



# RIIO-ED1 mid-period review: call for evidence

*Northern Powergrid's response to Ofgem's open letter dated 19 July 2017*

## KEY POINTS

**Ofgem set a deliberately tight scope for the mid-period review, and we are not aware of any items that meet the requirements for Northern Powergrid.**

- This tight scope was necessary in order to prevent the eight year price control period breaking down into two four year price control periods...
- ... and to give companies the strongest possible incentives for companies to innovate in order to contain costs as patterns of network usage change.
- Ofgem's scope limits the mid-period review of outputs to:
  - changes to outputs that are justified by clear changes in government policy; and
  - new outputs required to meet the needs of network users.
- Although several changes to government policy have caused our costs to be higher than they would otherwise be, these have not led to changes in required outputs.
- It also seems unlikely any new outputs would be identified, as the RIIO-ED1 outputs framework was developed over several price control reviews, and based on well over a decade of stakeholder engagement by Ofgem and companies like Northern Powergrid.
- Moreover, our ongoing stakeholder engagement has not identified any new stakeholder requirements that would satisfy an increase in costs.
- The biggest developments we can see to the electricity distributor role come from changing patterns of network usage, such as the need to move to increasingly active forms of network management, becoming distribution system operators (DSO)...
- ...but the RIIO framework was built to encourage this, through its emphasis on minimising the total costs of running the system, and therefore there is no pressing need for new outputs, which can wait until the DSO role has developed and the outputs are better defined.

## Responses to Ofgem's consultation questions

1. Ofgem's open letter asks two questions, which we answer in turn below.

**Question 1: We are seeking views from stakeholders on any issues that should be considered as part of a potential MPR.**

2. To answer this question, we have started from the scope of any RIIO-ED1 review set out in Ofgem's strategy decision.

*The scope of this review will be restricted to **material changes to outputs that can be justified by clear changes in government policy, and the introduction of new outputs that are needed to meet the needs of consumers and other network users.**<sup>1</sup> [emphasis added]*

3. As can be seen from this definition, the scope is intended to be tightly limited. As the emphasis shows, it is limited to two separate limbs of a test that, if met, could justify a mid-period review. These two limbs relate to different reasons, and one limb can only result in more limited adjustments than the other. We consider each in turn below.
4. As part of the first set of RIIO-1 reviews, we understand that Ofgem included in its *Final determinations* additional provisions that expanded the potential scope of the mid-period review. We are not aware of any similar provisions for electricity distribution.

***Material changes to outputs that can be justified by clear changes in government policy***

5. This limb of the test for a mid-period review allows for changes to existing outputs, or *potentially* the introduction of new outputs, provided that the change is:
  - a. sufficiently material; and
  - b. justified by a clear change in government policy.
6. We are not aware of any issues that meet both of these tests for Northern Powergrid.
7. We do however note that there have been several changes to government policy since the RIIO-ED1 *Final determinations* that have caused our costs of delivering our outputs to increase. For example, the government's policy on membership of the European Union has changed, causing the pound to weaken significantly and raising the cost of our imported materials (such as cable and transformers). An apprenticeship levy has also been announced, which when introduced would apply to large

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<sup>1</sup> Ofgem, 2012, Strategy decision for the RIIO-ED1 electricity distribution price control, Overview, Paragraph 8.16

business such as our own. Our comments are limited at this stage, but we will make additional representations later in the process should this become relevant.

***Introduction of new outputs that are needed to meet the requirements of network users***

8. This limb of the test is **limited to the introduction of new outputs**, where these are needed to meet the requirements of network users. It **is not** met by changes to the existing outputs.
9. The RIIO-ED1 price control has a well-developed framework for outputs, building as it did on the set of outputs already introduced at DPCR5 or previous price controls, and following extensive stakeholder engagement by Ofgem and the electricity distributors including Northern Powergrid over the course of more than a decade. It was always unlikely that new output requirements would be identified at this stage.
10. Moreover, if new outputs were to be introduced, this would lead us to incur higher costs than we would otherwise incur. These costs would need to be allowed for by Ofgem through the mid-period review process, and so they would raise charges to the generality of network users. This raises the bar for the introduction of new outputs, since their benefits would have to justify the costs.
11. Although we undertake significant stakeholder engagement on an ongoing basis, the feedback we receive is usually about existing outputs, rather than new outputs. And where a new output is suggested, it would not typically meet the threshold for imposing additional costs on the generality of customers.
12. There are however some candidates that, over the longer term could meet the relevant thresholds. One such candidate is need for electricity distributors to take on an increasingly active role as distribution system operators. However, this activity is already strongly incentivised under the RIIO-framework, which was designed to encourage total cost minimisation, including through active network management where possible. The role is also not yet clearly defined, so it is too early to specify new outputs. Another potential candidate is a future role for electricity distributors in ensuring car charging facilities are available when required, but again it is too early to introduce relevant outputs.
13. So, although these appear increasingly likely to be important areas in future, bearing in mind their early status, and the high threshold for a mid-period review of outputs, it is not clear to us that either should be taken forwards at an ED1 mid-period review.

***Question 2: We welcome feedback from stakeholders on our proposed timetable and process.***

14. Ofgem's proposed timetable and process appears sound.
15. We welcome in particular the proposed consultation on any potential issues for a mid-period review of outputs, which will allow any unjustified candidates to be ruled out promptly, as well as the proposed decision early in the process on whether or not to proceed.