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Dear Geoff

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

This response is submitted by National Grid Gas Transmission (NGGT). We operate and own the gas transmission assets in Great Britain. Our response only covers the Mid Period Review (MPR) of the Avonmouth pipelines.

Overall we disagree with Ofgem's minded to position on Avonmouth pipelines and believe it sends the wrong message to network companies regarding ex-ante incentivisation and the promotion of innovation which are cornerstones of the RIIO regulatory framework.

To set our response into context, the Avonmouth output and associated solutions were triggered by a letter from National Grid Gas LNG Storage in June 2011, stating that they no longer might be able to provide reliable services and potentially no service at all, beyond the end of their price control period (May 2013). In response to this and against a background of the viable solutions at the time, we included two pipelines within our RIIO-T1 business plan in July 2011, and stated "It should be noted that this is our current view and, given the fact that the requirement for this analysis was only triggered in June following the letter from NGG LNGS, we are continuing to assess the issue". Following an assessment of the information contained within our Business Plan, and supplementary information, Ofgem established a baseline allowance, based on the viable pipeline solutions, in RIIO-T1 Final Proposals. They also established the totex incentive mechanism which shares the risks and benefits of any cost increases or reductions from that baseline between NGGT and consumers.

As we progressed our assessment, we continued to seek the best solution for consumers to manage the loss of services from the Avonmouth LNG facility. The Avonmouth LNG facility provides two services, the first is support for peak gas demand in the South West and the second to assist in the orderly run down of the system following a local physical problem on the network, such as a pipeline failure. With regard to the first service, due to falling demand in the South West we evaluated that at this time investment in a pipeline solution is not justified, although this requires us to continue to manage the capacity risk. In terms of the second service, we undertook detailed analysis of the situations that Avonmouth can currently support and engaged with the Health and Safety Executive (HSE) and Wales and West Utilities

to fully understand the implications of not providing this protection. We employed an external consultant to consider the societal risk of the available options, applying the As Low As Reasonably Practicable (ALARP) methodology. Based on the analysis and evidence generated, we were able to demonstrate, that not building the pipeline represented ALARP. This decision was not opposed by the HSE.

Ofgem have not disputed either decision. We have managed this issue in the context of responding to the totex incentive that was established as a key part of the new RIIO framework and have acted in the best interests of consumers in the decisions we have taken. The financial benefit of not undertaking the pipeline build will currently flow through to customers and NGGT through the totex incentive mechanism and we believe it is appropriate and consistent with the principles of RIIO for National Grid to share in some of the benefit we have delivered. However, we also recognise that the Avonmouth output was recognised from the outset as a special situation, and therefore was included as a topic for the MPR.

Ofgem's minded to position removes the Avonmouth output and associated allowance, minus directly attributable costs incurred thereby removing all of NGGT's share of the benefits delivered. We strongly disagree with this position as it is inconsistent with the RIIO principles of incentivisation and benefits sharing and sends a message to all network companies which we do not believe is in the long term interests of consumers. Whilst we disagree with Ofgem's minded to position, we should highlight that for it to be self-consistent, it would need to leave NGGT with the same risk profile in respect of the South West that we accepted as part of Final Proposals. Therefore the incentive scheme termed Transmission Support Services (TSS) scheme that we accepted in Final Proposals, and which falls away based on the then expected completion of the Avonmouth pipeline solution on 30 September 2018, would need to be extended to the end of the RIIO-T1 price control.

Although we disagree with Ofgem's current minded to position, we can understand that there may be views that the total benefit due to accrue to NGGT through the totex incentive mechanism is too high. However, we do not think that accruing zero benefit can be considered appropriate either. Recognising the specific circumstances in this case, a position that allows NGGT to retain its share of the benefits accrued through the totex mechanism to this point, and then stopping the further accrual of its share of the benefits going forward would be consistent with a forward looking re-opener and address the concerns in relation to undermining incentivisation under RIIO.

This case also highlights the wider concern of defining outputs as specific asset solutions and then assessing whether a company has met an output solely based on the delivery of the specified asset solution. In the case of Avonmouth, we have delivered the genuine consumer outcome of managing the loss of services from Avonmouth LNG facility. We believe that this is a significant issue that should be addressed through Ofgem's parallel work as we believe that Ofgem's current approach has the potential to create distorted incentives that are not consumers' long term interests, and undermines the RIIO principles of promoting innovation.

We hope you find this response constructive and would ask that you re-consider your minded to position in light of this response. If you would like to discuss any of the above please do not hesitate to contact Martin Watson.

Yours sincerely

[By e-mail]

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