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To National Grid Electricity
Transmission, SP Transmission
Ltd and all interested parties

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Decision on funding arrangements for the Western High Voltage Direct Current link ("Western Bootstrap")

The electricity transmission companies' overall strategic investment programme for accommodating the anticipated significant growth of renewable generation in Scotland includes, amongst other projects, a subsea "**bootstrap**" running down the west coast of GB, referred to as the **Western High Voltage Direct Current link (Western HVDC link)**. The Western HVDC link is being developed jointly by National Grid Electricity Transmission (NGET) and SP Transmission Ltd (SPTL) (referred to as "the TOs" in this letter).

The TOs requested funding for construction works on the Western HVDC link under our Transmission Investment Incentives[1] (TII) framework. In August 2011 we consulted on our minded-to position (see the Annex to this letter), with its associated conditions, which we then maintained in our updates of November 2011 and February 2012. Our April 2012 Final Proposals for SPTL under RIIO-T1[2] confirmed that in the price control period commencing 1 April 2013 the Western HVDC link, while being treated as a baseline project, would be subject to re-opener provisions to allow revenues to be adjusted for certain pre-defined events. We published the headlines of our Initial Proposals for NGET under RIIO-T1 on 16 July 2012, and we set out those Initial Proposals in more detail today.

We consulted in May 2012[3] (our **May 2012 consultation**) on the details of our proposed funding arrangements for the Western HVDC link for NGET and SPTL under both TII and RIIO-T1. **The purpose of this letter is to set out our final funding decision on the Western HVDC link,** following consideration of responses to our May 2012 consultation and further review of our minded-to position.

While noting that one of the conditions attached to that minded-to position remains outstanding in light of the planning issue for the southern convertor station, we do not think it appropriate to defer our final funding decision until this matter is resolved. Therefore, **we have updated our position on cost recovery** and reached a final funding decision. However, in the interests of consumers we have retained the option to revise funding in certain circumstances. We expect the TOs to manage outstanding delivery risks in an efficient manner to avoid unnecessary costs being incurred.

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[1] See TII webpage, where all documents related to TII that are referred to in this letter can be found: http://www.ofgem.gov.uk/Networks/Trans/ElecTransPolicy/CriticalInvestments/InvestmentIncentives/Pages/InvestmentIncentives.aspx
[2] See RIIO-T1 webpage, where all documents related to RIIO-T1 that are referred to in this letter can be found: http://www.ofgem.gov.uk/NETWORKS/TRANS/PRICECONTROLS/RIIO-T1/CONRES/Pages/ConRes.aspx
[3] Consultation on proposed funding arrangements for Western High Voltage Direct Current (HVDC) link ("Western Bootstrap"), Ref 73/12, May12

We set out below a high level summary of our decision on the ex ante allowances and risk sharing arrangements between the TOs and consumers for this project under TII (to end 2012-13) and RIIO-T1 (from 2013-14 onwards):

- We are setting the TOs a total ex ante allowance of **£1050.7 million** (2009-10 prices), linked to deliverables consistent with the assumptions on which the allowance is based.
- We are treating the project as a whole by adopting a fixed cost allocation ratio of 68.5:31.5 between NGET and SPTL both ex ante and ex post, and by applying a re-opener mechanism that is specific to this project. This re-opener mechanism is in line with that set out in SPTL's Final Proposals under RIIO-T1, and will apply to both NGET and SPTL and take into account allowances and expenditure in both the TII and RIIO-T1 funding periods.
- The efficiency incentive sharing factor applying to NGET and SPTL will be specified separately in line with their respective RIIO-T1 Final Proposals, and will also apply in the TII period (ie 50 per cent for SPTL and yet to be finally determined for NGET).
- We are also retaining the option to allow funding to be reviewed if the planning issue for the southern convertor station has a material impact on the cost or delivery of the project. This is to ensure that only efficiently incurred costs can be recovered.

Our funding decision is in line with the proposals set out in our May 2012 consultation. However, we have refined the cost allocation ratio (previously 70:30) in light of further analysis.

The Annex to this letter sets out the details of our funding decision, and includes the background to and scope of our decision. It also discusses how, in updating our position on cost recovery, we have taken into account responses to our May 2012 consultation and the status of the conditions attached to our August 2011 minded-to position.

Way forward

We will separately take forward work to develop the licence changes that are necessary to reflect our funding decision and to enable the associated cost recovery within the TII and RIIO-T1 frameworks. We note that this may require some cross-referencing between the respective licence conditions of NGET and SPTL, consistent with the treatment of the project as a whole. It may also require inclusion of specific provisions to reflect the differences in treatment of this project under TII as compared to other projects funded under TII to date. We will work with the TOs in developing these licence changes.

The total ex ante allowance of £1051 million for this project includes £144 million in the TII period, which increases the total of all allowances determined under TII, across all projects, to £761 million (previously £617 million). In line with our decision on the licence changes to extend the TII policy framework into 2012-13[4], we will take the allowances determined for the TII period into account in setting future revenue adjustments to reflect the true-up against the allowances assumed for the purposes of setting revenues up to the end of 2012-13. These revenue adjustments will be applied from 2013-14 onwards and will have no impact on revenues already determined for years up to and including 2012-13.

Any questions on this document should be directed, in the first instance, to Cheryl Mundie (e-mail: cheryl.mundie@ofgem.gov.uk, tel: 0141 331 6003).

Yours faithfully,

Ian Marlee
Senior Partner – Smarter Grids & Governance: Transmission

[4] Transmission Investment Incentives (TII): Decision under section 11A(1)(a) of the Electricity Act 1989 to make modifications to electricity transmission licences to reflect extension of the TII framework into 2012-13. Jun'12

Annex: background and details of our decision

Background

The TII framework was introduced in 2010 to provide project-specific, interim funding[5] for critical large-scale investments that the transmission companies identify are required to support achievement of the Government's 2020 renewable energy targets. The TII framework will be superseded on 1 April 2013 by the funding arrangements to apply under RIIO-T1.

On 1 August 2011[6] we set out, for consultation (our August 2011 consultation), our minded-to position on funding of the Western HVDC link subject to certain conditions. We then published updates on 10 November 2011[7] (our November 2011 update) and February 2012[8] (our February 2012 update) in which we maintained our minded-to position, and the conditions associated with it.

Our RIIO-T1 Final Proposals for SPTL[9] in April 2012 confirmed that, in SPTL's case, the Western HVDC link is to be treated as a baseline project and subject to a re-opener provision specific to this project, but that the details of funding for this project will be subject to the outcome of this (TII) assessment process.

Our May 2012 consultation set out details of our proposed funding arrangements for the Western HVDC link for NGET and SPTL both under TII and RIIO-T1. We explained how our proposals had been informed by consultancy work and developed with reference to the TOs' final plans for the Western HVDC link and the status of the minded-to conditions. We also discussed how we had taken into account interactions with our work on RIIO-T1, and the fact that the Western HVDC link is being delivered jointly by two licensees, and explained why we considered that the Western HVDC link warrants a different approach to other projects funded under TII.

Our proposed funding arrangements included annual ex ante allowances for each TO, the deliverables to be linked to those allowances, and our approach to dealing with changes in costs and/or outputs. We also set out the proposed basis of the efficiency incentive sharing factor for each TO, and more detail on the proposed re-opener provisions that would apply to the project taking into account its specific characteristics including the latest status of the planning issue for the southern convertor station. We also set out our proposals for how we would deal with the situation if the Western HVDC link is not delivered as a consequence of the TOs not obtaining planning consents for the southern convertor station.

Further background on the TII and RIIO-T1 frameworks, our assessment approach for the Western HVDC link and our process to date can be found in our May 2012 consultation.

Consideration of responses to May 2012 consultation

Our May 2012 consultation closed on 20 June 2012. We received two responses, one of which was a joint response from NGET/SPTL. Both responses were non-confidential and generally supportive of our proposals. Both responses sought clarity on our approach to implementing our proposals, which we have addressed above in the "Way Forward" section in the main body of this letter.

[5] By "funding under TII" we mean to allow efficient cost recovery via a revenue stream calculated under the relevant provisions of the TII framework. The TII framework is set out in Special Condition D11 of NGET's licence and Special Condition J12 of the licences of SPTL and Scottish Hydro Electric Transmission Ltd (SHETL).
[6] Transmission Investment Incentives: consultation on minded-to position for the Western High Voltage Direct Current (HVDC) link ("Western Bootstrap"), Ref 94/11, Aug'11
[7] Transmission Investment Incentives: update on Western High Voltage Direct Current (HVDC) link ("Western Bootstrap"), Nov'11
[8] Transmission Investment Incentives (TII): further update on Western High Voltage Direct Current (HVDC) link ("Western Bootstrap"), Feb'11
[9] RIIO-T1: Final Proposals for SP Transmission Ltd and Scottish Hydro Electric Transmission Ltd, Ref 58/12, Apr'12

The response from NGET/SPTL raised some specific issues in relation to the following aspects of our funding proposals:

- **cost allocation between TOs** – NGET/SPTL proposed a marginally different ratio to Pöyry's recommended ratio of 70:30, in order to give a more accurate representation of costs and risks carried by each TO,
- **basis of the risk allowance** – NGET/SPTL proposed to base this on the P80 level (80% likelihood that costs will not exceed contingency) rather than the P50 level (50% likelihood that costs will not exceed contingency) recommended by Pöyry, and
- **efficiency incentive sharing factor** – NGET/SPTL proposed that this should be the same for each TO, and that a higher return should be provided in the TII period if aligning that sharing factor with RIIO-T1 rather than with TII funding to date.

Having considered these points and discussed further with the TOs, we do not think they warrant a change in our approach to the risk allowance or sharing factor. However, we have modified the cost allocation ratio to 68.5:31.5 in light of further analysis taking into account the latest information from the TOs on the cost split.

Regarding the risk allowance, we remain of the view that P50 is appropriate in this case[10] because:

- the risk allowance only captures residual risks not included in the contract – consumers are already protecting the TOs against some risks (eg first 60 days of bad weather),
- we think that the sharing factor and re-opener provisions provide sufficient protection for the TOs,
- setting the risk allowance based on P80 would, in this case, likely lead to consumers funding allowances that are larger than actual expenditure, and
- we are not swayed by the TOs' argument that a higher risk allowance is appropriate due to the scale and complexity of this single project and the inability of the TOs to balance risk across multiple projects - we note that the key issue for financeability is investors' ability to diversify risk across their portfolio.

We also remain of the view that it is appropriate that the efficiency incentive sharing factor applying to each TO for this project under RIIO-T1 should be the same as that specified for other capex in their respective RIIO-T1 Final Proposals.

- We think this is important in order to ensure that the TOs do not have incentives to reallocate expenditure between projects.
- We expect that by treating this project as a whole with fixed cost allocation ratios between the TOs, they will both face the same incentives to manage expenditure efficiently.
- Further, their respective sharing factors (determined at 50% in our RIIO-T1 Final Proposals for SPTL, and proposed at 48% in our RIIO-T1 Initial Proposals for NGET), are in any case unlikely to be significantly different from each other.

We also still consider it appropriate that, for this project, the sharing factor for the TII period should be the same as that under RIIO-T1 rather than that applying to other capex in TPCR4 (ie 25%), as adopted for TII funding to date.

- We retained flexibility to vary our approach to TII funding and we think it appropriate to do so in this case for the reasons set out in our May 2012 consultation, noting the size of the project, the fact that it is being taken forward through a joint venture, and the timing and scope of our funding decision.
- We think that aligning the TII sharing factor with that for RIIO-T1 will avoid the TOs having undesirable incentives to move expenditure between periods.
- We do not think that a higher return during the TII period is necessary, as the planned expenditure on this project under TII is relatively small compared to that under the wider price control, and the allowances for the TII period include costs already incurred.

[10] We will continue to assess any future projects on a case by case basis.

Review of minded-to position

Minded-to position set out in August 2011

Our minded-to position, as set out in our August 2011 consultation and maintained in our November 2011 and February 2012 updates, was **to allow efficient cost recovery under TII for construction works on the Western HVDC link from 2011-12, 'in principle', subject to the following conditions**:

a) consideration of responses to our August 2011 consultation
b) a positive conclusion from our ongoing project assessment
c) successful resolution of relevant licensing issues
d) successful resolution by the TOs of any licensing issues with the relevant authorities of Northern Ireland and Isle of Man, and any planning consents
e) statutory consultation on the relevant licence modifications to give effect to the Authority's final decision.

We set out in our August 2011 consultation that satisfaction of condition b is subject to:

- our final assessment of the case for delivering the Western HVDC link in 2015[11], following an updated review of needs case, scope and timing of the overall project[12],
- no material escalation in expected costs of the specific construction works[13] to which the funding request relates,
- confirmation by the TOs of firm plans for those works and demonstration of their readiness to proceed with those plans in 2011-12,
- determination of annual ex-ante funding allowances for 2011-12 and 2012-13, in line with our view of efficient costs of those works, which (a) take account of planned expenditure, and (b) can be linked to deliverables which reflect planned milestones and forecast output measures, and
- consideration of appropriate risk sharing arrangements between the TOs and consumers.

Approach to dealing with outstanding minded-to conditions

Our May 2012 consultation reviewed the status of the minded-to conditions. We noted that conditions a and c were already satisfied, while satisfaction of conditions b and e would be consequential to our conclusions on the specifics of funding and any subsequent licence modifications to that are necessary to reflect our final decision. However, we highlighted some outstanding issues for the TOs to resolve in relation to **condition d**. Specifically, we noted ongoing work by the TOs to resolve a planning issue at the southern convertor station, following rejection by the Flintshire County Council Planning Committee in February 2012 of the TOs' planning application for their proposed site at Kelsterton in Wales.

As of July 2012, condition d remains outstanding. This situation was anticipated in our May 2012 consultation, and our approach to dealing with this was reflected in our funding proposals set out in that consultation. We took the planning issue into account while being consistent with the expectation that it is resolved in a timely manner and does not have a material impact on the delivery of the link. We also took account of the possibility that the TOs do not obtain planning permission for any suitable site and in such a case would be unable to deliver the project such that condition d would not be satisfied. To address this risk, our funding proposals included additional safeguards to protect consumers in the event that the project is severely affected by the key risks highlighted by the TOs.

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[11] We concluded on this issue in our November 2011 update.

[12] As set out in paragraph 1.4 of Annex 1 of our August 2011 consultation, the overall project comprises the HVDC cable and convertor stations at either end (the "HVDC component), plus new substations at Hunterston East in SPTL's area and at Connah's Quay in NGET's area.

[13] These relate to the costs associated with the construction of the HVDC cable and convertors (ie the HVDC component of the link), including costs and risks not reflected in the contract price.

Case for reaching a funding decision at this stage vs deferring until condition d is satisfied

We expect the TOs to work effectively with stakeholders where applicable to address planning issues and to reach a solution in a timely manner. We note that until it is successfully resolved by the TOs, the planning issue at the southern convertor station will continue to have potential to have a significant impact on the cost or delivery of the link. Taking into account the latest information from the TOs as of July 2012 we still think that the likelihood that the TOs do not obtain planning permission for any suitable site, and are therefore unable to deliver the project, is low. We have sought to balance this risk against the potential consequences of delaying our decision or withholding funding while condition d remains outstanding. Overall we remain of the view, that it is appropriate to enable the TOs to maintain their planned delivery programme so that the expected benefits (which could be in the range one to four billion pounds[14]) of the project can be realised.

In reaching this view we have noted that if we were to delay our decision or to withhold any part of the funding until planning permission is granted, the TOs would be unlikely to proceed with the project which could lead to significant consumer detriment. For example, if the TOs cancel the contract in 2012-13 then they would have incurred costs of up to £144 million[15], the majority of which relates to payments under the contract with Siemens-Prysmian[16]. If, having cancelled the contract, the TOs subsequently decided to proceed with the project this would result in a minimum 2 year delay while they re-tender. This could result in around £0.2 billion[17] of lost benefits to consumers, compared to the potential benefits under the current planned delivery timescales. There would also be additional costs of having to re-tender the contract and the contract price may also increase. On balance, we think that the potential benefits to consumers of allowing the TOs to proceed with their delivery plans outweighs the low risk of planning permission not being granted (at the preferred site or an alternative).

Updated position on cost recovery

Having reviewed our minded-to position, we do not consider it appropriate to defer our funding decision until condition d is satisfied. We have therefore updated our position on cost recovery, as follows:

- Taking into account responses to our May 2012 consultation, we are satisfied that our approach to dealing with the planning issue within our funding proposals is appropriate.
- We have therefore reached a positive conclusion under condition b, and in turn have set out our final decision on the specifics of funding (see the "Funding decision" section below).
- Cost recovery in line with our funding decision remains subject to statutory consultation on any licence modifications that are necessary to reflect that funding decision under the TII and RIIO-T1 frameworks (see the "Way Forward" section in the main body of this letter).

Our funding decision allows the TOs to get on with their planned programme for delivery of the link. It takes the current status of the planning issue into account while being consistent with the assumption that it is resolved in a timely manner. In addition to ensuring the full potential benefits of the link can be realised, our funding decision endeavours to protect consumers by retaining the option for funding arrangements to be reopened in the event of non-delivery. This is to ensure that only efficiently incurred costs can be recovered.

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[14] This figure is based on analysis of net lifetime benefits set out in the August 2011 consultation, for a range of generation scenarios and central input assumptions. As set out in our November 2011 update, this range reduces to around £0.5billion to £2.5 billion when varying those input assumptions to stress test the CBA.

[15] Based on the sum of the ex ante allowances set out below for the TII period.

[16] This does not take into account any compensation payment that may be owed to the supplier for cancellation of the contract.

[17] This is based on TOs' estimate that delaying delivery of the Western HVDC link to 2017-18 would reduce net lifetime benefits by £165 million under the Gone Green scenario. This analysis, which we considered as part of the needs case assessment, does not take into account any impact on the costs to deliver the project.

We believe that our funding decision strikes the correct balance between providing certainty to the TOs with sufficient funding to cover the efficient costs of delivering the project in line with their latest plans, and providing incentives on the TOs to manage cost variations and project risks on behalf of consumers. However, in seeking to maintain their planned programme, we expect the TOs to manage outstanding delivery risks in an efficient manner in order to minimise costs incurred in the event of non-delivery. We will take such factors into account in determining the level of efficient costs that should be recoverable in such circumstances.

Funding decision

Scope of decision

The TOs' plans for the Western HVDC link are discussed in more detail in our May 2012 consultation and outlined as follows:

- The joint venture set up by NGET and SPTL awarded a contract to Siemens-Prysmian for the manufacture and installation of the HVDC cable and two convertor stations, for delivery in late 2015. The planned 600kV[18] design would provide a continuous capacity of 2.25GW and a short-term (6 hour) rating of 2.4GW.
- The HVDC cable will follow a predominantly subsea route between convertor stations located close to its respective landing points near new substations being constructed at Hunterston East in SPTL's area and at Connah's Quay in NGET's area. Those substations form part of the overall Western HVDC project, but are out of scope of this funding decision having already been considered separately[19].

The detail of our funding decision set out below applies to both NGET and SPTL, covers both the TII and RIIO-T1 funding periods, and relates to the costs of works associated with construction of the HVDC cable and convertor stations in line with the above plans, including costs and risks which are not reflected in the contract price. These works are collectively referred to as "the project" throughout this letter.

Unless otherwise specified, our funding decision is in line with the funding proposals set out in our May 2012 consultation.

Ex ante allowances

Table 1 below shows the **ex ante allowance** for the project as a whole and for each TO, for each year of expenditure.

Table 1: Annual ex ante allowance for whole project and for each TO

Ex ante allowance (£m)	TII		RIIO-T1				Total
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	
NGET (68.5%)	15.5	83.0	161.7	230.4	208.9	20.1	719.7
SPTL (31.5%)	7.2	38.2	74.3	106.0	96.1	9.3	331.0
TOTAL	**22.7**	**121.2**	**236.0**	**336.4**	**305.0**	**29.4**	**1050.7**

The total ex ante allowance, for the project as a whole, is based on information from the TOs up to March 2012. It covers all costs associated with the construction of the HVDC cable and convertor stations, including:

- the **contract costs** reflected in the contract price (£872.5m) for the HVDC cable and convertor stations,

[18] Achievement of this voltage and resulting ratings is subject to the outcome of testing once the link is physically in place.
[19] Transmission Investment Incentives (TII): decision on requests for funding in 2012-13, Ref 13/12, Jan'12

- the **non-contract costs** which are additional costs to the TOs for items not part of the contract (such as project management, land purchase and marine licences), and
- a **risk allowance**, representing a contingency for further costs to the TOs which may arise in relation to residual risks not borne by the supplier.

The contract costs and non-contract costs included in the above are set in line with the TOs' submissions. The risk allowance is derived from the results of the TOs' risk model, and set at a level which provides a 50% likelihood of exceeding the outturn cost for the modelled risks.

As noted in our May 2012 consultation, the **total ex ante allowance of £1050.7m** is **4% lower** than that requested by the TOs in their August 2011 submission, while incorporating provision for risks (including the planning issue) which have subsequently been identified or evaluated in more detail.

The **annual phasing** of the total ex ante allowance is as specified in Table 1. We note that any subsequent re-profiling of expenditure can be taken into account in the application of the efficiency incentive mechanism discussed below.

The annual ex ante allowances for each TO set out in Table 1 have then been derived from those given for the project as a whole by applying the **cost allocation ratio** of 68.5:31.5 for the split of forecast costs between NGET and SPTL respectively.

As set out above, the value of the cost allocation ratio has been updated since our May 2012 consultation, in light of further analysis. Consistent with treating the project as a whole, this cost allocation ratio will apply in all years and across all cost items, both ex ante (for setting the allowances for each TO in Table 1) and ex post (through the application of the efficiency incentive mechanism and re-openers for each TO as discussed below).

Efficiency incentive sharing factor

Under the **efficiency incentive mechanism**, over and under spends against the ex ante allowances will be shared between TOs and consumers based on a given sharing factor representing the proportion borne by the TO. Our decision regarding the **sharing factor** for the project is summarised in **Table 2** below with reference to the sharing factor to apply to each TO under RIIO-T1. The sharing factor for SPTL is 50%, as set out in our RIIO-T1 Final Proposals for SPTL. A sharing factor of 48% has been proposed for NGET in our RIIO-T1 Initial Proposals for NGET and will be finalised in our RIIO-T1 Final Proposals, in December 2012.

Table 2: Sharing factor for efficiency incentive mechanism

Sharing factor	TII	RIIO-T1
NGET	The value to be adopted for NGET under RIIO-T1	The value to be determined for all other NGET projects under its RIIO-T1 Final Proposals *(Note – a value of 48% is currently proposed in the RIIO-T1 Initial Proposals)*
SPTL	**50%** *(ie the value adopted for SPTL under RIIO-T1)*	**50%** *(ie the value already determined for all other SPTL projects under its RIIO-T1 Final Proposals)*

In the application of the efficiency incentive mechanism, we will treat the project as a whole by adopting a fixed cost allocation ratio of 68.5: 31.5 to apportion total expenditure on the project between NGET and SPTL respectively, for the purpose of identifying over and under spends against the ex ante allowance specified for each TO. This cost allocation ratio will apply in all years and across all cost items. We expect that any difference against actual expenditure by each TO individually will be dealt with via a commercial arrangement between the TOs.

Re-opener provision

The TII framework includes limited flexibility for adjustment to funding ex post via the asset value adjusting event mechanism and the output measures adjusting event mechanism. These mechanisms will not apply to this project, as they will be superseded by a re-opener provision that is specific to this project.

The **re-opener provision** specific to this project will be in line with that set out in our RIIO-T1 Final Proposals for SPTL, and based on the Cost and Output Adjusting Event (COAE) mechanism applying to Strategic Wider Works (SWW) projects. The re-opener provision will be triggered when a single pre-defined event leads to a change in total costs the magnitude of which exceeds a given threshold.

The relevant pre-defined events in scope of the re-opener provision are:

- adverse weather,
- unforeseen ground or seabed conditions, and
- the terms and conditions for any statutory consent, approval or permission.

The re-opener provision will:

- apply to the project as a whole, based on a joint submission from the TOs and with costs apportioned to each TO based on a fixed cost allocation ratio of 68.5:31.5 between NGET and SPTL (see above), irrespective of the actual incidence of costs,
- apply to a threshold of 10% of the total ex ante allowance (see Table 1) for the project as a whole, over both the TII and RIIO-T1 periods, and
- take into account expenditure in both the TII and RIIO-T1 periods in determining whether the threshold has been triggered.

Approach to dealing with the planning issue for the southern convertor station

The total ex ante allowance has been set taking the planning issue into account, and is consistent with the assumption that the planning issue does not have a material impact on the delivery of the link. We expect that, where relevant, changes in costs associated with the TOs' ongoing work to resolve the planning issue can be dealt with through the efficiency incentive mechanism and provisions for adjustment to funding ex post as described above.

Further, additional costs arising in the event that it is necessary for the TOs to progress an alternative site will, where relevant, be taken into account in our consideration of whether the above re-opener has been triggered under the pre-defined event relating to the terms and conditions for any statutory consent, approval or permission.

There remains a low risk that the TOs do not obtain planning permission for any suitable site for the southern convertor station and are unable to deliver the project. We have retained the **option to make an ex post adjustment** to allowances and associated outputs if the project is not delivered. This is to ensure that only efficiently incurred costs are recovered. This additional safeguard is intended to protect consumers in the event that the project is severely affected by those key risks that the TOs have highlighted.

Before making an ex post adjustment in such circumstances we will undertake a further assessment to determine the appropriate level of efficient costs that should be recoverable. That assessment will take into consideration the factors leading to non-delivery and the TOs' approach to managing outstanding delivery risks while seeking to maintain their planned programme. This will include consideration of any aggravating or mitigating actions undertaken by the TOs in relation to non-delivery and its impact on consumers, including any such actions undertaken in the period up to July 2012.

Deliverables

Given that our funding decision covers both the TII and RIIO-T1 periods, we will not define deliverables for this project for the period of TII funding. However, we still expect the TOs to report on progress through the annual reporting under TII, and the TOs will similarly be required to report on progress annually during RIIO-T1.

We will specify **wider works outputs** for this project in the licence under RIIO-T1 which are based on the TOs' plans as of March 2012, in terms of the capability provided across relevant boundaries and the completion timescales, and which are consistent with the assumptions underpinning the total ex ante allowance set out in Table 1 above. Those assumptions include the TOs' expectation that:

- the link is delivered at 600kV (achieving a boundary capability increase across Boundaries B6[20], B7 and B7a consistent with a continuous rating of 2.25GW and short-term (6 hour) rating of 2.4GW), and
- the planning issue does not have a material impact on the TOs' ability to maintain their current planned programme (for delivery in 2015-16).

The TOs will be jointly responsible for delivery of the wider works outputs. Once the project is commissioned, we will require the TOs to confirm delivery of the wider works outputs, and provide relevant supporting evidence. We will review the TOs' performance in delivery of the outputs. We will review deviations from agreed completion timescales to determine whether these constitute a contravention of the TOs' licence conditions. In such circumstances, we will consider whether late delivery constitutes a failure by the TOs in relation to the timely delivery requirements specified in the licence. In considering whether this is the case or not, we will look at the factors leading to the late delivery, the amount of consumer detriment caused and the extent to which the TO could be held responsible for events as well as whether or not they took reasonable steps to mitigate the impact of such events where they could do so efficiently.

If we are satisfied that the late delivery constitutes a contravention, TOs could be subject to a financial penalty which would be determined under the Authority's Statement of Policy with respect to Financial Penalties. In the case where the TOs under deliver in terms of capacity relative to the specified output, we may also determine whether the TOs have underperformed against their licence requirements and, if necessary, make an ex post adjustment to ensure that only efficiently incurred costs are recovered.

We expect that these arrangements, in combination with the above provisions for adjustment to funding ex post, will be sufficient to deal with any changes in the TOs' plans in terms of timing of delivery or capability provided.

[20] The value of 2200MW set out in SPTL's Final Proposals under RIIO-T1 for the increased boundary capacity across Boundary B6 was in line with SPTL's business plan submission and based on the central value within the capacity range for the Western HVDC link considered in the CBA.