



# Stakeholder engagement in utility regulation

Experience from GB

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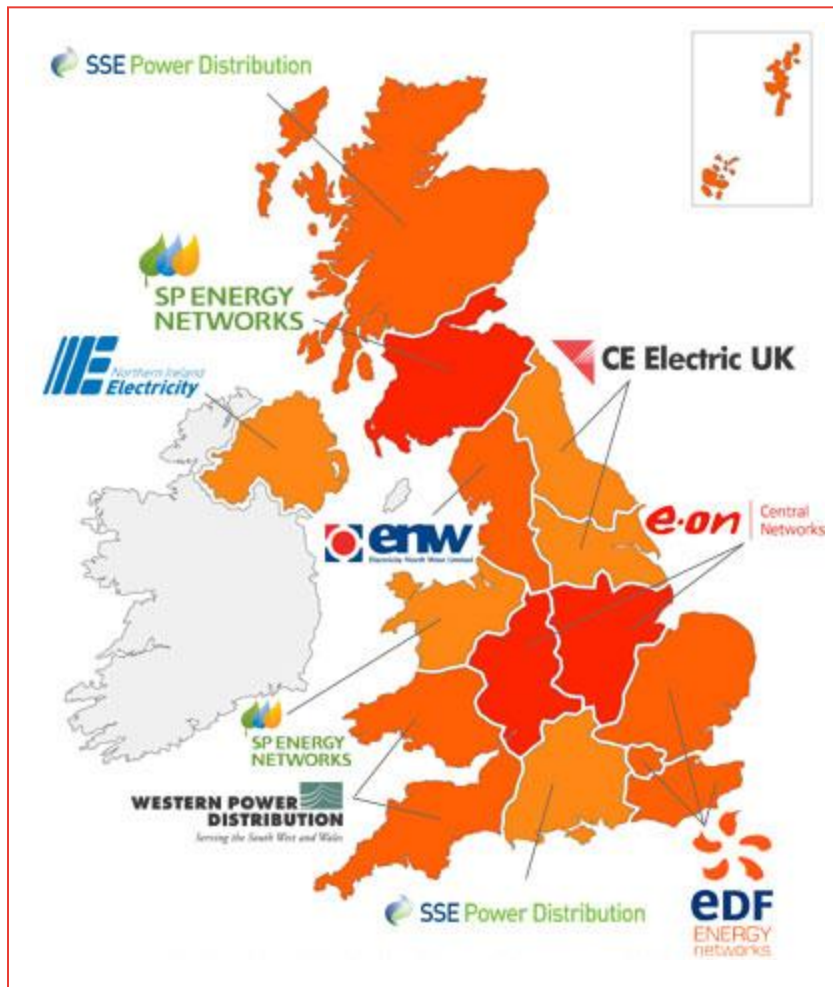
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# Overview of discussion today

- 1 Regulatory framework and incentives
- 2 Impact in practice
- 3 Evaluation – costs, benefits and risks

- Framework and incentives
- Impact in practice
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# GB electricity DNOs



## Key electricity network facts

- 14 DNOs, 2m customers and 55,000km of network on average.
  - Smallest network has 0.7m customers
- 7 DNO ownership groups
- 3 TNOs, and a single system operator for whole of GB (National Grid)

## History of GB network regulation

- RPI-X model of incentive regulation introduced at privatisation (mid 80s)
  - “High-powered” incentive regime (e.g. 40% of outperformance retained)
- Regulation has delivered strong efficiency benefits and lower bills.
- Increasing complexity over time:
  - RAV, WACC, benchmarking, market unbundling, quality targets, guaranteed standards.

# Primary objectives of RIIO model

RPI-X drove improvements

*“The RPI-X price control formula has a track record over two decades of delivering much lower network prices, better quality and service and substantial increases in investment by contrast to the nationalized industry days”* Alistair Buchanan, 2008

But Ofgem was concerned the model was not fit for purpose

## 1 The sustainability agenda:

- Uncertainty over what and how networks will have to deliver, but will probably need to deviate from ‘business as usual’.

## 2 Risk of cutting corners rather than costs under RPI-X

## 3 Changing role of networks in the system

- Idea that networks should move away from isolated “asset management” mindset, to more integrated, system-focussed and customer-focussed mindset.

Improved stakeholder engagement was seen as important to securing the outcomes Ofgem wanted in the RIIO model.

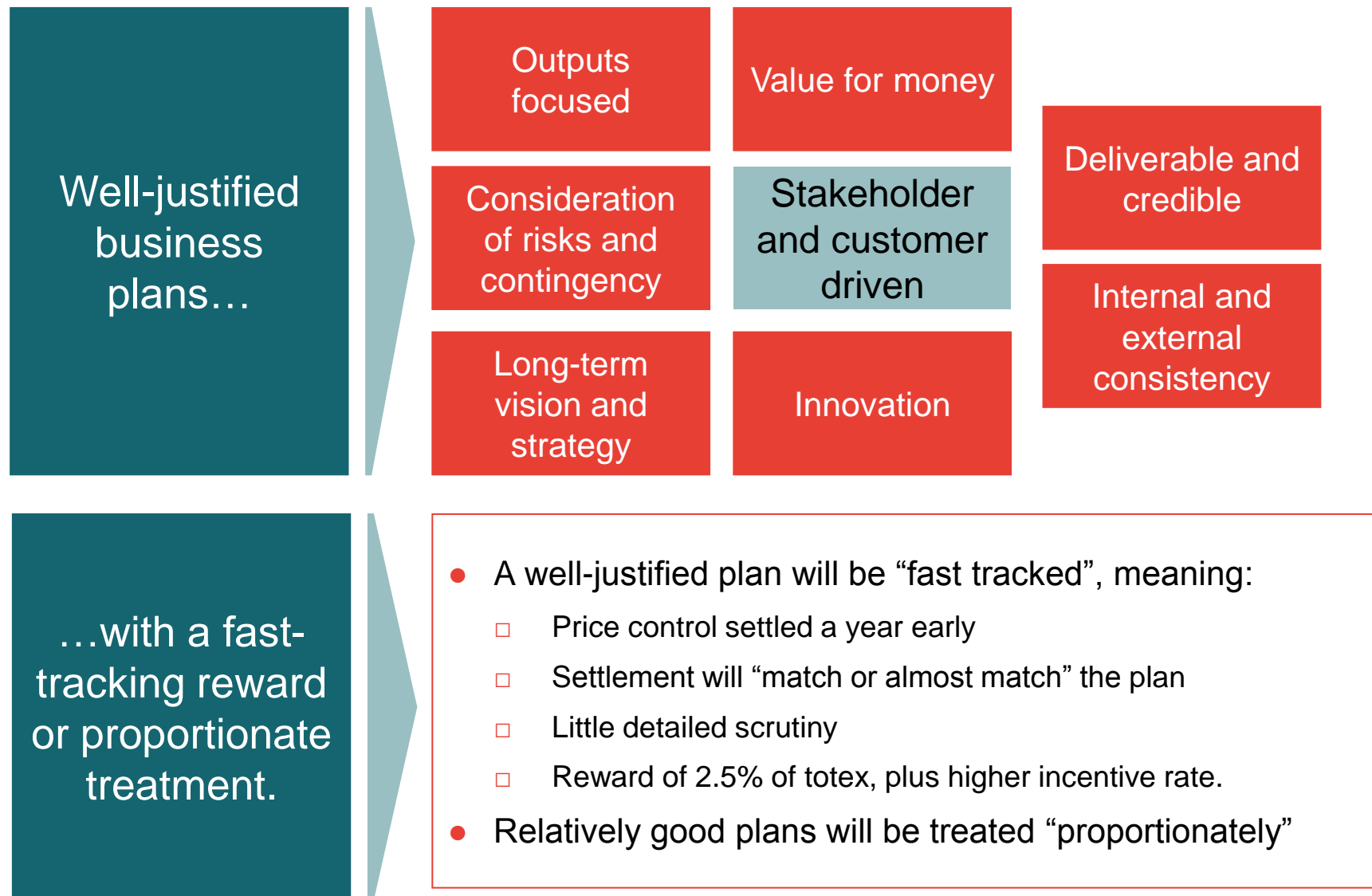
# Two sources of incentive for DNOs to improve stakeholder engagement



Business planning and  
price control review phase

Within the price control  
period – ongoing  
stakeholder engagement

# Business planning and price control review



# Within period – ongoing incentives





# Within period – ongoing incentives

## Some specifics

- Stakeholder engagement incentive within the “Broad Measure of Customer Satisfaction”
  - Annual requirement to demonstrate minimum level of stakeholder engagement activity.
  - Qualitative assessment of performance associated with discretionary reward of 0.5% of revenue.
- “Incentive on Connections Engagement”
  - Incentive targeted specifically at large customers.
  - DNO required to submit evidence of how they have “identified, engaged with, and responded to” customers
  - Penalty for failure to meet minimum requirements up to 0.9% of base revenue.
- Social objectives.
  - Vulnerable customer schemes with discretionary rewards.

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# What did the DNOs do in business planning?

Consumer  
challenge groups

Adverts, leaflets  
and website  
improvements

Stakeholder group  
workshops

Customer research  
surveys

Early publication of  
plans

Overall a substantial increase in the level of engagement activity –  
clearly the incentives had an effect!

# Ofgem's fast-tracking decision – Feb 2014

Review of plans – positive reflections on SE activity

*“The DNOs have clearly learned from the RIIO-T1 and GD1 price control reviews in transmission and gas distribution. All have engaged with stakeholders in developing their plans and reflect consideration of stakeholders’ views.”*

*“NPg submitted very well written plans which were praised by stakeholders for their clarity and readability. It is clear that stakeholder feedback has significantly informed the plan.”*

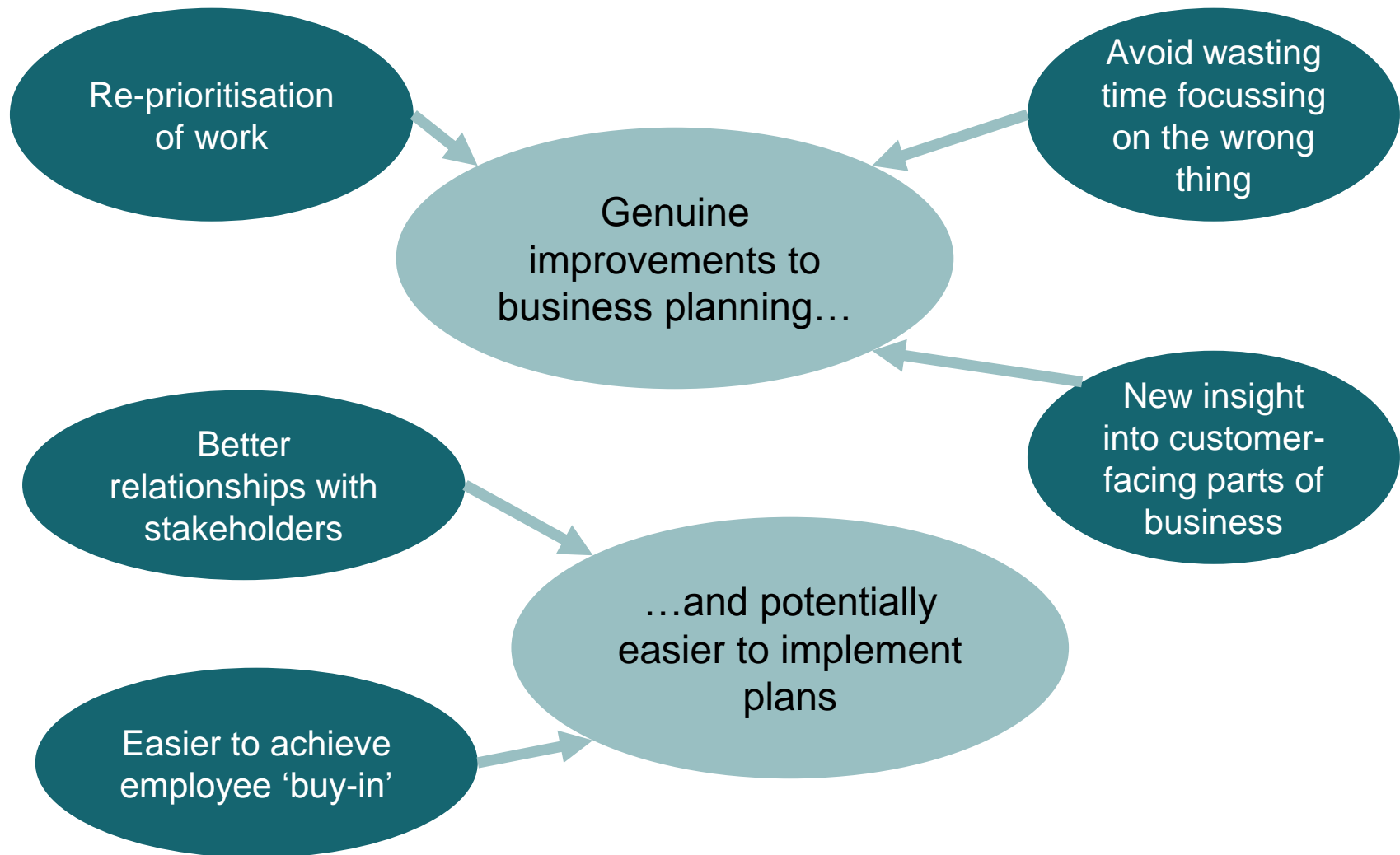
One DNO – WPD – was fast-tracked. WPD’s plan passed all Ofgem’s criteria.

**Table 1: Summary of assessment of DNOs’ business plans**

DNO Group	licensee <sup>10</sup>	Process	Outputs	Resources – efficient costs	Resources – efficient finance	Uncertainty and risk
Western Power Distribution	WMID					
	EMID					
	SWALES					
	SWEST					
Electricity North West Ltd	ENWL					
Northern Powergrid	NPgN					
	NPgY					
UK Power Networks	LPN					
	SPN					
	EPN					
SSE Power Distribution	SSEH					
	SSES					
SP Energy Networks	SPD					
	SPMW					

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## DNOs have undergone a genuine step-change.....



... and see benefits beyond the regulatory incentives.

## But there are clear problems and risks for regulators

Was it really any more than a box-ticking exercise?

Did DNOs actually change their plans? Or did they present stakeholder engagement where it supported their preferences?

Did customers actually benefit?  
Did Ofgem?

## ...and fast-tracking faces some difficult questions.

*“There could be an £860m difference between Western Power Distribution (WPD)’s ‘fast-track’ RIIO-ED1 assessment, approved by Ofgem, and Ofgem’s subsequent view of efficient costs in October 2014.*

*If this is an Ofgem miscalculation caused by fast-tracking, WPD customers may have to fund the £860m difference over the eight-year price control period.”*

Energy and Climate Change Committee Report into Network Costs.

*The report raised the question of whether a “miscalculation” by the regulator has led to WPD’s customers effectively being overcharged by £860 million. WPD’s financial settlement ... was fast tracked under a new system in May 2014. By the time the regulator made its determinations on the other networks, its view of efficient costs had changed. WPD declined to comment.*

Utility Week article, 23<sup>rd</sup> Feb

Two CMA appeals announced this week may see Ofgem’s whole process come under criticism.





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