***NGN CEG Response –12 May 2023***

**Consultation on frameworks for future systems and network regulation: enabling an energy system for the future.**

Introduction

The NGN CEG welcomes the opportunity to respond to this consultation.

The CEG was established in 2018 to scrutinise the RIIO-2 business planning process of NGN to ensure stakeholder and customer needs and preferences were considered and reflected in the plan.

You can find more about our work and findings at [www.NGNCEG.co.uk](http://www.NGNCEG.co.uk)

Our comments are a result of discussions within the group; with other stakeholders and with NGN; as well as observations from the early stages of Ofgem’s working groups. The Chair of NGN’s CEG has also been in discussions directly with Ofgem along with the Chairs of other CEGs (similar bodies retained by companies after the start of RIIO-2) to consider the role of stakeholder engagement in the future and lessons learned from enhanced engagement during RIIO-2 planning and monitoring.

Our deliberations started when we took part in an evaluation of the CEGs/UGs by Ofgem at the end of the formal GD2 processes in 2020, and we engaged in discussions with NGN after Ofgem issued its Open Letter to the network companies prior to this formal consultation.

We have restricted our comments to issues that the CEG membership feels competent to comment on and that are important to gas customers and the gas distribution networks, or where there is the potential to improve customer outcomes in the north of England across energy systems.

There remain however a number of areas where we are finding it difficult to form clear views, and it is clear that a considerable amount of further thinking will be needed by Ofgem, the companies and other parties who will be needed to plan and manage a reliable, resilient, and affordable energy system that delivers the UK’s Net Zero targets.

We clearly support Ofgem’s ambition that company business plans should be ‘informed by customer and stakeholder intelligence to deliver maximum consumer benefits and optimal, least cost solutions.’ But we would ask that there is real granularity when it comes to different stakeholders and customers and the way members of our communities can become better informed about the way in which they can engage and weigh up the options before us.

Clearly some major policy decisions are needed by Government before some pathways to Net Zero can be properly considered and whatever the timescales for the next price control period, we must not be complacent and wait for decisions, but ensure we use all existing regulatory mechanisms to drive forward innovation, and research/trials to provide the evidence we will need for energy systems of the future.

Households currently using gas for heating have little incentive to move to heat pumps in the current climate and the take up of grants and products has been paltry given the targets set out in Boris Johnson’s 10 Point Plan for Net Zero. Gas is likely to continue to be used without a greater shift in policy frameworks, the contractor supply chain and building retrofit schemes to make the customer journey easier and cheaper. Without mandatory changes and strong household incentives gas will continue to be the heating fuel of choice based on cost and convenience and it will be very difficult to progress the transition to lower carbon options, whether repurposing the gas networks for hydrogen, or electrification over the next 5-7 years.

Whilst it is right that there is sufficient time allowed to make considered decisions about the future regulatory frameworks, it is important that as much clarity as possible is provided by Ofgem about the specific incentive, assessment and reporting methodologies it will implement to ensure the Companies can design and draft their plans to reflect these prior to seeking stakeholder and customer feedback.

We support the evolutionary approach to energy regulation, developing frameworks based on evidence, and future need. RIIO-2 recognised the need to rebalance the benefits of the financial incentive schemes between shareholders and customers and whilst increased investment needs to be attracted, this must not result in unwarranted returns.

The RIIO-2 approach has sought to provide the necessary framework to incentivise innovation, high levels of service standards and value for money. These principles should be retained whilst recognising that we have to move more quickly.

New responsibilities and protections for customers in vulnerable situations have stimulated a range of new initiatives and programmes and it is vital that support for all customers, but particularly those who need extra help, is built into all future regulatory models including fixed licence obligation outputs and incentive mechanisms that lead to meaningful and measurable customer outcomes.

We agree that new governance structures and capabilities will be needed to optimise current energy systems and to plan for, and manage, future systems. Spatial and energy planning need to go hand in hand, but this will require a significant shift in Government resourcing of local/regional bodies.

Please note that the NGN CEG has not responded directly to the separate consultation on Local Energy Institutions and Governance, however, we have reviewed the response produced by the Northern Powergrid CEG (two members of NGN’s CEG are members of that Group) and we have supported its response to relevant questions.

**Q.1. What should the role of the ‘consumer voice’ be and through what institutions and processes should it be channelled?**

Firstly, it is important for Ofgem to reflect on the lessons it, and the companies, learned from enhanced stakeholder engagement through the planning and delivery stages on RIIO-2 to date. There was nothing in the consultation document that gave us or customers confidence that lessons had been shared across Ofgem at this stage, whilst recognising some changes were made to the ED2 process following learnings from GD/ET/GT2.

Ofgem undertook an evaluation exercise at the end of the GD2 and ET/GT2 planning process to understand the benefits of enhanced engagement and understand what had gone well to help inform future decisions. Ofgem undertook 73 interviews and reached a number of conclusions namely: the groups had improved the quality of the business plans submitted; they had acted as independent bodies; there had been constructive dialogue and scrutiny; the groups offered good value for money; they helped to broaden thinking, challenged assumptions and probed company structures and cultures.

It has been clear that some of the recommendation from that exercise have been implemented during ED2 - closer engagement with Ofgem, clearer guidance on deliverables and timescales, and liaison between the Groups to discuss common issues but it is important that the findings from the exercise are given strong consideration during this consultation process.

Secondly, we need to unpick what Ofgem means by ‘Consumer Voice’. It would be helpful to think not about ‘the’ consumer (perhaps this is due to wording in Ofgem’s statutory duties?) but about people who live in a region, a locality, or a street affected by company decisions and plans. Many of us hold views of a general nature, but these may change when impacted directly. NGN has created a range of stakeholder groups with different needs and interests, but they also engage with a Citizens’ Panel made up of people with little or no understanding of the company through to well informed individuals who have been impacted by the Company (requiring a connection/experiencing a planned or unplanned gas cut). Weighing up the range of views and responding to meet the preferences of all can sometimes be challenging but stimulating debate and asking customers to reach some shared view after considering trade-offs can help shape the design and delivery of customer services and network management.

There is, therefore, a need for Ofgem to mandate a detailed stakeholder engagement strategy which provides evidence of how stakeholder views have been sought and used to inform decisions in areas that stakeholders can reasonably be expected to contribute.

The NGN CEG was established in 2018 and was mandated by Ofgem for the gas distribution companies (the electricity and gas transmission companies had a similar mandate for User Groups). There were a clear set of requirements although the groups themselves produced governance documents setting out their Terms of Reference, Operating Models and in NGN CEG’s case, Effectiveness Criteria by which we would monitor our own performance. These documents have been updated to reflect our continuing, albeit non-mandated role to monitor delivery and contribute to the next price control planning process. A copy of the current TOR and annual effectiveness report for 2022-23 has been provided to Ofgem. Our next annual report on the company’s performance will be published on 1 July and we hope that these documents will help to inform Ofgem’s decision on the value of CEGs and the role they can play in the future. They demonstrate the way in which we have been able to hold the company to account for the commitments it made, and shaped meaningful engagement that continues to share delivery.

We strongly believe that development and delivery of NGN’s GD2 business plan has benefited greatly not only from the enhanced stakeholder strategy it has deployed but also the scrutiny role of the CEG, and we advocate similar processes be followed for the next price control.

In a nutshell we propose:

* Mandating by Ofgem of **independent** Customer/Stakeholder Groups for the next price control period and on an enduring basis. This will help the groups in securing evidence they require in a timely manner in order to report on how stakeholders/customers have influenced business plans, and on an annual basis on how well they are performing against their commitments to customers. It will also enable transparency and public awareness of the work of the groups through a requirement to report openly on a regular basis on how they are fulfilling their roles.
* Previously, the CEGs had no responsibility for scrutinising the financial aspects of the RIIO framework, and although some groups sought to challenge on the engineering justification plans/cost benefit analyses, this was more firmly within the remit of the cross-company Challenge Group. There was some inefficiency and duplication in roles of the national and company specific groups which should be addressed going forward.
* Some of the more technical aspects of the regulatory framework should be outside of the scope for CEGs, but it is important that the groups are able to question how the incentive mechanisms can drive company behaviours that result in meaningful outcomes for customers.
* Membership of the CEGs is regularly refreshed with a maximum time served of two regulatory periods. The companies should provide administrative support and adequate resources to facilitate recruitment to, and running of, the groups. Members should not seek to represent customers but have the ability to influence the way in which the energy industry undertakes stakeholder engagement (and how it interprets and responds) and have experience and professional knowledge of the key areas of delivery.
* Ofgem should engage with the groups on a regular basis to help benchmark performance and share good practise across the companies, and to build trust in the companies’ approaches to engagement and delivery, which will be fundamental if Ofgem wish to introduce elements of self-regulation/reduced reporting.
* We also believe that CEGs should become formal members of the proposed new regional energy institutions to help reflect wider stakeholder views in future energy systems planning. Ensuring the views of customers are considered by expert engineers and spatial planners is essential to designing and delivering systems that are needed and can be optimised. Having a regional energy systems remit as well as company remit is something that should be considered.

**Q.2. How detailed could an independent, cross vector view become to determine future plans for periods beyond RIIO-2 and support effective use of the ‘Plan and Deliver’ model?**

It has proved difficult to date to properly plan for whole systems. Gas and electricity planning has gone along parallel lines. It is timely to consider how we can bring together energy systems that are needed for the services they enable to communities and individuals as well as other service providers including transport and anchor institutions that are also tasked with Net Zero targets and enabling a low carbon transition.

There may be some merit to this approach therefore, if as is suggested in paragraph 3.7, the model will be based on the creation of Local/Regional Energy Institution strategic and detailed plans. However, the application of the different regulatory mechanisms that are being used in RIIO 2 needs to be made in a sector specific and project specific manner (see comments below).

**Q.3. Under what circumstances would competition, or other procurement models such as open book contracting, have benefits over ex ante incentives as a cost control mechanism?**

**Q.4. What is your view on the options identified for simplification of incentive regulation? What would be the benefits and costs by comparison to the approaches used in RIIO-2?**

**Q.5. What are the network activities where there would be benefits for a move to an ex post monitoring regime, and what would be the associated costs?**

**Q.8. What is your view on the most effective approach to regulation of Gas Distribution and Transmission beyond RIIO-2? What would be the benefits and costs of moving to a simpler approach to regulation of the ongoing costs of operating and maintaining the network?**

*We have bundled our responses to questions 3, 4, 5 and 8 below*

This is not an area where the CEG has specific expertise, however we are not convinced that the Plan and Deliver model as outlined will bring any real benefits to gas distribution over the next two years (assuming the price control period is extended for that period for GDNs). In fact, it could potentially reduce the benefit of regional planning and control in favour of a centralised approach which flies in the face of devolution.

We have seen evidence of how NGN has brought real efficiencies to drive down costs to customers through local procurement and using/creating the local contractor supply market. We note that Plan and Deliver relates better to larger scale projects for transmission companies or major cross sector initiatives and should be considered for these and the continued decarbonisation of the power grid.

Enhanced regional whole system planning which incorporates spatial planning could help identify where NGN investment will be needed, but we are not convinced that nationally procured contracts would lead to better outcomes in terms of price and quality. Evidence suggests that to the contrary, many nationally procured contracts are limited to a small number of major contractors and do not offer added value of local jobs, or any understanding of local area needs. Competitive tendering is already required for work over agreed amounts, and this could continue to be monitored by Ofgem.

We are supportive of the continuation of ex-ante regulation with some reduced reporting and a lighter touch approach for some areas of NGN’s business where it is able to demonstrate historic high levels of performance and where costs have been historically benchmarked, for example where there is a Health and Safety Executive Requirement to maintain or replace pipes, whilst not undermining the concepts of continual improvement, innovation and efficiency.

However, there must be clear penalties and regulatory intervention where companies underperform.

There are three fundamental questions that we believe that Ofgem and the companies need to be able to answer:

1. What tangible pass-through benefits will these different approaches have for customers? (i.e. enhance the fair distribution of efficiency savings and investments)
2. What evidence has been provided, or is needed, that shows that the different mechanisms will result in better services, a faster move to decarbonisation and cost savings to customers?
3. What would constitute ‘essential’ reporting to provide sufficient assurance to Ofgem that the companies are meeting their licence obligations, and therefore enable processes to be made simpler and allow a degree of self-regulation?

**Q.6. What are the benefits and costs of this approach for Electricity Transmission by comparison to an evolution of the approach in RIIO-2, and what are the implementation barriers?**

N/A

**Q.7. What is the potential for Electricity Distribution planning and commissioning to move to an alternative model by the end of RIIO-2, and what might be the benefits and costs of doing so?**

N/A

**Q.9. Should there be a shorter-term price control in gas distribution and/or gas transmission, and how could this work in practice?**

There is a rationale for extending the current period. What we need to ensure however is that we do not ‘waste’ two years in just delivering BAU to the detriment of exploring new ways of working and the pathways to meet local decarbonisation ambitions and the UK’s legally binding international commitments on climate change (including the UN Sustainability goals).

Extending the current Price Control period will allow time for some of the current policy uncertainties to be further considered and allow a new Government (of whatever make up following the next General Election due by the end of 2024) to bring forward new policies. It will also mean that the roles of the FSO and RSPs can be agreed and start to be established. Next stage hydrogen trials and developments will also provide more evidence on the potential future of this gas in homes, transport and industry. Decisions on Repex and asset stranding and decommissioning also need to be confirmed and this extended period might allow for more public discussion and modelling of impacts that can be shared with energy customers through Citizens Panels.

**Q.10. Would there need to be any changes to maintain a stable and consistent financial framework if we were to make greater use of different regulatory archetypes, and if so, what would those changes need to be?**

No comment

**Q.11. Do you have any views on our proposed analytical approach?**

No comment