

Delivering sustainable energy networks



Factsheet 100 31.03.11

www.ofgem.gov.uk

The gas and electricity sectors are responsible for more than half of Britain's carbon emissions, as well as local environmental impacts. As regulator of the gas and electricity sectors, we aim to be part of the solution and encourage energy companies to reduce energy sector pollution, whilst ensuring that investments are made in a way that delivers long term value for money for existing and future consumers.

Our key function is the regulation of the gas and electricity networks, and it is here that we can exert the greatest influence.

The new RIIO framework for energy network regulation is designed to focus the attention of energy companies on delivering sustainable outputs that provide benefits to the environment and to consumers.

Areas of focus include contributing to low carbon objectives, ensuring timely connections to renewable and low carbon energy sources, protecting visual amenity and improving customer satisfaction.

A central part of the new framework is ensuring that everyone's views are heard and taken into account by the companies when formulating their business plans

▶ RIIO = Innovation + Incentives + Outputs

RIIO strategy decision

Our strategy decision documents set out the way we intend to regulate the national gas and electricity transmission networks (RIIO-T1), and the local gas distribution networks (RIIO-GD1). The transmission and gas distribution price controls are the first to be conducted under the RIIO model. Please click [here](#) for the RIIO-T1 strategy decision document, and [here](#) for the RIIO-GD1 document.

Protecting the environment

Though most of the carbon emissions from gas and electricity come from generating electricity or burning gas, transmission and distribution networks have a vital role to play in reducing these emissions.

We are putting in place a set of arrangements to drive a step change in the contribution that transmission companies make to the UK's broader energy and environmental objectives at a national level. Networks will need to accommodate new generators, including wind farms often

located in remote areas, whilst protecting the visual amenity of the surrounding landscape.

At a local level, networks will need to respond to the demand for renewable electricity generation and energy production and changing consumption requirements, such as electric vehicles, renewable heat generation and biomethane production. Local networks will need to play a more active role in managing demand and supply, and take advantage of new opportunities to bring supply and demand into balance, made possible by, for example, the introduction of smart meters.

The arrangements will encourage energy companies to make investments in low loss networks to reduce the amount of electricity and gas that is lost in the journey from source to consumer. We will be looking for them to produce long term business plans that demonstrate how they will address the strategic issues in their sector, and handle the uncertainties relating to the future of the energy sector.

► RIIO = Innovation + Incentives + Outputs continued

Protecting the consumer

To deliver in excess of £30 billion of investment in electricity and gas networks over the next decade, consumers' bills will inevitably rise. However, our proposals are intended to enable companies to raise the finance they need for this investment, while containing cost increases and ensuring that consumers get the best possible value for money.

The package of measures we have announced provides companies with strong incentives to meet the challenges of delivering sustainable network services at long-term value for money to consumers. Our proposals will also reward or

penalise companies according to customer satisfaction with their services and will encourage them to play a role in addressing social issues – such as off grid fuel- poor customers and carbon monoxide poisoning.

Last year we conducted an impact assessment which compared the cost of our new RIIO approach to network regulation against the cost of our current RPI-X model. We estimated that our new approach will save consumers £1 billion over an eight year period compared with our previous regulatory regime.

► Key policy decisions

RIIO – T1

RIIO – GD1

Ensuring companies play their role in achieving UK environmental objectives

- Reputational incentive on promoting low carbon energy flows
- Subject to consultation an incentivised broad environmental measure for electricity transmission which may include:
 - An automatic financial reward for electricity transmission to facilitate a greater contribution to the UK's environmental objectives.
 - A discretionary reward for companies that deliver additional environmental outputs

- Reputational incentive on promoting low carbon energy flows
- Discretionary reward for companies that deliver additional outputs that contribute to environmental objectives
- For bio-methane plant, introduction of connection standards and provision of information to ensure timely connection

Ensuring companies minimise their own environmental impact, including carbon emissions

- A requirement for companies to report their business carbon footprint with reputational incentive
- A reputational incentive to reduce electricity losses. Transmission companies to outline investment solutions for fewer losses, gas shrinkage and gas venting in business plans
- Outputs for direct network emissions including business carbon footprint and sulphur hexafluoride (SF6) emissions
- A reliability output with network companies facing financial penalties of up to 3% of allowed revenue
- Guidance, and an allowance, for each company to reduce the visual impact of existing infrastructure in designated areas

- A requirement for companies to report their business carbon footprint with reputational incentive
- A shrinkage allowance mechanism to incentivise companies to minimise gas network losses
- An Environmental Emissions Incentive (EEI) to ensure companies consider the environmental value of carbon in minimising gas network losses
- Improving incentives for companies to engage in demand-side solutions to meet new capacity growth

RIIO – T1**RIIO – GD1****Ensuring companies are responsive to customers' needs**

- Financial incentives for companies' performance in survey of customer satisfaction, worth +/- 1% of revenue
- Discretionary reward to encourage companies to step up their engagement with stakeholders worth up to 0.5% of revenue
- Complaints metric, with a penalty up to 0.5% revenues (RIIO-GD1 only)

Contributing to other social objectives (RIIO-GD1 only)

- Continuation of the fuel-poor network extensions scheme and a regular review to ensure the fuel-poor continue to receive the most affordable heat solution
- Trials to determine the most appropriate role for local gas networks to address carbon monoxide poisoning
- Discretionary reward for companies that deliver additional outputs that contribute to social objectives

▶ Stakeholder engagement

The new RIIO framework requires the network companies to listen to and respond to the needs of their stakeholders, and we expect the companies to demonstrate how this engagement has informed the development of their business plans. Our policy work is also informed by stakeholder engagement.

Since July 2010 we have been developing policy through a number of working groups. These groups are attended by Ofgem, the network companies, users of the networks and environmental and consumer representatives.

We have also met with the Price Control Review Forum (PCRF) on a number of occasions to discuss and test our thoughts on RIIO policy. This is an advisory body made up of the network companies and representatives from all key stakeholder groups. The PCRF meets regularly to review policy development and discuss the various opinions and needs of all parties interested in the networks. For more information on how to get involved in the RIIO price controls please visit <http://www.ofgem.gov.uk/Networks/PriceControls/Pages/PriceControls.aspx>

In January we invited environmental interest groups, including green campaigners, trade associations and academics, to share their views on what sustainable network regulation could look like. A write-up of the meeting is available [here](#).

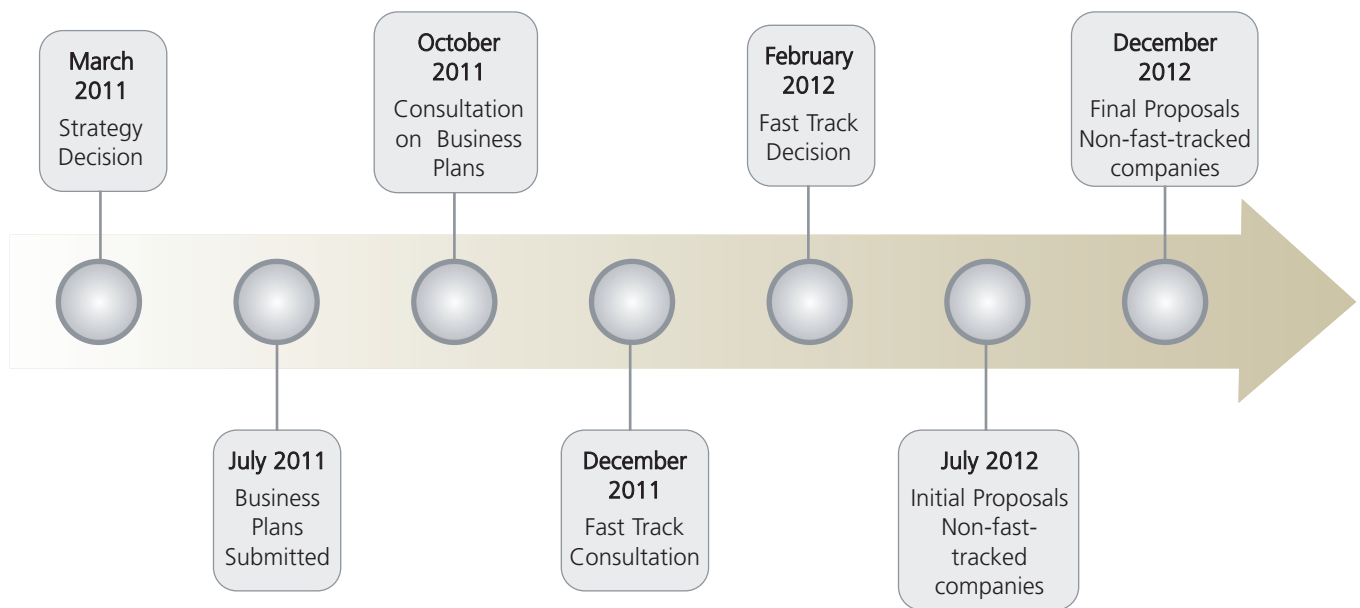
They agreed that the network companies had a central role to play in connecting renewable and low carbon generation, and told us that this should be at the heart of the environmental outputs we set, provided that the outputs are within the companies' control. They also saw a clear role for making the regulatory arrangement easier to understand for new entrants, and removing barriers where possible.

These discussions were very useful to us in developing our strategy decisions, and evidence from groups like this has formed part of our formal consultation process. Additionally, our Consumer Challenge Group of eight consumer experts has continued to provide consumer input into our policy development enabling Ofgem to get consumer input into some of the more complex issues.

► Next steps

Now that we have published our RIIO Strategy decisions it is up to the network companies to engage with their stakeholders and develop their business plans. These plans

will be submitted to Ofgem at the end of July when our detailed analysis will begin. An outline of the upcoming milestones for the RIIO-T1 and GD1 projects is set out below:



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