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Dear Geoff

### **Consultation on the mid-period review (MPR) of RIIO-T1**

This response is on behalf of National Grid Electricity Transmission plc. (NGET) and is not confidential. We are responding only to the Electricity Transmission issues contained within the consultation.

NGET welcomes the opportunity to respond to Ofgem's proposals for changes to the RIIO-T1 outputs and allowances via the mid-period review (MPR) uncertainty mechanism. We recognised this uncertainty mechanism and accepted it as part of Final Proposals for RIIO-T1.

Overall we agree with Ofgem that the regulatory certainty provided by the longer term 8-year RIIO-T1 framework benefits consumers as it encourages longer term planning, innovation and efficiency. As such the conclusion of the MPR for RIIO-T1 will be helpful as it gives us regulatory certainty for the remaining T1 period. On the specifics of the consultation we accept Ofgem's minded to position on the enhanced role of the SO issues, but we disagree with Ofgem's minded to position in relation to non-variant allowances as Ofgem is proposing inconsistent treatment across two output categories within this part of the RIIO framework. We do not believe is appropriate or has been justified.

#### Enhanced SO Role

We welcome Ofgem's support for additional allowances to fund the costs that our System Operator function has faced in delivering new outputs in relation to its enhanced role under ITPR. We also welcome Ofgem's support for additional allowances to fund the internal costs incurred for setting up and administering the new balancing services products SBR and DSBR. We would also like to highlight that, although a decision has been made to not contract DSBR for winter 2016/17, these allowances will fund the internal costs incurred in the successful delivery of two years of DSBR and the administration of tendering, testing and assessment of DSBR for winter 2016/17.

We appreciate Ofgem's comments regarding our efforts in relation to our Demand Side Response programme. Ofgem also proposes to require us to produce two short reports on the Demand Side Response Programme to describe the activities carried out over the relevant period, expenditure incurred and the benefits delivered by the programme to consumers. We accept this proposal, and as the costs of this programme are now largely sunk and Ofgem has set out its minded to position on

funding these costs we would welcome clarification that the focus of the report should be the activities and benefits delivered to consumers.

We note that Ofgem is minded to disallow some costs from our original funding submission, and although we believe our submission was justified, we accept Ofgem's minded to position on these issues.

#### Non-variant Allowances

Since the start of the T1 period significant and rapid changes in the generation background driven by our customers have occurred. We are currently forecasting 14GW of transmission connected generation in the T1 period compared to 25GW we forecast at the start of RIIO-T1. At the same time there has been a rapid increase in embedded generation with 10.9GW connected (to 1 April 2016) and a total of 24GW forecast for the full T1 period (compared with 0.5GW forecast at the start of T1).

These changes have swung the associated challenges presented in managing the network from fault level issues driven by large scale transmission connected generation to voltage management issues associated with embedded generation technologies. This has reduced the requirement for fault level reinforcements from nine to one site (reducing forecast expenditure to £38.9m below the allowance agreed at Final Proposals) and increased the requirement for Shunt Reactor investments from 11 to 25 (plus provision for further sites) currently forecast to be £89.1m above the allowance agreed at Final Proposals. This gives a net position of £50.2m costs above allowances. Given this level of expenditure above allowance and the totex incentive in place, Ofgem should be in no doubt that we are sufficiently incentivised to explore and use the most economic solutions to meet the need in the relevant timescales.

These nominal allowances are part of the non-variant 'pot' of allowances which are by definition fixed (i.e. not subject to an uncertainty mechanism) and therefore we accepted the risk associated with managing these requirements with a fixed allowance as part of Final Proposals. We did not use the MPR re-opener to attempt to make a case for increasing allowances associated with changed requirements as we accepted the opportunities and risks of managing these issues with fixed allowance as part of accepting the price control in the round.

Ofgem's minded to position appears to look at each output in isolation, to remove allowances for reduced fault level requirements but not acknowledge the corresponding increased costs of managing reactive requirements which stem from the same driver i.e. the changing generation background and are in the same subcategory of 'Wider Works General'. We do not agree with Ofgem's minded to position to treat these two non-variant outputs and allowances differently. Against the background set out above we do not believe Ofgem has justified why different treatment is appropriate. Its current position is asymmetric and inconsistent with one of the stated aims of the MPR which in para 1.3 of the consultation makes it clear that "any changes would be symmetric i.e. outputs and allowances could go up or down in response to changes in need."

In its considerations of these issues, there are two broader points that Ofgem has highlighted which we believe are important points of principle going forward, and with which we agree:

1. Ofgem argues that potential distortions that can result from defining specific investment solutions as 'outputs' (paras 3.24 and 3.25) where a broader range of tools may be available. We agree that NGET should be incentivised to innovate to find the lowest cost solutions which address customers' needs. Defining 'outputs' as specific solutions, or number of asset

or site interventions is not consistent with this, rather the focus should be on defining the desired outcome to be achieved for consumers. We believe this is an important principle for RIIO-T2.

2. Ofgem also argues that voltage management is NGETs issue to manage and that we have alternative sources of funding to draw upon to achieve that (paras 3.26 and 3.27) including interestingly from the broader non-variant pot. We agree that in accepting the RIIO-T1 control we accepted certain obligations, responsibilities, opportunities and risks along with the various funding mechanisms together in the round. We welcome Ofgem's acknowledgement of this and, upon conclusion of the MPR consultation and Ofgem's final decision, we welcome the certainty of our output requirements and funding mechanisms until the end of the T1 period.

The result of applying these principles back to the non-variant output issue would be to de-classify both the fault level and shunt reactor interventions as specified 'outputs' from the RIIO-T1 framework and leave the funding arrangements unchanged. The outcome being that NGET has the responsibility to manage both fault levels and voltage issues on behalf of consumers, using the funding agreed in final proposals, and consumers will share cost, risks, or benefits of achieving this through the totex sharing factors and potentially SO incentive arrangements.

We hope you find this response constructive and would ask that you reconsider your minded to position in light of our response. If you wish to discuss any of the points in more detail, then please contact Andy Balkwill (01926 655988) or Mark Brackley (01926 656024).

Yours sincerely

*[by e-mail]*

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