions about this decision, please contact James Thomson on james.thomson@ofgem.gov.uk.

Yours sincerely

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