



Citizens Advice
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Dear James,

I am responding on behalf of Citizens Advice to your consultation seeking views on the parallel work you have undertaken alongside the T1 mid-period review to finesse aspects of the RIIO framework. Detailed comments are offered below. In summary, we believe that:

- While variations to outputs should be governed by outcomes where appropriate, Ofgem should give further consideration to the perverse incentives post-hoc amendments to delivery mechanisms could create.
- National Grid Gas Distribution's offer to return £53.9m to consumers is welcome and appropriate, given the impossibility of delivery the output in GD1.
- The delay to the Western HVDC is concerning, and it is appropriate to delay revenue, review why this has occurred and consider further redress action if appropriate.
- The decision not to make adjustments to the NTS exit capacity incentive is not justified. Ofgem should adopt as a principle that they will adjust incentives that cost more than they save.

We also agree that SPT request for new assets to be added to their connections volume driver menu should be rejected, but have no specific comments to offer.

Accountability for output delivery

It is welcome that Ofgem is returning to consider an ambiguity under RIIO as to what constitutes output delivery. In principle, we see a strong case for

Patron HRH The Princess Royal

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clarifying this in favour of defining output delivery in terms of the purpose and outcome intended, rather than in terms of the particular specification envisaged being delivered. This encourages innovation and incentivises energy networks to seek more efficient outcomes.

We also welcome Ofgem considering this on a case-by-case basis for outputs, rather than proposing a wholesale transformation of RIIO to an outcome-focussed approach to output delivery. Given the potential for unforeseen consequences, a more modest approach is appropriate. For the two specific outputs under consideration, National Grid Gas Transmission's compressors output to comply with the Industrial Emissions Directive and SP Transmission's voltage control, we do not identify any objections to pursuing an outcome based approach.

Dangers of perverse incentives as a consequence of amending output delivery

While we do welcome Ofgem's approach in principle, the consultation document does not consider the potential for such adjustments to disrupt energy networks' incentives in the long-run.

NGGT's output expenditure for compressors and SP Transmission's output expenditure for voltage control will have been set on the presumption that a particular delivery method would be employed. They have now identified cheaper ways of delivering this and will be enjoying the financial benefits available as a consequence of the totex incentive mechanism. You estimate the total saving at £29.6m.

Our concern is that, in future price controls, this will encourage energy networks' to identify particular, more costly delivery methods for outputs in their business plans. They will do this in the expectation they will be able to convince Ofgem in the future to amend the output to be outcome focussed, which they can deliver at a lower cost with an alternative delivery method.

We think there are two ways to ameliorate this concern. First, given this problem has occurred as a consequence of ambiguity in RIIO-1's design, Ofgem should be clear about how it intends to resolve this ambiguity in

RIIO-2. Second, for these outputs only, Ofgem should appropriately reduce the percentage of revenue networks retain as part of the sharing mechanism, to reflect that network companies are enjoying this higher benefit as a consequence of unforeseen ambiguity in the RIIO framework.

Price control adjustments

We welcome National Grid Gas Distribution's offer to return £53.9m funding for the replacement of medium pressure pipes to consumers, given this output is subject to unforeseen delays outside of NGGD's control.

We also agree that it is appropriate the Western HVDC revenue be delayed, as network companies should not receive a timing benefit as a consequence of late delivery.

However, it is unfortunate that the output itself will be delayed, given the increased constraint costs to consumers of this delay will be £70m due to technical difficulties with the construction of the cable. Of the options you set out in paragraph 3.29, therefore, we believe it is appropriate that any benefits NGET and SPT receive as a consequence of this delay (such as payments from their suppliers for failed delivery) should be passed directly to consumers. This should provide some amelioration of the increased constraint costs to consumers. Ofgem should fully review the reasons for this delay and if they are not adequately explained, give consideration to enforcement action and redress payments.

NTS exit capacity incentive

We share British Gas' concern regarding the NTS exit capacity incentive. While it is good that distribution companies are being discouraged from using the most expensive exit points, it is important to consider what price tag this is coming at.

We note your analysis suggesting that the incentive scheme has cost consumers £15m more in the short term than in the absence of the scheme, compared to baseline expectations in their licences. As you accept, due to actual demand growth being lower than forecast, these baseline

expectations may already have been too high. It is unclear what long-term benefits Ofgem have identified that compensate for this consumer shortfall.

We therefore disagree with Ofgem's proposed position to make no changes to the NTS exit capacity incentive. Incentives that are costing more than the savings they are delivering cannot be justified. If Ofgem adopted the principle of adjusting incentive schemes that were costing more than they were saving, it need not lead to uncertainty - as most incentive schemes tend not to cost more than the value they produce in such a readily quantifiable way. Reasonable investors should accept this principle.

Please do not hesitate to contact me should you have any questions about this response.

Yours sincerely,

Morgan Wild

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Citizens Advice