

Decision on the closeout methodologies for RIIO-GT1

Subject	RIIO-GT1 closeout
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The RIIO-GT1 price control ran from 1 April 2013 to 31 March 2021. This document provides the detail of the methodologies that will be used to deal with uncertain costs within the price control and the delivery of outputs against specified targets. These methodologies will be included in the RIIO-GT2 Price Control Financial Handbook.

We consulted on the draft methodologies on 14 January 2022. This document sets out our methodology decisions following this consultation. We have published the non-confidential consultation responses alongside this document.

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Executive summary

The previous price control for gas transmission (RIIO-GT1) ran from 1 April 2013 until 31 March 2021. The RIIO-GT1 licence (the 'GT1 licence') makes provision in relation to several areas which, due to their uncertain nature, could only be settled once all costs and actual RIIO-GT1 performance is known. This means that some elements of the price control need to be subject to "closeout" once the price control has ended. To closeout the RIIO-GT1 price control, the following need to be addressed:

- Financial methodologies
- Pipeline Diversions
- South West Quadrant incremental capacity project
- Enhanced Physical Site Security (PSUP)
- Peterborough & Huntingdon compressor projects
- Hatton compressor project
- Disposals

This document provides a summary of each area of the price control where a closeout methodology was required, a summary of the consultation responses, a description of any changes made to the closeout methodologies since the consultation and the finalised closeout methodologies. The final closeout methodologies will be included in the RIIO-GT2 Price Control Financial Handbook (PCFH).

Related documents

Consultation on the methodologies to closeout RIIO-GT1

<https://www.ofgem.gov.uk/publications/consultation-closeout-methodologies-riio-gt1>

RIIO-T1 Strategy Decision,

<https://www.ofgem.gov.uk/publications/decision-strategy-next-transmission-price-control-riio-t1>

RIIO-T1 Final Proposals for NGGT

<https://www.ofgem.gov.uk/publications/riio-t1-final-proposals-national-grid-electricity-transmission-and-national-grid-gas-overview>

Supplementary documents to the RIIO-T1 Final Proposals

https://www.ofgem.gov.uk/sites/default/files/docs/2012/12/4_riiot1_fp_finance_dec12.pdf

Price Control Financial Handbook

[riio-gt1-price-control-financial-handbook_0.pdf \(ofgem.gov.uk\)](#)

RIIO-2 Final Determinations Transmission and Gas Distribution Network Companies

www.ofgem.gov.uk/publications/riio-2-final-determinations-transmission-and-gas-distribution-network-companies-and-electricity-system-operator

1. Background and overview

Background

1.1. The RIIO-GT1 price control set the outputs that National Grid Gas Transmission (NGGT) must deliver, and the revenues it is allowed to collect from customers, between 1 April 2013 and 31 March 2021.

1.2. Within RIIO-GT1 there are several areas of expenditure that require information about actual efficient costs incurred, revenue received and the extent to which outputs have been delivered before RIIO-GT1 can be fully closed out. These are compared with the costs, revenues etc. that were assumed in RIIO-GT1 Final Proposals ("Final Proposals")¹ to determine the value of any adjustment required for closeout.

1.3. We have not included closeout of the Network Output Measures (NOMs) in this Decision; NOMs is being consulted on separately due to their cross-sector scope.²

1.4. Table 1 gives a brief description of the areas of the price control that are subject to a closeout process.

Table 1: Cost areas for GT1 closeout

Area	Description	Chapter
Pipeline diversions	A "true-up" is required if material costs have been incurred during RIIO-GT1.	3
South West Quadrant	A mechanism is required to return allowances to consumers following cancellation of incremental capacity project.	4
Enhanced Physical Site Security	A "true up" is required if material costs have been incurred or avoided due to changes to PSUP requirements during RIIO-GT1.	5
Peterborough and Huntingdon compressors	A mechanism is required to ensure delivery of RIIO-GT1 compressor projects in GT2 and clawback allowances in the event of non-delivery.	6
Hatton compressor	An allowance adjustment is required for RIIO-GT1 Non-load capex to give effect to RIIO-GT2 Final Determination decision to fund elements of the Hatton compressor project in RIIO-GT1.	7
Disposals	Disposed assets are to be removed from the Regulated Asset Value (RAV) and values to be trued-up through the GT1 legacy PCFM.	8
NOMs	Consulted on separately due to cross-sector scope	N/A

¹ And following any subsequent re-opener Decisions

² [NOMs Closeout Submission Instructions](#) Guidance (May 21) and [Direction to changes to the NOMs Incentive Methodology](#) (Jun 21) have already been published.

RIIO-GT1 Closeout

1.5. On 14 January 2022 we consulted on our proposed methodologies for closeout of each of the elements of the price control in Table 1.³ The finalised methodologies detailed in this Decision document will be included in the PCFH. We will consult on amendments to the Price Control Financial Model (PCFM) and final revenue adjustments ahead of the November 2022 Annual Iteration Process (AIP).

1.6. Our Decision on the RIIO-GT1 closeout methodologies includes: mechanisms that “true-up” and reconcile actual expenditure against services provided by NGGT; output mechanisms which enable us to recover funds from NGGT if it has not delivered the outputs it was funded to deliver; mechanisms which deal with over or underspend against fixed allowances; and mechanisms that deal with over- or under-delivery against output targets.

1.7. We have based the methodologies on the approach and principles that we described in the RIIO-GT1 Strategy Decision⁴ and Final Proposals⁵, and as implemented in the GT1 Licence, relevant supplementary documents, and the PCFH.

1.8. For the calculation of financial adjustments under the Incentives Framework for NGGT’s output delivery against performance targets in RIIO-GT1, the methodologies are already established in the GT1 and GT2 Licences and therefore we did not include these within the closeout consultation.

Purpose of this document

1.9. This document sets out the background to the elements of the RIIO-GT1 price control that need to be closed out, detail of any changes we have made to the methodologies following the consultation, and the finalised RIIO-GT1 closeout methodologies.

³ [Consultation on the closeout methodologies for RIIO-GT1 | Ofgem](#)

⁴ [RIIO-GT1 Strategy Decision](#)

⁵ [RIIO-GT1 Final Proposals](#)

Responses to the RIIO-GT1 closeout consultation

1.1. We received one response to the consultation, from National Grid Gas Transmission (NGGT), which we have carefully considered when reaching our Decision on the RIIO-GT1 closeout methodologies.

1.10. A summary of the responses to the specific consultation questions is provided in the relevant chapters of this document, and we have published NGGT's non-confidential response on our website alongside this Decision.

Next steps

1.11. We will implement the closeout methodologies and make any necessary revenue adjustments as part of the November 2022 AIP. Further details are in Chapter 9.

Your feedback

1.12. We believe that consultation is at the heart of good policy development. We are keen to receive your comments about this decision document. We'd also like to get your answers to these questions:

1. Do you have any comments about the overall quality of this document?
2. Do you have any comments about its tone and content?
3. Was it easy to read and understand? Or could it have been better written?
4. Are its conclusions balanced?
5. Did it make reasoned recommendations?
6. Any further comments?

Please send any general feedback comments to Jon.Sharvill@ofgem.gov.uk.

2. Financial methodologies

This section describes the process which the Authority will follow in determining any revisions to NGGT's RIIO-2 RAV balances and revenue for the GT2 Price Control Period.

Background

2.1. To close out the Gas Transmission Price Control Review 4 (TPCR4), i.e., the price control that preceded RIIO-1, the RIIO-1 model contained "legacy" adjustments to Regulated Asset Value (LRAV) and revenue (LAR) in the 2013/14 regulatory year. For NGGT, the LAR value was spread over the 8 years of RIIO-1.

2.2. In contrast, the RIIO-GT1 licence introduced mechanisms that automatically true up revenue for outturn data on an annual basis. Therefore, the RIIO-GT2 Price Control Financial Model (RIIO-GT2 PCFM) does not need the same catch-all legacy terms used for TPCR4 closeout. Instead, the RIIO-GT2 LAR term is the sum of the pre-existing true-up mechanisms introduced in RIIO-1 (see Part A of Special Condition 7.1 for the list).

2.3. Rather than make a one-off adjustment to RAV at the start of RIIO-2, we now import the final RIIO-1 values into the RIIO-GT2 PCFM; this reflects the historical adjustments more transparently. Accordingly, the LRAV term has been repurposed to refer to the "outturn" (or ex-post) RAV additions in RIIO-1, rather than a one-off adjustment.

2.4. The LAR in RIIO-2 is the sum of existing true-up mechanisms, which have been extended into RIIO-2 to cover the closeout of RIIO-1.

2.5. One component of the RIIO-GT2 LAR term is "LMOD", which is calculated by the RIIO-1 Legacy PCFM on an annual basis. The LMOD term calculates an appropriate revenue adjustment for a future year, given a set of changes in historical years. MOD has been calculated annually as part of the AIP, and we continue to calculate it for the first two years of RIIO-2 (as it reflects changes on a two-year lagged basis).

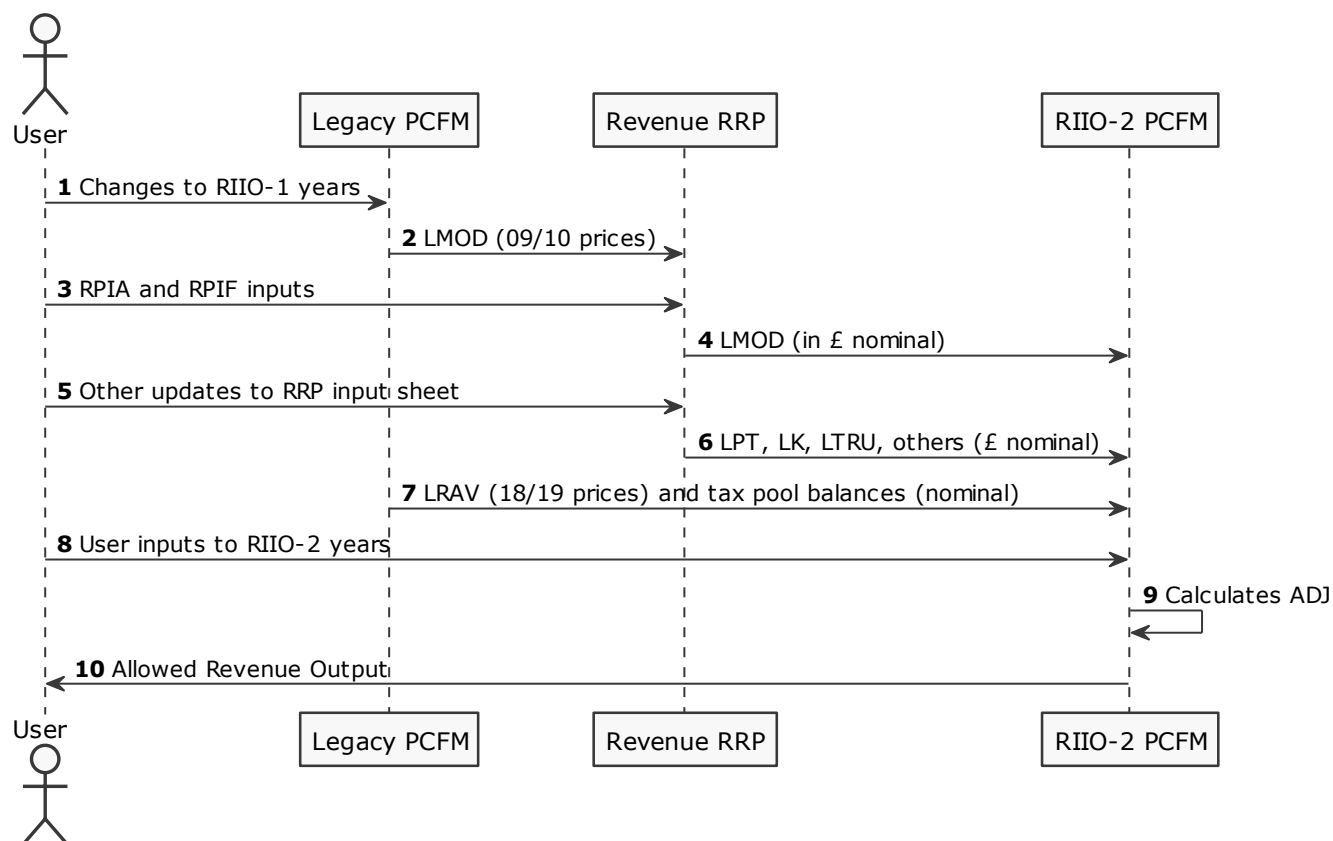
2.6. In the typical RIIO-1 process, the MOD term only reflects changes to pre-defined "variable values", and other values remain fixed through the price control. However, in the context of RIIO-GT1 closeout, we have decided to broaden the scope of values which may be modified or to add new calculations, if required, and then to extend the function of the MOD term to capture the effect of RIIO-GT1 closeout. We describe this closeout model as the GD1 Legacy PCFM. The steps of this process are as follows.

- In calculating adjustments, we will apply the methodologies set out in this decision document.
- Through Legacy PCFM working groups, and ultimately a statutory consultation on the GT2 Price Control Financial Handbook, Ofgem will propose specific implementations of these methodologies in the GT1 Legacy PCFM.
- The GT1 Legacy PCFM is now not a licence instrument, but a regulatory tool to provide the inputs to the RIIO-2 values, specifically the LMOD term

2.7. For illustration, Figure 1 is a sequence diagram, showing how the GT1 Legacy PCFM, the extended GT1 Revenue Regulatory Reporting Pack (Revenue RRP), and RIIO-GT2 PCFM interact and produce an allowed revenue value for the next regulatory year. Figure 1 should be read from top to bottom (the steps are numbered), while the arrows show where components come from and feed into. Each step is briefly summarised below.

1. Ofgem or the licensee will input changes to RIIO-1 values in the GT1 Legacy PCFM.
2. The GT1 Legacy PCFM is used to calculate LMOD value(s), which is then input into the Revenue RRP.
3. Inflation assumptions are input by the licensee into the Revenue RRP.
4. The Revenue RRP provides the LMOD value in £m nominal and is then input to the RIIO-2 PCFM.
5. Other inputs to the Revenue RRP are filled in by the licensee.
6. The remaining legacy values are input to the RIIO-2 PCFM, completing the 'LAR' input block for the corresponding year.
7. Legacy RAV additions are input from the GT1 Legacy PCFM to the RIIO-2 PCFM, after being converted to 18/19 prices.
8. The licensee updates all other variable values in the RIIO-2 PCFM.
9. The RIIO-2 model calculates the ADJ term for the following year.
10. The RIIO-2 model provides the licensee an Allowed Revenue value for the following year.

Figure 1: Sequence Diagram of the RIIO-2 AIP with Legacy Adjustments



Methodology proposed at consultation

2.8. We proposed to implement closeout methodologies via the GT1 Legacy PCFM by revising “yellow box” (non-variable) values as well as variable values or modifying the GT1 Legacy PCFM as necessary.

2.9. We proposed to implement the GT1 closeout methodologies in the November 2022 AIP, noting that corrections can be made in subsequent AIPs as necessary.

2.10. We proposed that rather than the cumulative impact of all changes being included in the next MOD value, the impact of the November 2022 AIP legacy adjustment is smoothed over the remaining three years of RIIO-2 by dividing the LMOD value by three.

Consultation responses

2.11. NGGT generally agreed with the proposed approach to the financial methodologies, however it queried our proposal to smooth the legacy adjustment over the first three years of RIIO-GT2.

2.12. NGGT's assumption was that networks could choose to make the legacy adjustment over one year or smooth over more years to reduce the impact on the consumer and proposed that it should have discretion to choose an appropriate legacy adjustment period.

Closeout methodology Decision

2.13. Our Decision is to implement the approach to financial methodologies that we consulted on do so through the GT1 Legacy PCFM in the November AIP. We consider this approach to be transparent, straightforward, and proportionate for both NGGT and consumers.

2.14. We are using the GT1 Legacy PCFM and existing RIIO-1 reporting packs as tools to calculate the correct closeout true-up. We consider this is an appropriate approach as they contain the full history of data from the RIIO-GT1 price control and using them as legacy calculation models would ensure that we calculate adjustments in a way that is transparent and correct.

2.15. We will engage with NGGT through the GT1 Legacy PCFM working groups to agree on the specific adjustments needed to the yellow box and blue box variables in the GD1 Legacy PCFM and the updates required to the Revenue RRP. Following this working group engagement, we will consult on the modified GT1 Legacy PCFM and legacy Revenue RRP.

2.16. We acknowledge the request that NGGT has flexibility in how it apportions adjustments in order to smooth the bill impact on consumers. Our decision is that the default position for closeout adjustments is to spread them out over the remaining three years of RIIO-GT2, because we think this is the most appropriate balance between current and future consumers, whilst minimising any impact on bills. However, it is possible that during the implementation of closeout, Ofgem may be persuaded that a different time period should be used if there is a compelling reason to do so.

3. Pipeline Diversions

This section details our Decision on the methodology and process we will follow to close out RIIO-GT1 Pipeline Diversions.

Background

3.1. Pipeline Diversion costs are those incurred by NGGT in relation to extant liabilities or other obligations to divert existing pipelines. These are costs incurred as a result of existing obligations/liabilities taken on by the Gas Council/ British Gas, for which NGGT is now responsible, and where NGGT can demonstrate it has done everything in its powers to recover costs from the relevant party requesting the pipeline diversion.

3.2. Due to the uncertain nature of this work no baseline allowance was provided at Final Proposals and we stated that work would instead be funded through an uncertainty mechanism.⁶

3.3. NGGT did not trigger the Pipeline Diversion re-opener during RIIO-GT1 and therefore received no allowances for pipeline diversion work, however assessment of previous annual reports demonstrates that it did incur costs in this area during the price control.

Methodology proposed at consultation

3.4. If the costs incurred are material⁷, we proposed a licence modification to enable an upward revenue adjustment to true-up all efficiently incurred costs.

3.5. If the costs incurred are immaterial, we proposed that we make no revenue adjustment, and that the expenditure is treated as totex and subject to the Totex Incentive Mechanism (TIM) sharing factor.

Consultation responses

⁶ National Grid Gas Plc (NTS) Gas Transporter Licence Special Conditions, 5E, p149-153.

⁷ NGGT materiality threshold is 1 per cent of average annual forecast revenue after the application of the totex efficiency incentive rate (RIIO-GT1 Final Proposals, Overview, para 4.48)

3.6. NGGT agreed with the proposed Pipeline Diversions methodology, however it requested clarity around any further information required from Ofgem to implement the closeout methodology.

3.7. NGGT also confirmed that all projects delivered under legacy pipeline diversions in RIIO-GT1 have been completed and that there will be no further expenditure in RIIO-GT2 in relation to these.

Closeout methodology Decision

3.8. Ofgem will implement the methodology proposed in the RIIO-GT1 closeout consultation without modification⁸. We consider it appropriate that NGGT is not exposed to material pipeline diversion costs for which it has not received an allowance, and that consumers do not fund immaterial costs where there is no provision in the licence to do so.

3.9. Ofgem considers the information already submitted by NGGT in its 2020/21 Regulatory Reporting Pack (RRP) submission will be sufficient to enable us to undertake an assessment of NGGT's pipeline diversion expenditure. However, if any additional information is required, Ofgem will engage with NGGT as necessary ahead of the 2022 AIP.

⁸ [RIIO-GT1 Closeout Consultation, pg. 14, para 3.5 – 3.8](#)

4. South West Quadrant

This section details our Decision on the methodology and process we will follow to close out the RIIO-GT1 South West Quadrant incremental capacity project.

Background

4.1. At Final Proposals we allowed NGGT baseline funding to deliver an incremental capacity project in the South West Quadrant⁹ that had been signalled ahead of the price control. However, the project was cancelled prior to construction with no costs incurred.

4.2. The forecast capital expenditure for this project was added to NGGT's RAV and NGGT has made returns on this project throughout RIIO-GT1. NGGT has committed to returning the allowance and any unearned RAV returns in relation to the South West Quadrant project to consumers in full.

Methodology proposed at consultation

4.3. We proposed adjusting the allowance values reflected in the Legacy PCFM to show that no expenditure was incurred by NGGT in relation to this project. These values are shown in cells AH265:AN266 of the NGGT TO sheet of the GT1 Legacy PCFM and will be replaced by zero.

4.4. The adjustment automatically corrects the RAV and base revenue values for the RIIO-GT1 period and feeds through to the RIIO-GT2 LRAV and LMOD variable values.

4.5. We also proposed that a similar adjustment be made to remove the revenue relating to the South West Quadrant project that was still reflected in the Legacy PCFM at the end of the RIIO-GT1 price control period.

Consultation responses

4.6. NGGT agreed with the proposed methodology for the South West Quadrant project.

⁹ [RIIO-GT1 Final Proposals, Cost assessment & uncertainty Annex](#), para 7.65

4.7. NGGT added that it has calculated the revenue impact within the Legacy PCFM and included the value in LMOD2 for the November 2021 AIP.

4.8. NGGT also requested that Ofgem confirm how deductions will be shown in the RIIO-GT2 PCFM as the RIIO-1 LRAV numbers are hard coded numbers.

Closeout methodology Decision

4.9. Ofgem will implement the methodology proposed in the RIIO-GT1 closeout consultation without modification¹⁰. We consider it appropriate that all allowances and revenues associated with this cancelled project are returned to consumers in full.

4.10. Regarding NGGT's point about adjusting hard-coded numbers in paragraph 4.8 above, as the Legacy PCFM has now been superseded by the RIIO-GT2 PCFM and is now only being used as an instrument to closeout RIIO-GT1, there is now nothing preventing the modification of RIIO-1 LRAV numbers.

4.11. We will engage with NGGT at the Legacy PCFM working groups and detail the process for making deductions through the Legacy PCFM, which will then be implemented at the November 2022 AIP.

¹⁰ [RIIO-GT1 Closeout Consultation, pg. 15, para 4.3 – 4.7](#)

5. Enhanced Physical Site Security (PSUP)

This section details our Decision on the methodology and process we will follow to close out the RIIO-GT1 Physical Security Upgrade Programme.

Background

5.1. As part of the government’s Physical Security Upgrade Programme (PSUP), networks are required to implement physical security enhancements at sites listed as Critical National Infrastructure (CNI). The Department for Business, Energy and Industrial Strategy (BEIS) determines which sites require upgrades, and the design specification at each site must meet the requirements of the Centre for the Protection of National Infrastructure (CPNI)¹¹.

5.2. PSUP is a cross-sector programme. At RIIO-GT1 Final Proposals network companies were provided baseline funding for known PSUP projects, and PSUP outputs and allowances were adjusted following re-openers in 2015 and 2018. However, Special Condition 3F of the GT1 Licence made no explicit provision to either (i) true up immaterial costs, or (ii) make allowance adjustments for material costs as part of RIIO-GT1 closeout.

Methodology proposed at consultation

5.3. If NGGT incurred efficient costs in excess of the RIIO-GT1 materiality threshold for which it was not funded, or if NGGT has been funded a material amount to deliver projects that were later cancelled, Ofgem proposed a licence modification to enable an allowance adjustment to true up those net costs.

5.4. If the net costs incurred or avoided by NGGT fall beneath the materiality threshold, we proposed that there is no revenue adjustment made at closeout and that expenditure is treated as totex and subject to the TIM sharing factor.

Consultation responses

¹¹ [Centre for the Protection of National Infrastructure | CPNI](#)

5.5. NGGT agreed with the proposed PSUP methodology, however it sought clarification around what information it was required to submit in order for Ofgem to complete our closeout assessment.

5.6. NGGT enquired as to whether the proposed Tech Audit(s) for completed sites would need to be provided for all PSUP sites delivered in RIIO-GT1 or only for the sites where the completion has been delayed into RIIO-GT2. Additionally, NGGT requested clarification from Ofgem regarding at which stage of the project they would need to submit the audits.

5.7. NGGT sought clarity on whether it would need to submit any further information regarding the list of CNI sites above and beyond what it provided as part of the May 2015 and May 2018 reopeners¹².

5.8. NGGT also requested that language in paragraph 5.10 of the PSUP proposed methodology in the closeout consultation be changed to *"We propose that incurred costs in RIIO-GT2 are to be reported as a specific project under the PSUP cost category as non-load capex in RIIO-GT2 RRs and treated as totex, therefore all RIIO-GT2 expenditure will be subject to the TIM"*, similar to the Peterborough and Huntingdon compressor closeout methodologies.

Closeout methodology Decision

5.9. We will implement the closeout methodology for PSUP as consulted on without modification. We consider it appropriate that NGGT is not exposed to material PSUP costs for which it has not received an allowance, and that if consumers have funded material costs for projects that were cancelled this money is returned to them.

5.10. For projects funded in RIIO-GT1 that will be completed in RIIO-GT2 we expect NGGT to submit a Tech Audit upon project completion. For projects completed in RIIO-GT1, Ofgem considers that it already has enough information in the 2020/21 RRP submission to complete our assessment and there is no requirement to submit a Tech Audit in relation to these projects.

5.11. Ofgem confirms that NGGT is not required to submit any additional information above that submitted in its 2015 and 2018 re-opener submissions in relation to the CNI list.

If any further information is required to complete any part of the PSUP closeout assessment Ofgem will engage with NGGT and request this at the closeout implementation stage.

5.12. Costs incurred in RIIO-GT2 in relation to RIIO-GT1 projects are to be reported as a specific cost line under the PSUP cost category as 'Other Capex' in RIIO-GT2 RRs and treated as totex. Therefore all expenditure will be subject to the TIM. No additional allowance will be provided in RIIO-GT2 in relation to projects funded in RIIO-GT1.

6. Peterborough and Huntingdon compressors

This section details our decision on the methodology and process we will follow to close out the RIIO-GT1 Peterborough and Huntingdon compressor projects.

Background

6.1. At Final Proposals, Ofgem set ex-ante baseline funding for Peterborough, Huntingdon and Aylesbury compressor sites to achieve compressor emissions compliance with Integrated Pollution and Prevention Control Directive (IPPCD)¹³ Phase 3 and Industrial Emissions Directive (IED)¹⁴ phase 1¹⁵.

6.2. These projects were originally due to be delivered in 2020. Although the project at Aylesbury has been completed, the completion of the Peterborough and Huntingdon projects was impacted by Covid and issues with the Main Works Contractor (MWC). These projects must be completed by 2023 in line with emissions compliance requirements and are currently forecast for completion in late 2022.

6.3. NGGT has committed to delivering these projects in RIIO-GT2 from its existing totex allowances and has not requested any additional funding at close out for either RIIO-GT1 costs incurred in excess of the allowance or for RIIO-GT2 forecast costs to project completion.

Methodology proposed at consultation

6.4. Ofgem did not propose to adjust allowances for these projects in response to any challenges NGGT has encountered in delivering the work in RIIO-GT1, and proposed that any RIIO-GT1 allowance overspend is treated as totex and subject to the TIM.

6.5. We proposed to consider the outputs delivered upon commissioning of each compressor unit, with NGGT to provide a copy of the commissioning certificate at RIIO-GT2 closeout.

¹³ [IPCC Directive](#)

¹⁴ [Industrial Emissions Directive](#)

¹⁵ [RIIO-T1: Final Proposals for NGET and NGGT – Cost assessment and uncertainty](#), p98, 7.93-7.95

6.6. We proposed a licence modification to attach a Price Control Deliverable (PCD) to these projects in NGGT's GT2 Licence to ensure that, if the projects are not delivered to specification, consumers are not exposed to the cost of non-delivery.

6.7. We proposed that incurred costs in RIIO-GT2 are to be reported as specific projects under the compressor emissions cost category as non-load capex in RIIO-GT2 RRs and treated as totex, therefore all RIIO-GT2 expenditure will be subject to the TIM.

Consultation responses

6.8. NGGT agreed with the proposed methodology for the Peterborough & Huntingdon compressors.

6.9. NGGT sought clarity on whether the proposed PCD would mean a new Special Condition in the GT2 Licence or if the projects would be added to Special Condition 3.11 (Compressor emissions Re-opener and Price Control Deliverable).

6.10. NGGT also stated that *'as this PCD will not adjust any allowances (paragraph 6.6), we would like further clarity from a PCFM point of view, if Ofgem are proposing to include a line in the PCFM with the other PCD projects, but with zero allowances for consistency'*

Closeout methodology Decision

6.11. Following consideration of the consultation response we are making a slight change to the methodology to closeout the Peterborough and Huntingdon compressors that was consulted on. The policy intention remains the same, however rather than making the delivery of this project a PCD in the licence, we are instead adding it to the licence as a specific output that NGGT must deliver.

6.12. PCDs in RIIO-GT2 must adhere to the provisions contained within Special Condition 9.3 and the PCD Reporting Requirements and Methodology Document¹⁶. The document states that in the event a PCD is not delivered "we will reduce allowances by the entire amount associated with the PCD less efficient costs of undertaking reasonable and

¹⁶ [Price Control Deliverable Reporting Requirements and Methodology Document | Ofgem](#)

necessary work up to the point of cancellation”, with any allowance adjustment based on the formula:

*Adjustment to allowances = (1 – Proportion of output delivered) * ex-ante allowance.*¹⁷

6.13. However, as this project was funded in RIIO-GT1 and the ex-ante allowance in RIIO-GT2 is zero, this effectively means that no allowance adjustment could be made in the event NGGT does not deliver the project to the funded specification.

6.14. Therefore, to make provision for an allowance adjustment we either have to modify the PCD Reporting Requirements and Methodology Document and change the adjustment formula in 6.12 above or include this project in NGGT’s licence as an output rather than a PCD. We consider that as reporting on this project through the RRP gives us sufficient oversight of its delivery, and we do not require enhanced PCD reporting, that adding it as an output rather than a PCD is more appropriate.

6.15. For the avoidance of doubt, paragraph 6.6 of the consultation document stated that no allowance adjustment would be made *‘in response to the challenges NGGT has encountered delivering the work’* in RIIO-GT1, not that no allowance adjustment would be made for failing to deliver the project as funded. We will use the GT2 Licence to reserve the right to clawback allowances at RIIO-GT2 closeout in the event these delayed RIIO-GT1 projects are not delivered, or not delivered to the funded specification, in RIIO-GT2.

6.16. We will consult on adding a special condition to NGGT’s licence that makes provision to assess delivery of this project at RIIO-GT2 closeout. If the project is not delivered, or not delivered to the funded specification, we will also include provision for an adjustment to NGGT’s RIIO-GT2 totex allowance not in excess of the allowance NGGT received for the project in RIIO-GT1.

6.17. We will add a new line to the RIIO-GT2 PCFM (“PHCt” – Peterborough Huntingdon compressor term) for this project showing zero allowances, and any allowance adjustment required following assessment of the project in accordance with 6.16 will be reflected by directing a negative value to this term, smoothed evenly over the five years of RIIO-GT2.

¹⁷ [PCD Reporting Requirements and Methodology Document](#) Paragraph 5.4(1)

6.18. We will engage with NGGT on the specific drafting of this output then consult formally on implementing it in NGGT's licence at the earliest appropriate time.

6.19. NGGT is to report expenditure for Peterborough and Huntingdon as specific projects in the RIIO-GT2 RRs, reported under the compressor emissions cost category as non-load capex.

6.20. All RIIO-GT2 expenditure on these projects will be treated as totex and be subject to the RIIO-GT2 TIM.

7. Hatton compressor

This section details our decision on the methodology and process we will follow to close out the RIIO-GT1 Hatton compressor project.

Background

7.1. The Industrial Emissions Directive (IED) is one of three main Directives influencing NGGT's compressor emissions. Under this directive NGGT were required to decommission two IED non-compliant RB211 compressor units at Hatton.

7.2. In its RIIO-GT2 Business Plan submission, NGGT requested funding for the full project costs including Front-End Engineering Design (FEED). However, it forecast some initial spend in RIIO-GT1 to develop the project, with the actual construction costs then going into RIIO-GT2¹⁸.

7.3. At RIIO-GT2 Final Determinations we set NGGT an allowance of £74.51m to replace one compressor unit at Hatton to achieve compliance with IED legislation, which included £5.38m for Year 8 in RIIO-GT1 for project development costs. To date, NGGT has received no allowance to deliver the RIIO-GT1 element of this work.

Methodology proposed at consultation

7.4. Ofgem proposed to give effect to our RIIO-GT2 Final Determinations decision and increase NGGT's RIIO-GT1 allowance by £5.38m¹⁹ to cover project development costs already incurred.

7.5. We proposed that we would adjust the PCFM Variable Value 'IAEIE' (Uncertain costs – Industrial Emissions) in the GT1 Legacy PCFM and re-run the legacy PCFM to calculate revised LMOD and LRAV variable values, which then feed into the RIIO-GT2 PCFM per the process described in Chapter 2 of the consultation²⁰ document.

¹⁸ [Our decision on National Grid Gas Transmission's compressor investment needs case at St Fergus and Hatton](#)

¹⁹ This is the figure published in RIIO-GT2 Final Determinations, and is therefore in the 2018/19 price base.

²⁰ [Consultation on the closeout methodologies for RIIO-GT1](#), page 21, para 7.11

7.6. We proposed that when assessing the RIIO-GT2 PCD we will assess the delivery of the whole project, making any adjustment as necessary to account for the costs provided for at RIIO-GT1 closeout.

7.7. We also proposed that any over- or under-spend against the 2020/21 RIIO-GT1 allowance is treated as totex and subject to the TIM sharing factor.

Consultation responses

7.8. NGGT agreed with the proposed methodology for the Hatton compressor project.

Closeout methodology Decision

7.9. Ofgem will implement the methodology proposed at consultation without modification. This decision gives effect to our Decision on the Hatton compressor project at RIIO-GT2 Final Determinations.²¹

²¹ [RIIO-2 Final Determinations, NGGT Annex REVISED](#), para 3.48

8. Disposals

This section details our decision on the methodology and process we will follow to close out RIIO-GT1 disposals.

Background

8.1. When a licensee sells an asset that was originally funded by consumers, we think the proceeds of that asset sale should be passed to consumers.

8.2. Where network assets are no longer required, NGGT may dispose of such assets or relinquish operational control of them, subject to the consent of stakeholders (e.g., landowners). Some of these transactions may include the disposal of land.

Methodology proposed at consultation

8.3. We proposed that NGGT provide Ofgem with the details of any assets or land disposals that occurred in RIIO-GT1 so that Ofgem can undertake a light touch assessment of the disposal of any network assets to ensure the sale price reflects true market value.

8.4. We proposed that RAV is adjusted to reflect the net sale proceeds, entailing netting off the proceeds of disposals from RAV additions, with tax implications also considered using the following formula for the true-up:

$$\text{True-up value} = (\text{proceeds of disposal} - \text{cost of disposal}) \times (1 - \text{tax rate})$$

8.5. We proposed that any disposals will be included within the year the disposal took place, thus considering the time value of money. This would remove any residual asset value from the RAV.

Consultation responses

8.6. NGGT agreed with the proposed methodology for disposals.

8.7. NGGT sought clarity on what information Ofgem would need to complete its assessment, and how Ofgem will show net off the proceeds of disposals and show deductions in the RIIO-GT2 PCFM given the RIIO-1 LRAV are hardcoded numbers.

Closeout methodology Decision

8.8. We will implement the methodology for closing out disposals as consulted on. We consider it appropriate that the proceeds of asset sales are returned to consumers.

8.9. Ofgem considers that it already has the information required in NGGT's 2020/21 RRP submission to undertake the assessment, however we will engage with NGGT if any additional information is required at the closeout implementation stage.

8.10. The RIIO-GT1 LRAV values that feed into the RIIO-2 PCFM are "blue box" variable values that we will modify based on changes to the Legacy PCFM. We will engage with NGGT at the PCFM working groups and detail the mechanical process to make adjustments through the PCFM, which will then be implemented at the November 2022 AIP.

9. Next steps

9.1. Ofgem will engage with NGGT as necessary to implement the closeout methodologies and effect any necessary revenue adjustments as part of the November 2022 AIP. Specifically, we will:

- Consult via working groups on which values or rows in the PCFM to modify to effect the closeout methodologies, and prepare a reconciliation workbook from the final published RIIO-GT1 PCFM (2019) to the final closeout GT1 Legacy PCFM.
- Consult via working groups on modifications to the GT1 Legacy PCFM to allow the phasing of the LMOD term.
- Describe the modifications and updates in the GT2 Price Control Financial Handbook, via statutory consultation.

9.2. NGGT has already submitted its 2020/2021 RRP. Ofgem expects that this information will be sufficient to enable us to undertake a robust assessment of NGGT's RIIO-GT1 performance and determine the extent of any over or underperformance against its targets and allowances. If any additional information is required Ofgem will engage with NGGT and request this as necessary at the closeout implementation stage.

9.3. We will consult separately outside of the closeout process on the licence modification required to give effect to the Peterborough and Huntingdon compressors closeout methodology and intend to make the necessary licence modification ahead of the November 2022 AIP.