Decision

Decision on the closeout methodologies for RIIO-ET1

Subject	**RIIO-ET1 closeout**
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The RIIO[1]-1 electricity transmission price control ran from 1 April 2013 to 31 March 2021. This document provides the detail of the methodologies and funding mechanisms that will be used for the price control closeout. These methodologies will be included in the RIIO-ET2 Financial Handbook.

We[2] consulted on 31 January 2022. This document sets out our decisions following this consultation. We have published the non-confidential consultation responses alongside this document.

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[1] RIIO stands for "Revenue = Incentives + Innovation + Outputs".
[2] The terms 'we', 'us', 'our' refer to the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.

Contents

Executive summary

The RIIO-1 electricity transmission ('RIIO-ET1') price control ran from 1 April 2013 until 31 March 2021 (an eight year period). The RIIO-ET1 electricity transmission licence (the 'T1 Licence') makes provision in relation to several areas which, due to their uncertain nature, could only be settled once all costs and/or outputs are known or can be forecast with sufficient accuracy. This means that some elements of the price control need to be subject to "closeout" once the price control has ended and all the relevant information is available (eg. actual costs incurred or outputs delivered).

For the purposes of closeout, the following need to be addressed:

- Financial methodologies
- Sole Use Entry and Exit Connections and Directly Allowed Revenue Terms (DARTS)
- Transmission Provisions Wider Works (TPWW) claims
- Customer terminated connection projects
- Treatment of land costs associated with the North London Reinforcement Project
- Preconstruction project spend
- 'Crossover' volume driver projects where funding provision is made in related RIIO-ET1 volume driver mechanisms
- Generation connection volume driver 'clawback'
- Adjustments for Enhanced Physical Site Security
- Financial proceeds from the disposal of assets and land
- RIIO-ET1 Visual Impact of Scottish Transmission Assets (VISTA) projects

We are also confirming an approach to provide funding for 'crossover' projects, where the delivery of outputs is expected in RIIO-ET2 or beyond and for which the RIIO-ET1 price control provided no allowances for spend incurred in the RIIO-ET1 period.

This document provides a summary of each area of the price control where a closeout methodology or funding mechanism 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 / funding mechanism. The final closeout methodologies will be included in the RIIO-ET2 Price Control Financial Handbook.

Related documents

RIIO-T1 Strategy Decision,
https://www.ofgem.gov.uk/publications/decision-strategy-next-transmission-price-control-riio-t1

RIIO-T1 Final Proposals for Scottish Power (SPT) and Scottish Hydro Electric Transmission (SHET)
https://www.ofgem.gov.uk/publications/riio-t1-final-proposals-sp-transmission-ltd-and-scottish-hydro-electric-transmission-ltd

RIIO-T1 Final Proposals for National Grid Electricity Transmission (NGET)
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

RIIO-ET1 Price Control Financial Handbook
https://www.ofgem.gov.uk/sites/default/files/docs/2017/08/et1_handbook_-_v2.0.pdf

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

RIIO-ET2 Financial Instruments
Notice of proposed modifications to the Regulatory Instructions and Guidance and Regulatory Reporting Packs for RIIO-2 | Ofgem
and
Proposed direction to make modifications to the ESO and ET2 Price Control Financial Instruments | Ofgem

1. Background and overview

Background

1.1. The RIIO-ET1 price control sets the outputs that the three onshore electricity transmission network owners (ETOs)[3] must deliver, and the revenues each is allowed to collect from customers, between 1 April 2013 and 31 March 2021.

1.2. The RIIO-ET1 price control includes several areas of allowed expenditure that require information on the actual efficient costs incurred, revenue received and/or the output delivered before they can be settled. These are compared with the allowed costs, revenues and/or outputs targets that were incorporated in the modelling of the RIIO-ET1 Final Proposals (FP)[4].

1.3. We have not included closeout of the Network Output Measures (NOMs) in this Decision; NOMs is being consulted on separately due to its cross-sector scope.[5]

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 ET1 closeout

Area	Description	Chapter
Sole Use Entry and Exit Connections	A "true-up" to reconcile the difference between payments received by each of the ETOs across RIIO-ET1 and the assumptions made when establishing the baseline allowance at the start of the price control period.	3
Directly Allowed Revenue Terms (DARTS)	A true-up to reconcile the difference between the actual income received across RIIO-ET1 and the assumptions made when establishing the total allowed revenue to be recovered from annual charges at the start of the price control period.	3

[3] Scottish Power (SPT), Scottish Hydro Electric Transmission (SHET) and National Grid Electricity Transmission (NGET).
[4] And following any subsequent re-opener Decisions and the Mid Period Review.
[5] NOMs Closeout Submission Instructions Guidance (May 21) and Direction to changes to the NOMs Incentive Methodology (June 21) have already been published.

Transmission Provisions Wider Works (TPWW) claims	An adjustment to NGET's TPWW licence term to recover costs efficiently incurred in boundary capacity projects, which are no longer required due to a change of external conditions.	4
Treatment of land costs associated with the North London Reinforcement Project	Return to consumers of any financial gains that NGET has derived from land ownership in relation to the North London Reinforcement project (whether through leasing out or sales).	4
Enhanced Physical Site Security	An adjustment to allowances to reflect updated needs cases for the programme of work to enhance physical security at specific sites, as required by the UK government as part of the Physical Security Upgrade Programme (PSUP).	5
Customer terminated projects	Adjustment to recover costs efficiently incurred on investments for terminated connection works net of settlement of the termination payments received from users within the RIIO-ET1 price control period.	6
Settlement of allowances for pre-construction work	An adjustment to reflect the difference between the actual costs incurred and the value of fixed allowances associated with the delivery (or non-delivery) of RIIO-ET1 pre-construction activities related to 'named' outputs specified in the T1 Licence.	7
Financial proceeds from disposals	An adjustment to net off any cash proceeds through assets disposal from additions to Regulated Asset Value (RAV) from the year in which they occur.	8
'Crossover' volume driver projects	An adjustment to the funding for connection projects whose output delivery is expected in the first two years of T2 and where an automatic trigger exists to adjust allowances through an extension of the T1 volume driver.	9
'Crossover' projects without a volume driver to fund costs incurred during the RIIO-ET1 period.	An approach to provide the funding for crossover projects that are not subject to adjustment through the T1 volume driver arrangements and where our T2 process has already assessed the need and total costs of the project.[6]	10
Generation connection volume driver 'clawback'	The output delivered under SPT's T1 volume driver mechanism is significantly lower than the agreed baseline threshold. A clawback of allowance is therefore required to replicate the operation of the volume driver mechanism in the opposite direction.	11

[6] The preconstruction costs associated with these investments will be allocated against existing RIIO-ET1 allowances.

RIIO-ET1 Visual Impact of Scottish Transmission Assets (VISTA) policy	An adjustment to SHET's RIIO-ET1 allowed expenditure to fund the agreed costs it has incurred on the projects in 2020/21, in accordance with the published directions.	12
NOMs	Consulted on separately due to cross-sector scope	N/A

1.5. The document also confirms:

- areas of the price control where no closeout process is required. This includes the Western HVDC link joint venture project (chapter 13) and the treatment of innovation allowances (chapter 14).

- areas of the price control that were not included as part of the original consultation but based on consideration of the responses received, require a decision on how to proceed. These areas are set out in chapter 15.

RIIO-ET1 Closeout

1.6. On 31 January 2022 we consulted on our proposed methodologies / funding mechanism for closeout of each of the elements of the RIIO-ET1 price control.[7] The finalised methodologies detailed in this Decision document will be incorporated into the RIIO-2 Price Control Financial Handbook (PCFH). We will consult on amendments to the PCFM and final revenue adjustments ahead of the November 2022 Annual Iteration Process.

1.7. Our Decision on the RIIO-ET1 closeout methodologies includes: mechanisms that "true-up" and reconcile actual expenditure against services provided by the ETOs, output mechanisms which enable us to recover funds from ETOs in the case of non-delivery of 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.

[7] Consultation on the closeout methodologies for RIIO-ET1 | Ofgem hereafter referred to as the January 2022 consultation.

1.8. We have based the proposed RIIO-ET1 closeout methodologies on the approach and principles we set out in the RIIO-T1 Strategy Decision[8], Final Proposals for SPT and SHET[9], Final Proposals for NGET[10], relevant supplementary documents, and Price Control Financial Handbook. We have also considered elements of the RIIO-ET2 Final Determinations where appropriate.

Purpose of this document

1.9. This document sets out the background to relevant elements of the RIIO-ET1 price control, detail of any changes we have made to the methodologies / funding mechanisms following the consultation, and the finalised RIIO-ET1 closeout methodologies / funding mechanisms.

Responses to the RIIO-ET1 closeout consultation

1.1. We received three responses to the consultation, which we have carefully considered when reaching our Decision. All respondents gave comments on specific elements of the proposed methodologies. The network companies all provided views on the overarching approach, as well as very specific comments.

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 the non-confidential responses on our website alongside this Decision.

Next steps

1.11. All network companies will be required to submit a final 'performance assessment submission' to confirm the value of the closeout adjustment to be made and to provide further information to explain and justify their performance in each closeout area.

1.12. We request that a final performance assessment submission (data template and accompanying narrative) from each company is received on or before 4 July 2022.

[8] RIIO-ET1 Strategy Decision
[9] RIIO-ET1 Final Proposals
[10] RIIO-ET1 Final Proposals

1.13. Based on our assessment of the information and further engagement with the network companies, we will implement the closeout methodologies and make any necessary revenue adjustments as part of the November 2022 Annual Iteration Process (AIP). Further details are in Chapter 2.

Your feedback

1.14. 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 eliska.antosova@ofgem.gov.uk.

2. Financial methodologies

This section describes the process which the Authority will follow in determining any revisions to the RIIO-2 RAV balances and revenue for the ET2 Price Control Period.

Background

2.1. To closeout TPCR4, the RIIO-ET1 model contained "legacy" adjustments to RAV (LRAV) and revenue (LAR) in the 2013/14 regulatory year. For NGET, the LAR value was spread over the 8 years of RIIO-ET1, while SHET and SPT had a one-off adjustment in 2013/14.

2.2. In contrast, the RIIO-T1 electricity transmission licence (the 'T1 Licence') introduced mechanisms that automatically true up revenue for outturn data on an annual basis. Therefore, the RIIO-ET2 Price Control Financial Model (PCFM) does not need the same catch-all legacy terms used for TPCR4 closeout. Instead, the LAR term is the sum of the pre-existing true-up mechanisms introduced in RIIO-ET1 (licence terms MOD, PT, TRU, for example).

2.3. Rather than make a one-off adjustment to RAV at the start of RIIO-ET2, we now import the final RIIO-ET1 values into the RIIO-ET2 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-ET1, rather than a one-off adjustment.

2.4. The revenue adjustment (LAR) in RIIO-ET2 is the sum of existing true-up mechanisms, which have been extended into RIIO-ET2 to cover the closeout of RIIO-ET1.

2.5. One component of the LAR term is "MOD", which is calculated by the RIIO-1 PCFM on an annual basis. The MOD 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-ET1 Annual Iteration Process (AIP), 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-ET1 closeout, we have decided to make use of the RIIO-1 PCFM, modified or with new calculations as required, and then extend the calculation of the MOD term to capture the effect of RIIO-ET1 closeout. We describe this closeout model as the ET1 Legacy PCFM.[11] The steps of this process are as follows.

- This Decision document sets out the methodology by which an adjustment will be calculated.
- Through PCFM working groups, and ultimately a statutory consultation on the ET2 Price Control Financial Handbook (PCFH), Ofgem will propose specific implementations of these methodologies in the ET1 Legacy PCFM.
- The ET1 Legacy PCFM is not a licence instrument, but a tool to provide the inputs to the RIIO-2 values, specifically the Legacy MOD ("LMOD") term.
- A phased set of Legacy MOD values will be entered into the RIIO-ET2 PCFM, for the methodologies to take financial effect.

2.7. For illustration, Figure 1 is a sequence diagram, showing how the ET1 Legacy PCFM, the extended ET1 Revenue Regulatory Reporting Pack (Revenue RRP), and RIIO-ET2 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. The steps we set out in the consultation are summarised below:

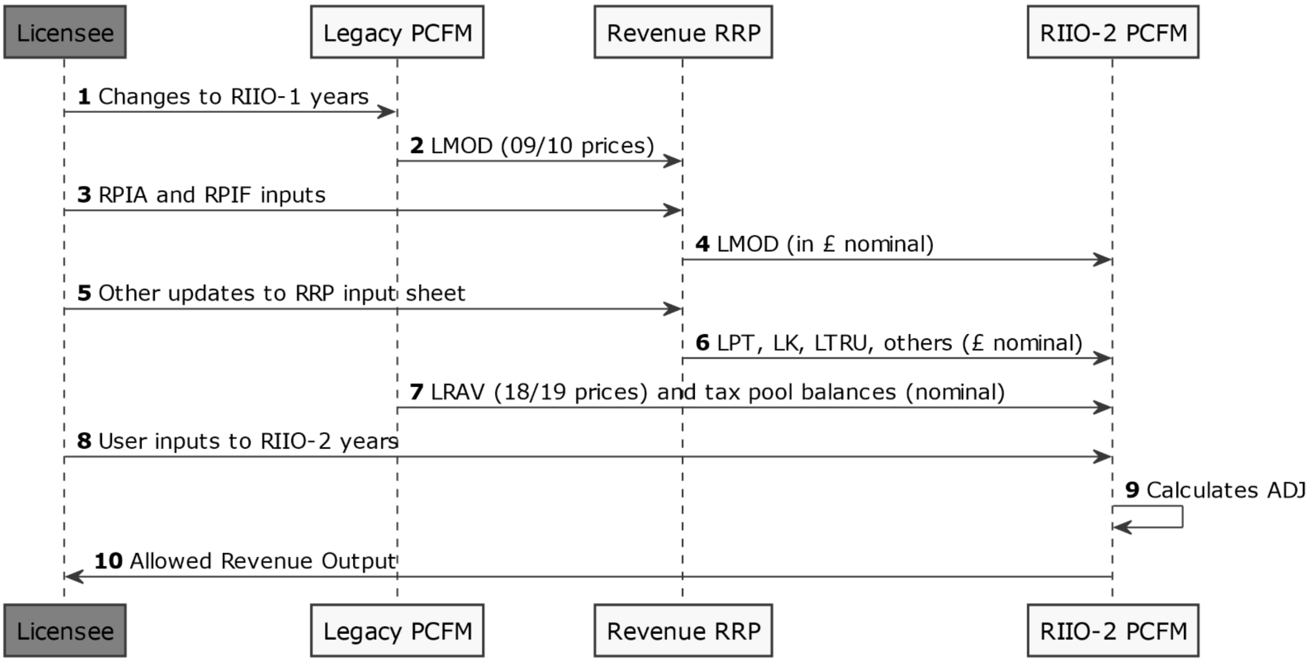
1. Ofgem or the licensee will input changes to RIIO-1 values in the ET1 Legacy PCFM.
2. The ET1 Legacy PCFM is used to calculate legacy MOD (LMOD) value(s), which is then input into the Revenue RRP.
3. Inflation assumptions are input by the licensee into the Revenue RRP.
4. The Revenue RRP provides the LMOD value in £m nominal, which is then input to the RIIO-ET2 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 legacy PCFM into 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.

[11] The ET2 PCFM already contains starting values based on a provisional Legacy PCFM that was extended to produce MOD terms for the first two years of RIIO-2, and some provisional modifications have been made. The ET1 closeout process aims to finalise the ET1 Legacy PCFM.

10. The RIIO-2 model provides the licensee an Allowed Revenue value for the following year.

2.8. This process is set out in the PCFH and the network licence special conditions.

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



Methodology proposed at consultation

2.9. We proposed to implement closeout methodologies via the Legacy PCFM by revising "yellow box" (non-variable) values as well as variable values or modifying the ET1 Legacy PCFM, where we will set out the required changes in the legacy chapter of the ET2 PCFH.

2.10. We proposed to implement the RIIO-ET1 closeout methodologies in the November 2022 AIP, noting that corrections can be made in subsequent AIPs if necessary.

2.11. As a result of the timescales associated with implementing aspects of the mechanical closeout adjustments, interim adjustments to the Legacy PCFM - to ensure routine updates to variable values continue to be made - were agreed and processed through the AIP in the period September to October and included in the November 2021 AIP. The process of implementing the closeout methodologies will finalise the adjustments to be made.

2.12. 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

2.13. All respondents agreed that the description of the process to implement RIIO-T1 closeout methodologies via the Legacy PCFM listed within the consultation (chapter 2, paragraph 2.7) matched their expectations of the process.

2.14. All respondents supported an approach to smooth the revenue impact of the closeout adjustments. Two respondents provided support for the proposed approach to phase the impact over the remaining three years of the T2 price control (2023/24 to 2025/26). The respondents' were of the understanding that the adjustment agreed and processed through the AIP process in November 2021 accounted for two years of revenue adjustment and the last three years of T2 will be considered for the remaining three fifths of the adjustment through the forthcoming AIP process.

2.15. One respondent did not agree with the proposal to phase the closeout impact over the remaining three years of RIIO-ET2. Instead, an alternative was proposed to phase the adjustment over the same time period in which the adjustments have built up, ie. an eight-year period. Under this approach the closeout adjustment will be phased over the remaining three years of RIIO-ET2 and five years of the next price control period. The respondent noted that the proposed approach offers an advantage of avoiding any differences to legacy treatment within a price control period.

2.16. The same respondent sought clarification on the way to phase the adjustment and the exact amendment required to the calculations, noting that different methods can be applied. It agreed that one way that the adjustment can be facilitated is by amending the 'Revenue' tab of the ET1 Legacy PCFM (to mirror the consultation document, paragraph 2.12 & 2.13) but highlighted that under the alternative eight-year approach noted above, row 32 of the 'Revenue' tab would require extending for a further eight years. A further alternative was also identified; to reflect the closeout adjustments within the ET1 Legacy PCFM as it currently stands and to compare the resulting 2022/23 MOD value to the 2022/23 MOD value from the ET1 Legacy PCFM as calculated during the November 2021 AIP. The delta between the two 2022/23 LMODs will provide the adjustment which would require phasing over future years.

2.17. A general query was raised by all respondents on whether the application of the closeout methodologies will result in adjustments to the existing values within the specified rows within the ET1 Legacy PCFM. Clarity was requested on whether adjustments will be made to existing values within the ET1 Legacy PCFM rather than an over-write and replacement of existing values.

2.18. One respondent commented on the sequencing of the process as listed in the consultation and proposed revisions to improve clarity and ensure consistency between the illustrative Figure 1 in the consultation and the descriptive steps listed. These include:

- Step 7: update to the tax pool balance to be included.
- Step 4: the November 2021 AIP does not include the functionality for the calculation of nominal LMOD values beyond 2022/23, and will therefore require updating.
- Step 9: description currently implies that changes to LRAV and LAR (which includes the LMOD term) would flow through ADJ, which is not correct. LAR forms part of Allowed Revenue but is outside of the Calculated Revenue term. As such any changes to previously set LAR values would affect Allowed Revenue and therefore would flow through K as an under- or over-recovery.

2.19. All respondents supported incorporating the final closeout methodologies in chapter 8 of the RIIO-ET2 PCFH, and some respondents suggested changes to the PCFH to accommodate the legacy process (ie. methodology). This included capturing features such as the smoothing principle and new terms required to capture any new adjustments proposed as part of the closeout decision.

2.20. One respondent noted a specific proposal (in paragraph 2.6 of the consultation paper) to make changes to values other than "variable values" to the RIIO-ET1 PCFM in developing the ET1 Legacy PCFM. The respondent requested that the forthcoming statutory consultation on changes to the RIIO-ET2 PCFH provide explanation on the processes to ensure the closeout adjustments work as intended.

Our views

2.21. We note that while all respondents were supportive of an approach to smooth the revenue impact of the closeout adjustments over a number of years, two respondents sought further clarification on the exact amendment and calculations required to apply the proposed five-year phasing calculation and one respondent did not support the proposal, suggesting an alternative approach to phase the adjustment over an eight-year period.

2.22. We wish to avoid unnecessary prolongation of true-ups into future price controls and keep the process as simple as possible, but only if doing so is in the best interests of customers. After further consideration of the views received, we will estimate the magnitude of the closeout adjustment before making a final decision on the phasing approach. Starting with a simple assumption of phasing over the remaining three years of RIIO-2, we will consider the financial impact and the overall profile of charges and determine whether an alternate arrangement is in customers' interests. We have therefore decided to delay our final decision on the duration of phasing the closeout impact until the statutory consultation.

2.23. We note that interim adjustments were processed through the AIP process in November 2021 that accounted for two years of a five year revenue adjustment. By finalising the values in the closeout process, it will account for the remaining value of the adjustment in the next calculated MOD value. The process will not double count any the adjustments already accounted for during the November 2021 AIP process, by virtue of maintaining the "recalculated base revenue" values from the November 2021 AIP in the legacy model.

2.24. In response to the request for clarification on the exact amendment required to the 'Revenue' tab of the ET1 Legacy PCFM (paragraph 2.16 above), we will make decisions on the final implementation through working groups. Specifically, the workbook and revenue tab needs at least one additional year added to the "year selector" to calculate an additional MOD value. It could be further modified to perform the phasing, or the working group could explore performing the phasing in the RIIO-2 model instead, such as taking a single input and dividing by three.

2.25. We can confirm that the adjustment process will revise the existing values within the ET1 Legacy PCFM (they are not an over-write as suggested in paragraph 2.17 above). ETOs are required to submit values in the 2009/10 price base to enable input to the PCFM. In a reporting workbook, the ETO will provide the 2019 position of the value and all applicable adjustments through pre-existing or closeout methodologies. The final position will be a simple sum of these values, which will then be input into the ET1 Legacy PCFM.

2.26. In relation to the specific sequencing points raised in paragraph 2.18, we agree with the points raised and have incorporated these into the description.

2.27. We consider that for the issue raised in paragraph 2.19 above – a request to incorporate the final closeout methodologies in the RIIO-ET2 PCFH - the best forum to discuss the appropriate modifications to the handbook would be at a PCFM working group where we can consider any additional details in full.

2.28. We will engage with ETOs at the PCFM working groups and detail the mechanistic process for accommodating closeout methodologies in the November 2022 AIP.

Closeout methodology Decision

2.29. We consider the general approach laid out in our consultation to be transparent, straightforward, and proportionate for both ETOs and consumers.

2.30. We will ensure a sufficiently robust assurance process is in place for all modifications and engage with the ETOs through the PCFM working groups to agree on the most straightforward way of implementing the detail of these methodologies. As a principle, we wish to balance a simple process with avoiding the maintenance of RIIO-1 legacy workbooks for many years into the future. We will engage either an internal or external audit of the modifications depending on the complexity and scale.

2.31. We have decided to proceed with the methodology as provided in Appendix 1 taking into account specific comments on the methodology.

3. Adjustments to true-up with connection payments

This section details our Decision on the methodology for closing out connection activity funded directly by the connecting customer. This process applies to all the electricity transmission network owners (ETOs).

Background

3.1. The efficient expenditure for delivering local enabling works[12] is funded directly by the connecting customer. This is through payment either over an agreed period or over the life of the asset, in accordance with the relevant charging methodology (see section 14 of the Connection and Use of System Code[13]).

3.2. An offer of connection will typically identify two types of work:

- transmission connection assets, which are installed solely for and only capable of use by an individual user ('sole use'). These costs are recovered by ETOs through a combination of up-front capital contributions and annual connection charges; and

- transmission infrastructure assets that cannot be solely attributed to an individual user (and are potentially shared by more than one user). These costs are recovered by ETOs through transmission network use of system charges after connection.

3.3. RIIO-ET1 baseline allowances were set on the assumption that each ETO would recover a certain amount through their customer connection activities between 1 April 2013 and 31 March 2021.

3.4. A process is required to ensure that any variance between the total payment received by each ETO across RIIO-ET1 and the assumptions made to establish the RIIO-ET1 baseline is trued up.

[12] These are the minimum transmission works that facilitate the connection of users seeking to export energy onto the onshore transmission system (entry) or take power from the onshore transmission system (exit).
[13] https://www.nationalgrideso.com/document/141131/download

Methodology proposed at consultation

3.5. We proposed an adjustment calculation to reconcile the difference between the actual income received by each of the ETOs across RIIO-ET1 and the assumptions taken when establishing the total allowed revenue to be recovered from annual charges at the start of the price control period.

3.6. We proposed two calculations:

i. A true-up between the forecast customer connection contributions (listed as negative capital expenditure) included in Baseline Load Related Allowed Expenditure and the actual contributions received for the investment categories relevant to "sole use entry" and "sole use exit" connection activity. The resultant profile would then be input to the ET1 Legacy PCFM (row 84).

ii. A true-up between assumed annual connection charges and the actual connection income received. The resultant profile would then be input to the ET1 Legacy PCFM (row 213).

Consultation responses

3.7. All respondents agreed in principle to the proposals in relation to the true-up calculation and process of financial revision to the RIIO-ET1 Legacy PCFM.

3.8. However, one respondent observed that the description of the true-up set out in the consultation (paragraph 3.7, bullet one) might be further clarified to reference 'sole use' capital expenditure, not simply contributions, to reflect more accurately how the original Baseline Allowances in the sole use investment category were set and the true-up required.[14]

3.9. All respondents agreed with the proposed approach to incorporate the review of sole use entry connections as part of closeout in RIIO-ET1 and to ensure that similar adjustment is made for exit connections.

[14] The baseline allowances included a forecast for capex to be incurred on sole use connection activity less a forecast for contributions expected to be received from customers across T1. A true-up is required to reflect the actual net capex incurred (and to reflect the removal of actual income received from total allowed revenue).

3.10. One respondent commented on the description of the calculation process as listed in the consultation (paragraph 3.8) and proposed condensing steps 4 to 6 and replacing them with a single step to "*update the current annual charges forecast values in the PCFM to the actuals for the RIIO-T1 period*". The respondent noted that its proposal produces the same effect as the process in steps 4 – 6 in Ofgem's consultation proposal but without the need for an additional step.

3.11. A separate respondent requested confirmation regarding the adjustment to the PCFM in row 84 (see Step 7 of the proposed methodology) and clarity that the process will revise the existing values within the ET1 Legacy PCFM, not over-write any total allowances already included in this row with the value of true-up adjustment only.

Our views

3.12. We note the support for each of the proposed true-up calculations and the proposal to incorporate the review of sole use entry connections.

3.13. In relation to the descriptive point raised in paragraph 3.8 above, we note that the process will seek to ensure ETOs' neutral performance in the delivery of connection activity and provide a clear line-of-sight between original baseline allowances and actual expenditure / revenues as a result of providing sole use connection assets during the RIIO-ET1 price control period.

3.14. We agree with the proposed simplification of the methodology description (paragraph 3.10 above) in relation to the true-up of annual charges. The methodology text has been amended accordingly.

3.15. In response to the request for clarification on the exact amendment required (paragraph 3.11 above), we confirm that row 84 will be overwritten with the customer contributions component of actual connection charge income, and not the value of the true-up adjustment only.

Closeout methodology Decision

3.16. Our Decision is to implement the methodology proposed in the RIIO-ET1 closeout consultation with the above-mentioned minor modifications. We have decided to proceed with the methodology as provided in Appendix 2.

4. Adjustments for terminated wider works projects

This section details our Decision on the methodology for closing out allowances for terminated wider works projects through the TPWW term in Special Condition (SpC) 6J of NGET's T1 Licence. This chapter applies to NGET only

Background

4.1. Under the RIIO-ET1 framework, an explicit volume driver mechanism was established to provide funding to NGET to deliver electricity transmission projects that meet Network Development Policy (NDP) criteria[15], strengthen specific network boundaries in England and Wales, and increase their transfer capability. The projects and associated outputs are referred to as Incremental Wider Works (IWW).

4.2. Under the RIIO-ET1 framework NGET could proceed with certain projects based on best information then available about the contracted generation background, demand changes forecast, and clusters of prospective transmission reinforcements to best meet consumers' long-term needs.

4.3. However, Ofgem recognised that conditions could change leading to delay or disappearance of the needs case. In some cases it was no longer in the interests of existing and future consumers for an investment to proceed as completed infrastructure work could not be used subsequently to contribute to other outputs delivered by NGET within the RIIO-ET1 period. The RIIO-ET1 framework introduced a mechanism to allow NGET to recover the efficient costs incurred on such projects to that point.

4.4. Transmission Provisions Wider Works (TPWW) is a term within SpC 6J of NGET's T1 Licence which allows the licensee to recover costs efficiently incurred in progressing construction activities in the delivery of an IWW output up to the point of cancellation of the project[16], where conditions have changed and it is no longer aligned with consumers' needs to continue the project to completion.

[15] Required by Part B of SpC 6J of NGET's T1 Licence. The NDP clarifies for stakeholders how NGET makes decisions about the reinforcement of wider transmission system boundaries during the RIIO-T1 price control period. The NDP is available from National Grid's website: download (nationalgrid.com)
[16] Pre-construction costs for IWW projects were separately provided in NGET's baseline allowances. Costs incurred on associated pre construction activity will be allocated against existing RIIO-ET1 allowances.

4.5. As part of its ongoing monitoring of investment plans in accordance with its NDP[17], NGET has identified specific IWW projects that fall under the remit of the TPWW definition. Of these, one project was the subject of a decision in October 2018[18]; the remaining project claims will be the subject of settlement through the RIIO-ET1 closeout process.

Methodology proposed at consultation

4.6. Our proposed approach is to assess and evaluate each TPWW project based on documentation to be submitted by NGET in support of its claims using the agreed cost assessment methodology developed jointly between NGET and Ofgem[19].

4.7. Closeout would entail verification of the non-reusable expenditure (ie the costs incurred that cannot be used to deliver a different output) and establish the value of efficiently incurred expenditure on construction activity recoverable through the TPWW mechanism for each claim.

4.8. We proposed an adjustment calculation that involves the following steps.

1) For the period between 1 April 2014 and 31 March 2021, establish the total expenditure incurred in progressing construction activities in the delivery of an IWW output up to the point of the cancellation of the project. NGET would source this information directly from its internal financial system.

2) Establish the total income received against the projects noted in step 1, the effect of spend in the previous price control period[20] and/or any prior funding[21] (where applicable).

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[17] The NDP clarifies for stakeholders how NGET makes decisions about the reinforcement of wider transmission system boundaries during the RIIO-T1 price control period. The NDP is available from National Grid's website: download (nationalgrid.com)

[18] https://www.ofgem.gov.uk/system/files/docs/2018/10/assessment_of_request_under_the_transmissionprovisions_for_wider_works_mechanism.pdf

[19] The evaluation method was previously developed and agreed to support the review of NGET's 2017 TPWW claim (the North London Reinforcement Project methodology)

[20] The total costs within the RIIO-ET1 business plan submission (both pre-RIIO and during RIIO) were used to create a unit cost allowance (UCA) for each system boundary. When an IWW output is not delivered the volume driver claws back an amount of allowed expenditure for the project by multiplying the size of the megawatt output by the applicable boundary UCA. The mechanism may clawback a value greater than the baseline allowance as a result of expenditure forecast to be incurred in the roll-over year in 2012/13.

[21] Closeout will exclude expenditure provided through the TPCR4 Work In Progress mechanism.

3) Deduct the cumulative value of step 2 from the cumulative value in step 1 to determine the adjustment across the relevant period.

4) The result would be input to the ET1 Legacy PCFM as an adjustment to the relevant company input tab row 19, "Network development and wider works volume driver (NGET only)" under the heading PCFM Variable Values Table.

Consultation responses

4.9. One respondent (NGET) commented on the proposals, agreeing with the approach for assessing TPWW costs but disagreeing with Ofgem's proposal to input the RIIO-T1 TPWW adjustment into the ET1 Legacy PCFM. NGET explained that the proposed financial modelling approach would result in capitalisation rates being applied to the termination amounts and stated that "*capitalisation rates within the PCFM do not take into account the risk of termination and the associated accounting risk*". NGET proposes that to align with the financial accounting treatment and cost profile, the agreed allowance adjustments are treated as 100% 'fast'[22] money (ie. no 'slow' money impact and no associated LRAV adjustment).

4.10. NGET requested that paragraph 4.9 of the proposed methodology clarify that '*spend relating to a previous price control period*' is included in step 1, which refers to cost, rather than step 2 which refers to income and prior funding.

4.11. NGET also sought clarity on the phasing of values in steps 3 and 4 of the proposed methodology in the closeout consultation (paragraph 4.9), proposing that it is appropriate to reflect values in the revenue calculation in the year in which the expenditure was incurred.

4.12. In terms of the adjustment calculation, NGET considered that the appropriate TPCR4 Time Value of Money should be reflected within the adjustment calculation for pre RIIO-ET1 expenditure and noted that the RIIO-ET1 sharing factor should be incorporated into the calculation.

[22] The terminology of fast and slow money in the context of the RIIO-ET1 framework is further explained in the ET1 Price Control Financial Handbook.

4.13. In response to the consultation question on potential revisions to the T2 Licence, NGET proposed:

- clarification that expenditure includes pre-construction spend in the RIIO-T2 period to avoid any future ambiguity in claim submissions in RIIO-T2.
- clarification that recoverable costs associated with terminated projects in RIIO-T2 include costs efficiently incurred in the previous price control period. The proposed amendment (to Special Condition 3.30.10) would therefore explicitly state that TPWW adjustments in RIIO-T2 will provide funding for all efficient expenditure incurred from the period commencing 1st April 2013 i.e. start of RIIO-ET1.

Our views

4.14. In response to the request have the TPWW adjustment processed as a fast money adjustment rather than an input to the variant totex allowance (paragraph 4.9 above), we note that the RIIO-1 PCFM was not designed with management of the components of totex in mind. The proposed approach would require a new entry line that feeds directly into fast money, which if not also fed through the totex tab could reduce clarity of reporting from the PCFM in the future. We are satisfied that the overall capitalisation rate in the RIIO-1 price control remains appropriate. For this reason, we have decided to maintain the proposed process of modifying the TPWW input and therefore variant totex allowances.

4.15. We have made amendments to clarify the language in step 1 and step 2 of the adjustment calculation description in the methodology (paragraph 4.10 above). The methodology text has been amended – see Appendix 3.

4.16. In terms of the query raised on the phasing adjustment (paragraph 4.11 above), we will delay our decision until the statutory consultation, after evaluating the magnitude of the closeout true up. For more detail on our rationale please refer to chapter 2, paragraphs 2.21 and 2.22.

4.17. In response to the issue raised in paragraph 4.12, we agree that a claim to recover efficient expenditure on TPWW projects incurred in a previous price control period can be raised for consideration through the RIIO-ET1 closeout process. We understand this circumstance might apply to only a limited number of TPWW projects and we will evaluate the evidence and justification provided in each case to determine whether it is appropriate to proceed with an adjustment to LAR and LRAV values. The exact form of the adjustment calculation will be discussed at a PCFM working group where we can consider any additional details in full.

4.18. We acknowledge the proposed amendments to the RIIO-T2 Licence (paragraph 4.13 above) and agree in principle to the clarifications they seek to deliver. We will develop and set out our proposals in the forthcoming statutory consultation on changes to the RIIO-ET2 Licence.

Closeout Methodology Decision

4.19. Ofgem will implement the methodology proposed in the RIIO-ET1 closeout consultation with minor modification to reflect the proposed amendment in paragraph 4.10.

4.20. We have decided to proceed with the methodology as provided in Appendix 3.

5. Enhanced Physical Site Security

This section details our Decision on the methodology and process we will follow to close out the RIIO-ET1 Physical Security Upgrade Programme (PSUP). This process applies to all the electricity transmission network owners (ETOs).

Background

5.1. As part of the UK 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)[23].

5.2. PSUP is a cross-sector programme. At RIIO-ET1 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.[24]

5.3. By a decision of 28 September 2018 on NGET's application for an increase in its baseline allowance, we reserved the right to recover any allowances in the context of RIIO-ET1 closeout if the outputs in question were not delivered and decided that RIIO-ET1 closeout would cater for adjustments.

Methodology proposed at consultation

5.4. The consultation set out the following proposal in relation to RIIO-ET1 closeout:

- to claw back all unused allowances for projects that are no longer required due to changes to the CNI list and to clawback unused allowances for outputs not delivered (ie there has been no change to the CNI list and the work is still required, but the agreed output has not been delivered).

[23] Centre for the Protection of National Infrastructure | CPNI
[24] The ability to amend allowances for PSUP was provided under SpC 6H of the T1 Licence.

- to provide an allowance for all efficiently incurred costs where ETOs have incurred costs on projects where the needs case later fell away.

- where an allowance was provided in RIIO-ET1, for a PSUP project that has been delivered, expenditure would be treated as totex and any over- or under-spend subject to the Totex Incentive Mechanism (TIM).

- where an allowance was provided in RIIO-ET1, for a PSUP project that has been partially delivered against the original specification, the consultation proposed a requirement on ETOs to detail why the project was not delivered and to provide evidence that the costs have been efficiently incurred.

5.5. The consultation also recognised that ETOs may have incurred costs during RIIO-ET1 on projects, for which they have not received funding (ie the UK Government has directed that work is required) and proposed adjustments to facilitate the recovery of efficiently incurred costs and outputs delivered as part of RIIO-ET1 closeout.

Consultation responses

5.6. All respondents agreed with the proposed PSUP methodology set out in the consultation, including the proposed ET1 Legacy PCFM adjustments (row 14, "Uncertain costs – enhanced security"). All respondents did, however, request that Ofgem confirm this will be an adjustment to the values already in row 14, not a replacement of existing values.

5.7. One respondent sought clarification around the proposed clawback or true-up and whether it would be implemented when the delivery timeline had slipped into RIIO-ET2 as a direct result of the Covid-19 pandemic. Additionally, the same respondent requested clarification from Ofgem regarding:

- the principles to be employed in assessing the information and the process of evaluation to be applied, and

- the timeframe for evaluation, noting it should take place in advance of any Final Decision on the direction of RIIO-T1 closeout and before "*the end of the calendar year*" (as noted in paragraph 10.15 of the closeout consultation).

5.8. A respondent enquired about the information it was required to submit in order for Ofgem to complete its closeout assessment regarding costs efficiently incurred on PSUP projects that received no allowance during RIIO-ET1. The same respondent also requested that the language in paragraph 10.16 of the proposed methodology in the closeout consultation be amended to provide that ETOs have the opportunity to recover the costs incurred from third party driven work in this situation.

Our views

5.9. In response to the request for clarification on the exact amendment required to PCFM input row (paragraph 5.6 above), we can confirm that the adjustment will not over-write any total allowances already included in this row with the value of true-up adjustment only.

5.10. We have made amendments to the methodology description relevant to the evaluation timeframe (paragraph 5.7 above) and to confirm the intent that the methodology will facilitate consideration of costs which have been incurred within RIIO-ET1 as a result of UK Government direction where network companies have not received an allowance for this work.

5.11. We can also confirm the following principles to be applied in our methodology governing the assessment and recovery of costs.

- It is appropriate that ETOs are not exposed to material PSUP costs incurred within RIIO-ET1 for which they have not received an allowance. We recognise that the UK Government regularly review the guidance for the scope of work required at PSUP sites and their assessment of which sites should be included in the PSUP. This means that ETOs assessment against the CNI criteria to determine the optimum security solution is a fluid process which has created instances of additional sites requiring security enhancements within RIIO-T1. The ETOs are therefore permitted to demonstrate the costs they have incurred for this work for consideration as part of RIIO-ET1 closeout and to provide evidence that the costs have been efficiently incurred.

- If consumers have funded material costs for projects that were cancelled this money is returned to them (net of costs deemed to be efficiently incurred).

- We will endeavour to conclude our assessment of the relevant information submitted in a timely manner in order to feed into the AIP process in November 2022.

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

5.12. We note that there may be RIIO-ET1 PSUP projects that were delayed where an output is now expected to be delivered in RIIO-ET2 timescales. For projects funded in RIIO-ET1 that will be completed in RIIO-ET2 we expect ETOs to submit a 'Tech Audit'[25] upon project completion. For projects funded and completed in RIIO-ET1, Ofgem considers that it already has enough information to complete our assessment and there is no requirement to submit a Tech Audit in relation to these projects[26].

5.13. Finally, we make the broad observation that costs incurred in RIIO-ET2 in relation to PSUP projects funded in RIIO-ET1 are to be reported as a specific cost line under the PSUP cost category as 'Other Capex' in RIIO-ET2 RRPs and treated as totex. Therefore all expenditure will be subject to the TIM. No additional allowance will be provided in RIIO-ET2[27] in relation to PSUP projects funded in RIIO-ET1.

Closeout methodology Decision

5.14. Our Decision is to implement the closeout methodology for PSUP as consulted on with modification to reflect the minor points noted above. The process will also adopt a proportionate approach to encompass projects that do not have pre-agreed funding but where costs have been incurred within RIIO-ET1 as a result of UK Government direction.

5.15. We have decided to proceed with the methodology as provided in Appendix 4.

[25] A Tech Audit will set out the actual solution installed at the sites (ie type/length of fencing, number of cameras, security lights etc) and will provide confirmation that the work meets CNI requirements.
[26] We note that the requirement to provide confirmation of the value being sought and accompanying high level narrative as part of the final performance assessment submission remains unchanged.
[27] We note that ETOs can submit a claim through the Re-opener mechanism under SpC 3.4 Physical security Re-opener and Price Control Deliverable where the project meets the specified criteria.

6. Adjustments for terminated connection projects

This section details our Decision on the methodology for closing out RIIO-ET1 allowances for terminated connection projects, taking into account NGET's total income from termination receipts received directly from customers within the RIIO-ET1 period. This chapter applies to NGET only.

Background

6.1. Users of the transmission system can terminate their bilateral agreements (or agree a capacity reduction) prior to commencing use of the requested connection.

6.2. It is difficult to identify which projects will ultimately terminate (or reduce capacity) and when this might occur. There was no ex-ante or baseline allowance set in RIIO-ET1 for terminations/reductions.

6.3. The nature of the calculation of generation termination liabilities (Cancellation Charges) is defined in the Connection and Use of System Code (CUSC). The methodology is generic and may not reflect the actual costs incurred to meet a customer's desired connection date. In addition, NGET receipts are calculated depending on the type of liability the customer has selected, either 'fixed' (based on a forecast of spend) or 'actual' (based on the final cost). Hence, there is a potential for NGET expenditure to either exceed or fall short of the customers' termination liabilities.

6.4. In the event a customer terminates their connection agreement with the Electricity System Operator (ESO) prior to commencing use of the connection, the RIIO-ET1 framework introduced mechanisms for NGET to recover any deficit in or return any surplus termination payments as compared to costs efficiently incurred on such connections.

6.5. Special Condition (SpC) 6F of NGET's T1 Licence[28] ensured that the costs efficiently incurred in progressing construction activities in the delivery of a user terminated generation connection (licence term TPG) and the income from termination receipts from user terminated generation connections (licence term TPRG) during the RIIO-ET1 period are reported. Similar provisions existed in SpC 6L of NGET's T1 Licence relevant to the

[28] Paragraph 8 in Part A of SpC 6F of NGET's T1 Licence paragraph 8 in Part A of SpC 6L of NGET's T1 Licence.

reporting of user termination of demand bilateral connection agreements within the RIIO-ET1 period[29].

Methodology proposed at consultation

6.6. We proposed to assess documentary evidence submitted by NGET to ascertain:

- the costs incurred in RIIO-ET1 in relation to all projects where the users have terminated generation and demand bilateral agreements.[30] The data would be derived from NGET's financial system SAP for each project and reflect only RIIO-ET1 costs (and confirm any other costs prior to RIIO-ET1 that NGET considers have received funding from previous price controls).

- that these costs are economic and efficient, including where costs have been recovered through drawing down of security.

- the income received by NGET from termination payments for all projects where the users have terminated generation and demand bilateral agreements. The income data would be taken from customer invoices paid by the customer. The submission would identify specific invoices which remain unpaid by the customer.

- that the assets associated with the above-mentioned projects cannot be used subsequently to contribute to other projects or outputs delivered by NGET, or where NGET can recover costs through subsequent sale or scrappage.

6.7. We set out a proposed requirement that NGET provide a level of cost explanation and justification that is proportionate to material claims only. We therefore proposed that NGET would provide an Engineering Justification Paper (EJP) for each scheme as part of our RIIO-T1 close-out submission where the costs incurred are equal to or greater than an agreed threshold (£1m in 2009/10 prices).

[29] Paragraph 8 in Part A of SpC 6L of NGET's T1 Licence.
[30] This will not include projects which have terminated since April 2019 when National Grid ESO and National Grid ET became legally separate entities within the National Grid Group.

6.8. We proposed an adjustment calculation involving the following steps.

1) Establish the total expenditure incurred where the users have reduced capacity or terminated generation bilateral agreements (TPG) or users have terminated demand bilateral agreements (TPD) for the period between 1 April 2014 and 31 March 2019[31]. NGET would source this information directly from its internal financial system.

2) Establish the total income received against the projects noted in step 1 (TPRG and TPRD). NGET would source this information from customer invoices paid by the customer for the relevant year that the customer is charged.

3) Deduct the cumulative value of income in step 2 from the cumulative value in step 1 to determine the true-up adjustment across the relevant period.

4) The result would be input to the ET1 Legacy PCFM as adjustments to the relevant company input tab:

- row 23, "Generation connections volume driver" under the heading "PCFM Variable Values Table" in respect of Generation Connections.
- row 21, "Demand related infrastructure volume driver" under the heading "PCFM Variable Values Table" in respect of Demand works.

6.9. Paragraphs 5.10 – 5.14 of the consultation set out our proposed methodology for the treatment of 'Terminations that are yet to happen', projects where NGET have incurred cost but that are not currently expected by NGET to result in a completed connection (or output delivery) despite the customer still being contracted.

Consultation responses

6.10. One respondent (NGET) commented on the proposals, agreeing with the approach for the treatment of terminated costs and receipts subject to amendments to reflect points arising from further engagement with Ofgem. These amendments include:

[31] In April 2019, National Grid ESO and National Grid ET became legally separate entities within the National Grid Group. National Grid ET will seek the full cost of projects which terminated since April 2019 from National Grid ESO.

- the threshold for submission of EJPs (noted in paragraph 6.7 above) is to be proportionate to materiality, and an EJP would not be required for schemes equal to or less than £2m.

- the materiality is to be based on the net claim position (e.g. TPG-TPRG) and level of justification would be more proportionate to claim value. In its response, NGET stated "*that claims towards the £1m/£2m level would not require a full EJP but should capture the high-level information surrounding the claim*".

6.11. NGET disagrees with the proposed approach outlined in the methodology document for 'Terminations yet to happen' (paragraphs 4.13 to 4.16 of the consultation). NGET's contention is that the RIIO-T1 costs have been incurred efficiently and the RIIO framework should provide timely funding for these costs. NGET considers it poor regulatory practice to implement a process where a price control is not fully closed out at the end of the period and do not believe leaving licensees to carry the risk of unfunded investment is appropriate.

6.12. NGET also commented that delaying the funding of these costs introduces regulatory risk as the settlement of costs will require a further process to capture expenditure incurred that could span multiple price control periods and the need for potential future adjustments to ensure no inappropriate gain / loss over this time period (if allowances were provided in future control periods). NGET therefore supports a solution to deal with RIIO-T1 spend now rather than later.

6.13. NGET commented that if Ofgem were not to pursue an approach to settle the funding of the efficiently incurred costs through T1 closeout, the current T2 licence will need to be developed to provide clarity over the time periods of spend that can be included in any claim. NGET proposed to update the defined term "Regulatory Year" in the TPG and TPD definitions[32] to clarify that the applicable timeframe commences on 1st April 2013.

6.14. NGET also noted that within the T2 Licence the recovery of terminated connection projects are part of the volume driver calculations[33] which form part of Totex Allowances. This will result in capitalisation rates being applied to the termination amounts. NGET

[32] In the T2 Licence, Regulatory Year "means a period of twelve months commencing on 1 April".
[33] within Special Conditions 3.11 and 3.12.

disagrees with this approach because it does not allow for timely recovery of termination costs.

6.15. NGET raised further points on the following paragraphs in the consultation document:

- Paragraph 5.7: an inconsistency was noted in the expression of the proposed closeout methodology for TPG/TPD in RIIO-ET1 and the intent of claiming RIIO-ET1 expenditure in future price control periods.

- Paragraph 5.14: further clarification is requested on terminations that occur in price control periods beyond RIIO-ET2.

Our views

6.16. We acknowledge the points raised around amending the proposed materiality thresholds and the information required to support a termination claim. We support the adoption of the proposed materiality thresholds (based on the net claim position) and to make the level of justification proportionate to the claim value (no requirement for a full EJP but capture the necessary information to understand and evaluate the claim).

6.17. On the issue of 'terminations yet to happen', we note that, when a project eventually terminates, the TPG/TPD framework is intended to provide funding in line with the principle of funding efficient investment. We acknowledge that the arrangements could lead to funding long after the time at which the investment decision was made. Despite this, we hold the view that the regulatory information can be retained and utilised at the appropriate time to ensure the efficient spend is appropriately funded.

6.18. We strongly disagree that the proposed methodology represents poor regulatory practice, noting that the bespoke treatment of such projects is not built into the RIIO-T1 framework. After careful consideration we do not consider it appropriate to adopt NGET's alternative proposal for the following reasons:

1) the termination of the need is not yet confirmed within the context of the RIIO-ET1 period and there is no mechanism to fund such costs through the T1 closeout process and no mechanism whereby the proposed adjustment can be implemented.

2) in the absence of a mechanism we regard the licensee to be the appropriate party to bear the costs which materialise in this process until the projects eventually terminate and an assessment of efficiently incurred costs can be undertaken. This is consistent with the principle of funding efficient investment, while still maintaining appropriate protection to consumers from the costs of inefficient investment.

3) our regulatory intent is to provide a transparent and stable framework for the ETOs to operate as per our FP Decision. We do not consider it appropriate or proportionate to adjust the RIIO-ET1 framework to address the issue because the customers are still contracted and do not satisfy the definition parameters of the T1 Licence (SpC 6F and 6L).

6.19. We do, however, acknowledge the fundamental issue raised by NGET – that the current RIIO-T2 framework may not facilitate an appropriate response to provide funding of RIIO-T1 costs upon the eventual termination of these projects. In the RIIO-T2 Transmission Licence, the TPGt and TPDt terms only applies to each Regulatory Year (the first of which commences on 1st April 2021). We therefore propose to address this issue through amendment to the T2 Licence and to proceed with a statutory consultation to clarify the time periods of spend that a TPG and TPD claim can be raised for.

6.20. In response to the issue raised in paragraph 6.14, we are satisfied that the overall capitalisation rate in the RIIO price control remains appropriate and will maintain the current process.

6.21. We note the request for clarity on the approach for terminations that occur in price control periods beyond RIIO-ET2 (paragraph 6.15 above). We can confirm that our assessment process will seek to collate information on efficiently incurred costs to the point of termination in future price control periods under the applicable TPD/TPG mechanism, or an equivalent, within the relevant ET licence.

6.22. We also note NGET's comment that these 'not yet terminated projects' are not part of the RIIO-T2 baseline and the request for clarity on how funding through a RIIO-T2 shortfall would work in practice. We believe the best forum to continue discussion on the process for how this may operate is through continued bilateral engagement under the RIIO-ET2 framework and consideration against the parameters of the T2 Licence rather than the RIIO-ET1 closeout process.

Closeout methodology Decision

6.23. Following consideration of the consultation responses we are making minor amendments (noted above) to the closeout methodology that was consulted on.

6.24. We have decided to proceed with the methodology as provided in Appendix 5.

7. Settlement of allowances for pre-construction work

This section details our Decision on the methodology for closing out baseline allowances associated with the delivery of specified pre-construction activity under SpC 3L of the T1 Licence. This process applies to all electricity transmission network owners (ETOs).

Background

7.1. The RIIO-ET1 settlement contained a 'use it or lose it' ex-ante allowance for each ETO to progress pre-construction engineering works where these are preparatory for Strategic Wider Works projects.[34] These pre-construction works are referred to as Pre-Engineering Outputs ('PE Outputs') under SpC 3L of the T1 Licence.

7.2. Under the provisions of paragraph 9 of SC 3L of the T1 Licence, an ETO can raise a request to amend the details of the PE Outputs prescribed in the licence through an output substitution (OS).

7.3. Paragraph 17 of SpC 3L provides that the Authority may adjust baseline expenditure, in the event that the licensee does not deliver or only partially delivers a PE Output on or before 31 March 2021.

Methodology proposed at consultation

7.4. We proposed to assess documentary evidence to be submitted by the ETOs to ascertain:

- the costs incurred by the end of the ET1 price control period in relation to all PE Outputs set out in Part A of SpC 3L (reflecting the impacts of any previous OS decisions), and that these are economic and efficient. The data would be derived from ETO's internal financial system for each project and reflect only pre-construction costs incurred within the RIIO-ET1 period.

- the pre-construction engineering works associated with the above-mentioned PE Outputs that have been:

[34] SC 3L: Pre-construction Engineering Outputs for prospective Strategic Wider Works, paragraph 17.

    - completed and delivered on or before 31 March 2021,
    - partially delivered by 31 March 2021, or
    - not delivered by 31 March 2021.

- that the activities associated with above-mentioned projects cannot be used subsequently to contribute to other pre-construction outputs forecast to be delivered in RIIO-ET2 timescales (and which have been funded through other mechanisms).

7.5. Based on the information and justification provided by the ETOs submission, we proposed an adjustment calculation that involves the following steps.

i. Establish the total allowed expenditure associated with the PE Outputs that are confirmed by the ETO to have been partially delivered or not delivered.

ii. Establish the total allowed expenditure associated with the PE Outputs that are confirmed by the ETO to have been delivered by 31 March 2021.

iii. Deduct the cumulative value of allowed expenditure in step 1 from the total value of allowed expenditure in step 2 to determine the adjustment across the RIIO-ET1 period.

iv. This would be input to the ET1 Legacy PCFM as an adjustment to the relevant company input tab row 84, "Non-variant allowed load related capex expenditure" under the heading "Expenditure".

Consultation responses

7.6. All respondents agreed with the proposed methodology for assessing PE Outputs.

7.7. Two respondents sought confirmation that the assessment will be performed against the outputs specified in Part A of Special Condition 3L of the T1 Licence, reflecting the impacts of any previous OS decisions.

7.8. All respondents agreed that, in the event that our assessment results in an adjustment to allowances, the approach to amend the ET1 Legacy PCFM as set out in paragraph 6.6 of the consultation will be applied and adjustment will be made to the existing values in row 84, "non variant allowed load related capital expenditure".

7.9. One respondent requested that Ofgem confirm the process of adjustment (if applicable) to be applied in row 14 of the financial model.

Our Views

7.10. We can confirm that we have made decisions on two OS requests received during RIIO-ET1[35], and that our closeout assessment will be against the post-substitution allowances.

7.11. In relation to the point raised in paragraph 7.9 above, we agree that any adjustment will be to the values already in the applicable row of the PCFM, not a replacement of existing values.

Closeout methodology Decision

7.12. Our Decision is to implement the methodology proposed at consultation without modification. This is set out in Appendix 6.

[35] One Output Substitution request was received from each of SHET and NGET. These are available from the Ofgem website.

8. Adjustments for asset and land related disposals

This section details our Decision on the methodology and process we will follow to close out RIIO-ET1 disposals. This process applies to all electricity transmission network owners (ETOs).

Background

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

8.2. Where network assets are no longer required, ETOs 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 ETOs provide us with the details of any assets or land disposals that occurred in RIIO-ET1 so that we can undertake an appropriate assessment of the disposal of any network assets to ensure the sale price reflects true market value.

8.4. We proposed that Regulatory Asset Value (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:

True-up value = (proceeds of disposal – cost of disposal) x (1-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. All three respondents agreed with the intention to return a benefit to consumers in relation to assets that are disposed of where there are cash proceeds. However, only one respondent supported the proposed methodology for disposals described in the closeout consultation; two respondents did not agree with the proposed methodology.

8.7. Two respondents wanted the disposal of assets to be netted-off against Totex from the year in which the proceeds occur (and to apply the net proceeds of sale before application of the TIM). It was further noted that no rationale had been presented to justify why the proposed approach in ET should differ from the 'pre-TIM' approach currently used in the Electricity Distribution framework. The respondents considered that the alternative approach better incentivised ETOs to maximise the return that could be gained from the sale of assets that are no longer required (eg. land) which would be in the best interest of consumers, whereas netting off the disposal proceeds against RAV offers no financial benefit to the ETOs to achieve the best sale proceeds when disposing of assets.

8.8. One respondent (NGET) sought clarification on two issues:

i. that the adjustment is to be made net of tax paid, and

ii. the appropriate tax rate is the actual tax rate in the relevant year of disposal.

Our views

8.9. The approach to the treatment of Disposals was set out in RIIO-ET1 Final Proposals (FP)[36], and the January 2022 consultation confirmed the application of this approach in the RIIO-ET1 closeout process. Our regulatory intent is to provide a transparent and stable framework for the ETOs to operate as per our FP decision. Whilst it is noted that Ofgem has revised the treatment of disposal proceeds for RIIO-ET2, treating them as negative totex, we do not consider there is a case to re-open the policy that was agreed for RIIO-ET1.

8.10. We have decided to implement the methodology proposed at consultation: to reflect disposals within the year the disposal took place, thus considering the time value of money. The net proceeds will be made net of the appropriate tax rate in the relevant year of disposal and any reasonable costs incurred in disposing of the asset.

8.11. There was support for the proposed financial revision to enter the true up value in the relevant company input tab of the ET1 Legacy PCFM row 238, "RIIO post-vesting RAV

[36] RIIO1 Finance supporting document, paragraph 2.16. Published on 17 December 2012.

disposals", under the heading "RAV and assets". The adjustment will be entered as a negative value.

Closeout methodology Decision

8.12. We will closeout RIIO-ET1 disposals by applying the methodology as consulted on. We have decided to implement the methodology as set out in Appendix 7.

8.13. As noted in chapter 4 of the closeout consultation document, part of our published decision in relation to the North London Reinforcement Project under the TPWW mechanism noted that we will identify any financial gains that NGET derive from land ownership associated with this project (whether through leasing out or sales). We proposed that any value identified through the closeout process will be returned to consumers by application of the above-mentioned formula. Our Decision is to implement this approach.

9. Adjustments for crossover volume driver projects

This section details our Decision on the methodology for closing out allowances associated with the delivery of outputs in the first two years of RIIO-ET2 where funding provision is made in related RIIO-ET1 volume driver mechanisms.

Background

9.1. The RIIO-ET1 framework contained uncertainty mechanisms for load-related projects that included an automatic trigger to adjust allowances through an extension of the volume drivers into the first two years of the RIIO-ET2 period. This period is referred to as "T1+2"[37] and is applicable to relevant "crossover" projects. The RIIO-ET1 mechanisms include:

- *Generation connection works,* for NGET and SHET.
    - For NGET, it provides profiled allowances for new connected capacity (MW) and reinforcement to existing local infrastructure (circuit kilometres constructed using new overhead lines).
    - For SHET, it provides profiled combined allowances for sole use infrastructure capacity (MW) and shared use infrastructure capacity (MVA).[38]
- *Demand connection works* for NGET only.
- *Incremental Wider Works* (or IWW) that deliver an increase in the capability of specific transmission boundaries[39] for NGET only.
- *installation of underground cables* for planning purposes, for NGET only.

9.2. There are other company-specific features in the RIIO-ET1 framework that need to be reflected in the closeout in relation to relevant crossover projects. These are briefly summarised below.

[37] For brevity we reference the T1+2 period when referring to the duration of the volume driver mechanisms under the T1 Licence but recognise that NGET's undergrounding mechanism applies up to 31 March 2024.
[38] SPT's generation connections volume driver mechanism only adjusted allowances for outputs delivered up to 31 March 2021, so there is no closeout adjustment required.
[39] Table 1 of SpC 6J lists fifteen original transmission boundaries across England and Wales.

NGET

- The RIIO-ET1 price control contained a specific requirement that NGET provide a forecast of the expenditure expected to be incurred for outputs expected to be delivered in T1+2. This was discharged as part of NGET's regulatory reporting submission in July 2017 (RR2017). Changing customer requirements and delivery plan updates have led to a revised view of these projects and these will need to be trued up against the actual or best available forecast output delivery in T1+2 for each of the mechanisms detailed above, where necessary.

- The RIIO-ET2 framework contains baseline profiles across a range of metrics[40] which are currently based on the forecast information provided by NGET as part of the RIIO-ET2 Business Plan. These baseline profiles may need updated to align with the latest position of T1+2 delivery and as a result of the closeout decision within the T2 volume driver mechanism.

- Adjustments may be required to remove any double funding from the RIIO-ET2 baseline for projects that now have delivered or are expected to deliver outputs in T1+2 for each of the mechanisms detailed above.

SHET

- The RIIO-ET2 framework contains baseline profiles across a range of metrics[41] which are currently based on the forecast information provided by SHET as part of the RIIO-ET2 Business Plan. Similar to NGET, the T2 baseline profiles may need to be revised to align with the latest position of T1+2 delivery and as a result of the closeout decision within the T2 volume driver mechanism.

- Adjustments may be required to remove any double funding from the RIIO-ET2 baseline for projects that now have delivered or are expected to deliver outputs in T1+2 for the new generation volume driver mechanism.

[40] Including the physical output capacity (MW or MVA) expected to be delivered between 1 April 2021 and 31 March 2023, the length of overhead line reconductoring activity, length of new underground cable and the number of connection projects delivered across the T2 period.
[41] The RIIO-ET2 framework for SHET includes an additional metric not applicable under NGET's mechanism: the length of new build overhead line activity.

Methodology proposed at consultation

NGET

9.3. We proposed the following closeout process to true up NGET's allowances against the latest view of projects delivering outputs in T1+2 timescales:

- Where projects were forecast in NGET's RR2017 to deliver outputs in T1+2 (and thus receiving funding already) but will no longer do so, the amount of revenue already received would be returned to consumers
- For those projects that were forecast in NGET's RR2017 to deliver output in T1+2 and either have already delivered or are still expected to do so:
  - Where the project is being delivered in line with the forecast capacity and timing, NGET would keep the allowances on the basis of its RR2017 forecast under the volume driven RIIO-ET1 mechanisms during the T1+2 period. If there is also RIIO-ET2 funding provided for the same project, the T1+2 allowance would be offset by any RIIO-ET2 allowances given for that same project.
  - Where the actual or best available forecast of the project delivery is not in line with NGET's RR2017 forecast capacity and/or timing, the difference between the prior allowance and the revised allowances due under the volume driven RIIO-ET1 mechanisms during the T1+2 period would be calculated. This amount may be zero for those projects that have either completed during the RIIO-ET1 period or whose outputs would be delayed beyond T1+2. Again, the resultant sum will be offset as appropriate by any RIIO-ET2 allowances given for that same project.
  - Where projects were not included in the RR2017 forecast but either have delivered or are expected to deliver outputs in T1+2, the allowance due would be as under the volume driven RIIO-ET1 mechanisms, which would be offset as appropriate by any RIIO-ET2 allowances given for that same project.

9.4. Adjustments would be made to the NGET input tab of the ET1 Legacy PCFM for the following variable values:

- IWW in row 19, "Network development and wider works volume driver (NGET only)" under the heading "PCFM Variable Values Table".
- DRI row 21, "Demand related infrastructure volume driver" under the heading "PCFM Variable Values Table".
- GCE in row 23, "Generation connections volume driver" under the heading "PCFM Variable Values Table".

SHET

9.5. We proposed that projects that meet the delivery criteria of a crossover project and which are eligible to receive funding determined by the volume driver unit rates set within the T1 Licence would be remunerated accordingly. We would make appropriate adjustments to the level of funding applicable to the RIIO-ET1 and RIIO-ET2 component to facilitate this approach and to avoid double funding projects that are already included in RIIO-ET2 baseline. Closeout would confirm:

- projects that commenced in RIIO-ET1 but which have not yet delivered outputs:
    - Where the project is being delivered during the T1+2 period, the allowances due under the T1 generation connection volume driver during the T1+2 period will be calculated. This allowance would be netted off as appropriate by any RIIO-ET2 allowances given for that same project.
    - Where the project is not scheduled to be completed within the T1+2 period, the volume driven RIIO-ET1 mechanisms would not apply .
- projects that were scheduled to be delivered in the T1+2 period but have delivered by the end of RIIO-ET1. In this case the allowance due under the volume driven RIIO-ET1 mechanisms would be offset as appropriate by any RIIO-ET2 allowances given for that same project.

9.6. Adjustments will be made to the SHET input tab of the ET1 Legacy PCFM for the variable value GCE in row 23, "Generation connections volume driver" under the heading "PCFM Variable Values Table".

9.7. Paragraph 7.20 of the consultation also summarised the evidence that we proposed to require for all crossover projects (NGET and SHET) on anticipated delivery dates and costs to establish the basis and accuracy of the forecast outturn position provided for each scheme.

9.8. Paragraphs 7.46 – 7.53 of the consultation set out our proposed methodology for the treatment of connection number and linear elements between price control periods (SHET and NGET).

Consultation responses

NGET

9.9. NGET agreed with the approach outlined in the methodology document for assessing crossover projects.

9.10. To avoid ambiguity, NGET requested that the methodology document provide more detail on the application of the approach for both customer connection and IWW projects.

9.11. NGET disagreed with the requirement to provide an explanation of "*financial and cost benefit analysis*" (stated in paragraph 7.20 of the consultation), noting that the scope of works for connection projects has been agreed through a bi-lateral agreement and is subject to a licence obligation to deliver a connection, whereas for IWW projects the investment is supported by a CBA undertaken by the Electricity System Operator.

9.12. NGET also made the general observation that requesting a CBA distinguishes closeout crossover projects from other projects operating under the same mechanism, i.e. funded through the relevant T1 volume driver, and does not consider the RIIO-ET1 closeout process to be an opportunity to review historic investment decisions. NGET therefore requested that the CBA requirement is removed from the methodology document.

9.13. NGET were in broad agreement with the adjustments required to specific rows detailed within the ET1 Legacy PCFM, but a raised a general query on whether the application of the closeout methodology will result in adjustments to the existing values within the specified rows within the ET1 Legacy PCFM rather than an over-write and replacement of existing values.

9.14. NGET agreed with the proposed approach for dealing with post closeout changes in output date (paragraphs 7.22 to 7.28), but noted the methodology does not include the timings of when NGET can expect such adjustments to be consulted on and reflected in the

ET2 PCFM (change required to yellow box inputs 'non Variant Allowed load related capex expenditure').

9.15. NGET also agreed with proposals linked to addressing potential post closeout movements in connection output delivery volume (paragraphs 7.29 to 7.35 of the consultation), and agreed that updates would be reflected in BGC under SpC 3.11 for generation connections and BDC under SpC 3.12 for demand connections. NGET further noted the proposal to adjust baseline profile positions for any new generation or demand connections and supported the process of statutory licence modification consultation to implement any adjustment.

9.16. NGET identified that the proposed methodology for the closeout of crossover volume driver projects addresses the funding of demand or generation-related infrastructure costs triggered as a consequence of providing additional capacity in the T1+2 period, it does not capture the funding position for associated "sole-use"[42] works incurred in this timescale.

9.17. NGET explained that the presence of unfunded sole-use work in the T1+2 timeframe is the result of two factors: (i) differences in the calibration of the connection volume driver arrangements between RIIO-ET1 and RIIO-ET2, and (ii) the scope of the proposed Excluded Services true-up. Therefore, solely applying the volume driven RIIO-ET1 mechanisms for new connections in the manner expressed in the consultation will result in unfunded sole-use investments associated with delivery of outputs in the T1+2 period. NGET believes that, in the absence of any other funding route, provision for the sole-use works must be captured in the closeout methodology.[43]

SHET

9.18. SHET agreed with Ofgem's proposed approach to include the full RIIO-ET1 and RIIO-ET2 allowance within the RIIO-ET2 PCD for each crossover project reflecting the assessment of total efficient costs for the applicable schemes. SHET noted that to implement this approach will require a true-up to reconcile allowances for the latest view of

[42] As explained in chapter 3, the cost of assets provided solely for a particular customer are recovered directly from the relevant customer via connection charges and treated as excluded services.
[43] This is applicable to NGET only; a similar change was not made to the calibration of the connection volume driver mechanisms of SPT and SHET between RIIO-ET1 and RIIO-ET2.

crossover projects delivering outputs in T1+2 timescale that will be delivered in a final performance assessment submission.

9.19. SHET disagreed with the requirement to provide an explanation of "*financial and cost benefit analysis*" and "*any other relevant evidence from (or in relation to) the licensee's decision-making process*"[44], noting that a CBA template was not used in any decision making during RIIO-ET1 and that a new template will therefore need to be developed and provided to facilitate this requirement. For these reasons SHET requested the removal of the requirement from the proposed methodology.

9.20. SHET agreed with proposals linked to addressing potential post closeout movements in connection output delivery date (paragraphs 7.22 to 7.28 of the consultation), and agreed that output delivery of projects agreed at crossover will be added to the capacity baseline against the "BGC" term in appendix 3 of SpC 3.11 of SHET's T2 Licence (paragraph 7.45 of the consultation)

9.21. SHET also supported proposals to address potential post closeout movements, both up and down, in connection output volumes (paragraphs 7.29 to 7.35 of the consultation), and stated that any incremental movement "*will result in allowances as agreed at close out being adjusted to reflect the incremental movement in output based upon T2 volume driver rates*".

9.22. On the treatment of connection number and linear elements between price control periods (paragraphs 7.50 to 7.53), SHET agreed with our proposed approach that any movements between typical and atypical will be subject a true-up to adjust allowances and volumes.

Our views

9.23. We note that NGET was supportive of the proposed methodology to closeout the funding for crossover projects to which volume driven RIIO-ET1 mechanisms apply.

9.24. In response to the concerns raised on the proposed CBA requirement expressed in the consultation (paragraphs 9.11, 9.12 and 9.19 above), on reflection we agree that such a requirement for the purpose of closeout is not appropriate. We acknowledge that RIIO-

[44] Paragraph 7.20 of the consultation document.

ET1 closeout is not a mechanism for reviewing historic investment decisions. Furthermore, we agree and that, due to the mechanistic nature of the volume driver mechanisms, a CBA template was not used in any decision making during RIIO-ET1 and a new template would therefore need to be developed to facilitate this requirement. In the circumstances, we consider it is reasonable to remove this requirement from the closeout process.

9.25. We do, however, expect the basis of the performance submission to update and augment the information previously provided in the 2020/21 RRP submission, where appropriate. The information must therefore be updated to reflect the latest information on expenditure, volume delivery and completion of each crossover investment under each of the relevant volume driver mechanisms. This will also provide visibility and explanation of the calculation of the project allowance for each investment based on the unit rates and construction profile set out in the T1 Licence.

9.26. We note the request to provide further detail on the application of the methodology. We consider that the principles described in paragraphs 9.3 and 9.4 above explain its application. We can consider any additional details provided through the performance submission in working groups.

9.27. In terms of the existence of unfunded sole-use works associated with crossover volume driver projects (paragraph 9.16 above), we agree that there is a gap in the funding provision caused by the different calibrations of the connection volume driver mechanisms. We note the following points:

- The RIIO-ET1 connection volume driver mechanisms of NGET (SpC 6F and 6L) were calibrated to provide allowances under the "Local Enabling Entry" and "Local Enabling Exit" investment cost categories[45]. The RIIO-ET1 funding from 1 April 2013 to 31 March 2023 (ie T1+2) that will be delivered by each mechanism relates to infrastructure works only.

- In contrast, under RIIO-ET2, the volume driver arrangements for Entry connections and Exit connections in NGET's area have been calibrated based on an extended scope of costs data that also included costs under the "Entry Sole-use" and "Exit Sole-Use" investment cost categories. These include assets forming the immediate connection to

[45] Infrastructure assets which are associated with an individuals' choice of the design and type of connection.

the transmission substation and capable of use by only one customer[46]. As such, the RIIO-ET2 funding from 2023/24 onwards that will be derived by each mechanism relates to both the sole-use and infrastructure works.

- The costs incurred in relation to sole-use works associated with delivery of outputs in the RIIO-ET1 price control period were anticipated to be funded via the trued-up Excluded Services Allowance (see chapter 3 for more details).

- While an approach to recover the costs incurred in relation to sole-use works associated with volume driver projects anticipated to be delivered in the T1+2 period was not directly referenced in the RIIO-ET1 Final Proposals documentation, the true-up calculation associated with such works was established. The process of true-up will seek to ensure ETOs' neutral performance in the delivery of connection activity and provide a transparency on the actual expenditure / revenues as a result of providing sole use connection assets.

9.28. In addition, we recognise that a number of sole-use investments which NGET expects to deliver in T1+2 timescales were included in NGET's RIIO-ET2 submission and have received funding in the RIIO-ET2 baseline. The closeout process will therefore seek to determine the schemes and the value of adjustments to be made in a manner that will avoid the risk of double funding projects that are already included in RIIO-ET2 baseline and remove the risk of unfunded sole-use investments within the first two years of RIIO-ET2. We can consider any additional details provided through the performance submission in working groups.

Closeout methodology Decision

9.29. Following consideration of the consultation responses we have decided to apply the closeout methodology that was consulted on with the following adjustments.

- We have removed the CBA requirement originally proposed, and

- We have included provision for sole-use investment associated with the delivery of crossover volume driver projects in the T1+2 period through a baseline adjustment

[46] More information on the parameters of the RIIO-ET2 mechanisms is provided in chapter 4 of the RIIO-ET2 Final Determinations publication entitled "RIIO-2 Final Determinations Electricity Transmission System Annex".

reflecting the expected costs in T1+2 as part of the RIIO-ET1 closeout, consistent with the treatment for other T1+2 allowances.

9.30. We have decided to proceed with the methodology as provided in Appendix 8.

10. Approach for crossover projects without volume driver

This section explains our approach to fund 'crossover' projects where the delivery of outputs is expected in RIIO-ET2 or beyond and for which the RIIO-ET1 price control provided no allowances for spend incurred in the RIIO-ET1 period.

Background

10.1. In our RIIO-ET2 Final Determinations (FD), we stated our decision[47] that for load related (LR) projects which span RIIO-ET1 and RIIO-ET2 we will carry out the true-up of the RIIO-ET1 funding as part of the RIIO-ET1 closeout. The previous chapter set out our proposed methodology to close out the funding for LR "crossover" projects to which RIIO-ET1 volume drivers apply. This chapter deals with specific crossover LR projects identified by SHET & NGET that are not subject to adjustment through the arrangements described in chapter 9.

10.2. The funding provision detailed in the FD for each company is briefly summarised below.

NGET

10.3. Expenditure information was provided by NGET for each crossover LR project through the original RIIO-ET2 Business Plan (BP) submission. This included forecast information for the remaining RIIO-ET1 period (2019/20 and 2020/21) and expenditure expected to be incurred in progressing the delivery of outputs across the RIIO-ET2 period and beyond. The information was subjected to our engineering and cost assessment process[48].

10.4. Based on our assessment of that information, in our FD we:

- set baseline funding for the RIIO-ET2 period and set Price Control Deliverables (PCDs). The associated allowances for each PCD represent only the expected expenditure in the RIIO-ET2 period and not any expenditure in the RIIO-ET1 period.

[47] RIIO-2 Final Determinations – ET annex (published 3 February 2021) – paragraph 3.32.
[48] RIIO-2 Draft Determinations – ET annex (published 9 July 2020) – pages 50-63.

- stated our decision to apply a further positive allowance adjustment to reflect the expenditure to be incurred in the RIIO-ET1 period and to provide full project funding for the efficient forecast expenditure for the LR crossover projects identified by NGET. We said this was a provisional figure and would be reviewed at a later date. The value of the adjustment was £87m (2018/19 price base).

10.5. The provisional funding was included within the RIIO-ET2 baseline allowance[49] by 'netting off' against a negative adjustment applied to non-load related capex work that spans work in RIIO-ET1 and RIIO-ET2 (see Special Condition 3.38 of NGET's T2 Licence)[50].

SHET

10.6. Expenditure information provided by SHET on the total cost profile for each project was provided through the original RIIO-ET2 BP submission. This included forecast information for the remaining RIIO-ET1 period (2019/20 and 2020/21) and expenditure expected to be incurred in progressing the delivery of outputs across the RIIO-ET2 period. The information was subjected to our engineering and cost assessment process.

10.7. Based on our assessment of that information, in our FD we set funding in two parts.

- The RIIO-ET1 component of each project was provided ex-ante funding (£46m in 2018/19 price base). At SHET's request, the funding was not included in the first year of RIIO-ET2 (2021/22) but moved into the final year of RIIO-ET1 (2020/21). This was implemented through the ET1 Legacy PCFM for the November AIP process (2021).

- The expected expenditure in the RIIO-ET2 period was used to set PCDs. The associated allowances for each PCD represent only the expected expenditure in the RIIO-ET2 period and not any expenditure on the RIIO-ET1 period.

[49] RIIO-2 Final Determinations – NGET annex (published 3 February 2021) – paragraphs 3.35- 3.36. See also page 38, Table 7 and footnote of the same document.
[50] The value of the negative adjustment was based on our calculation of excess non-load related capex allowance in RIIO-ET1 (£-166m in 2018/19 price base). See RIIO-2 Final Determinations – NGET annex (published 3 February 2021) – paragraphs 3.72- 3.74.

Methodology proposed at consultation

NGET

10.8. The proposed methodology described in the consultation sought to determine the required modifications to the RIIO-ET2 licence to amend the existing PCDs and set the new PCDs for the crossover projects based on the information provided by NGET.

10.9. We proposed to assess documentary evidence to be submitted by NGET to ascertain:

- the revised forecast output delivery dates for each of the applicable crossover projects, and that the information is based on accurate and reliable evidence; and

- any assumptions or sensitivity analysis applied by NGET in determining the revised delivery date forecast and/or evidence on relevant factors that may have a bearing on the delivery date and the outputs expected to be delivered.

10.10. No changes to the ET1 Legacy PCFM were proposed because the PCD methodology would be used to clawback the allowance if a project is not Fully Delivered by modifying RIIO-ET2 totex allowances.

SHET

10.11. We proposed to consider all changes to the timing and scope of output delivery associated with the five original crossover projects. We would then use it to inform our view of the adjustments necessary to the PCDs.

10.12. We proposed to assess documentary evidence to be submitted by SHET to ascertain:

- the revised forecast output delivery dates for each of the applicable crossover projects, and that the information is based on accurate and reliable evidence; and

- any assumptions or sensitivity analysis applied by SHET in determining the revised delivery date forecast and/or evidence on relevant factors that may have a bearing on the delivery date and the outputs expected to be delivered.

10.13. No changes to the ET1 Legacy PCFM were proposed because the PCD methodology would be used to clawback the total allowance (including T1 allowances) if a project is not Fully Delivered by modifying RIIO-ET2 totex allowances.

Consultation responses

NGET

10.14. NGET disagreed with elements of the proposed approach for crossover projects without a volume driver and cited a range of factors in support of this view. These factors are summarised below.

- An approach that seeks to capture connection outputs as PCDs does not, in NGET's view, align with the principles of the RIIO Framework. NGET's contention is that the PCD process was introduced for Wider Works projects in RIIO-ET2 and was intentionally not applied to generation and demand connection projects[51] because the agreed volume driver will automatically adjust allowances depending on the outputs ultimately delivered. NGET therefore opposes the introduction of a RIIO-ET2 mechanism (ie PCDs for crossover projects without volume drivers) to the RIIO-ET1 framework as a means to adjust funding.

- The approach proposed in the consultation increases regulatory risk. This is based on NGET's view that converting RIIO-ET1 and RIIO-ET2 outputs associated with crossover projects without volume drivers to PCDs changes the established rules of the RIIO-ET1 framework, and effectively re-opens an element of the RIIO-ET2 price control. NGET is of the opinion that this constitutes a retrospective change to the funding framework and consider that this will have a negative impact on confidence in making investment decisions over the price control period by undermining certainty in the funding mechanisms used for these decisions.

- The proposed process does not fully close out the arrangements at the end of the RIIO-ET1 period and will create more complicated arrangements. It is NGET's view that Ofgem is already in a position to assess and agree the funding position in RIIO-ET1. NGET's preferred approach to adjusting the provisional allowance provided and to account for any delay or non-delivery of outputs beyond baseline assumptions through

[51] Except in the case of one connection output, which NGET considers to be "*exceptional*".

the existing agreed RIIO-ET2 price control uncertainty mechanisms for the investment types concerned.

- Using RIIO-T1 closeout in this manner was not trailed in the RIIO-ET2 FD documentation.

10.15. NGET further noted that if a clawback were implemented through the proposed PCD mechanism the RIIO-ET2 licence would need to ensure that the existing uncertainty mechanism did not also operate to clawback the funding position.

10.16. NGET also disagreed with the omission of the Bramford Stage 2 project[52] for consideration within Ofgem's closeout in this area, noting that leaving the RIIO-ET1 element of this investment unfunded is not appropriate. NGET explained that while the investment was not included in the forecast expenditure incurred in the RIIO-ET1 period initially notified to Ofgem, and did not form part of the positive allowance adjustment[53] (described in paragraph 8.4 of the consultation), changing circumstances have meant that the ability to recover the efficiently incurred costs of this project through the RIIO-ET1 framework[54] is no longer viable. NGET therefore requests that the investment be included in Ofgem's closeout process.

SHET

10.17. SHET agreed with the proposed approach set out in the consultation; each of the applicable projects[55] will receive funding for a successfully delivered outcome, and the PCD will include the full RIIO-ET1 and RIIO-ET2 allowance for each crossover project reflecting Ofgem's assessment of total efficient costs.

10.18. SHET sought clarity on the treatment of indirect costs, indicating that the expression of the proposed ET1 Legacy adjustment in the consultation does not recognise the recovery

[52] Works to extend Bramford substation that do not form part of a TPWW claim submitted by NGET for the cancelled Bramford–Twinstead project to be assessed as part of the arrangements set out in Chapter 4.
[53] At the time of providing information to support our assessment of load related outputs that were considered to be unfunded by the T1 price control, NGET anticipated making a separate TPWW funding request to recover the efficient RIIO-ET1 costs incurred in progressing construction activities associated with the Bramford Stage 2 investment. No costs were therefore submitted or included in our assessment to determine the value of the positive allowance adjustment confirmed in our FD.
[54] NGET explains that it no longer considers the Stage 2 investment to fall within the scope of the TPWW provisions because the works support the new Bramford-Twinstead overhead line scheme that was submitted in the RIIO-ET2 business plan, has funding agreed in FD and is progressing toward a 2028 completion date.
[55] East Coast 275kV Upgrade, Kinardochy, North east 400kV Upgrade and Tealing 275kV Busbar.

of associated indirect costs for the specified projects. SHET said that an adjustment is needed to account for the associated additional indirect costs, the allowance to be based upon the agreed T2 opex escalator rate.

Our views

NGET

10.19. We have carefully considered each element of NGET's opposition to the proposed approach for the provision of funding for crossover projects that are not subject to a volume driver. Our views on each area are set out below.

10.20. Alignment with the principles of the RIIO-1 framework - we proposed to introduce a PCD for each specific project with the full RIIO-ET1 and RIIO-ET2 allowance, and that any identified works would be subject to our existing PCD methodology. NGET disagreed with the proposed approach and considered that it introduces the use of a RIIO-ET2 mechanism (PCDs) to a RIIO-T1 framework. We have considered this response and remain of the view that the proposed approach is consistent with the principles of RIIO as it will ensure that ETOs are funded for total efficient spend incurred in successfully delivering the outputs.

10.21. Furthermore, we disagree with the view that the application of the PCD process for bespoke projects within the RIIO-ET1 closeout process is inconsistent with the application of the RIIO-1 framework, noting that:

- the investments had no mechanism in the RIIO-ET1 price control to recover what is deemed to be efficient incurred spend and would have remained unfunded in the absence of some form of intervention. We consider the approach proposed in the consultation to be justified and consistent with a central principle of the RIIO-1 Framework to ensure NGET receives funding for efficiently incurred costs. We also note that being flexible in our approach to remunerate in this manner is in the longer term interests of both consumers and ETOs to ensure that efficient and effective investment decisions are made and to assist in the delivery a safe and secure transmission network.

- the application and the use of PCDs is not subject to restriction that prohibits their use in the proposed manner, and

- the process does not invalidate or contradict other principles embedded in the RIIO-ET2 volume driver mechanisms.

10.22. Increased regulatory risk – we note NGET's position that the proposed approach creates a new level of regulatory risk, which we understand to be driven by the view that the proposal (to introduce PCDs) seeks to replace a funding reconciliation process which is already in place (volume driven RIIO-ET2 mechanisms). We accept that both approaches contain the ability to adjust allowances should outputs not be delivered or be delayed, but we remain of the view that the application of an approach utilising PCDs, reflecting our assessment of the total efficient costs of each project, provides an approach that is consistent with the principle of funding efficient investment while still maintaining appropriate protection to consumers from the costs of inefficient investment. We also consider the approach to be proportionate and note that:

- its application will result in no additional complexity relative to other similar areas of the closeout arrangements (see chapter 9) or the operation of the RIIO-ET2 framework.

- any perceived complexity is unlikely to be material (relative to NGET's preferred application of T2 UMs by investment type) and will be offset by associated improvements in the transparency of the regulatory arrangements and to the RIIO-ET2 annual reporting information throughout the price control period.

- we strongly disagree that developing a regulatory approach to provide a positive allowance adjustment for projects that would otherwise be unfunded increases the regulatory risk of NGET. Conversely, we consider that the provision of allowance reflecting the total efficient costs of each project directly reduces the risk for these projects.

- our provisional allowance adjustment reflected our assessment of the project information received from NGET and the strength of the needs case in recognition that NGET included costs in the RIIO-ET2 BP submission and received funding in the RIIO-ET2 baseline for the investments. It is rational for us to apply a mechanism developed as part of the RIIO-ET2 framework and to provide funding on a total efficient cost basis.

- the funding approach expressed in FDs, and the further detail set out through the closeout process, serves to demonstrate that Ofgem remains willing to respond to circumstances that are outside the normal parameters of the regulatory framework and to actively address the challenges of a changing energy landscape where investments are demonstrated to be in the consumers' interest. We remain of the view that the approach to provide funding for these specific crossover projects is in the interests of both NGET and existing and future consumers.

10.23. Delays in output delivery - NGET commented that delaying the funding of these costs introduces regulatory risk as settlement will require a further process to capture expenditure incurred that could span multiple price control periods. We acknowledge that there is potential for delay in the delivery of the bespoke investments and that future assessment will be required as a result. However, we hold the view that the necessary regulatory information can be retained and utilised at the appropriate time to ensure the efficient spend is appropriately funded. Furthermore, we note that the PCD framework is designed such that work is ongoing to develop other existing mechanisms to potentially recover expenditure where the factors driving non-delivery are outside the direct control of ETOs. Potential revisions to the RIIO-ET2 licence are discussed elsewhere in the document and will be progressed through the forthcoming statutory consultation process.

10.24. Not trailed in FD – NGET considered the proposed approach represents a change to the RIIO-ET2 settlement as it was not trailed in the RIIO-ET2 FD. In response, we note that the issues was first flagged to us in late 2020 and our thinking on this issue has evolved as a result of further engagement and discussion with NGET. A timeline of engagement and development in our thinking is briefly summarised below.

- Our RIIO-2 Draft Determinations for the ET sector[56] set out our proposed approach for dealing with funding for capex projects starting in RIIO-1 and completing in RIIO-2. We said that where funding provided in RIIO-ET1 was fixed and the "true-up" could be done with certainty together with our determination of the net amount to be allowed in RIIO-ET2 we would reflect such true-up in our proposed RIIO-2 baseline totex allowance in our FDs. In cases where we needed to confirm the actual funding amount and eventual outturn costs after the end of RIIO-ET1, we proposed to carry out the adjustment as part of the RIIO-ET1 closeout process.

- Further discussions with NGET took place in late 2020 to establish the evidential trail of the LR crossover projects that NGET considered to be unfunded by the T1 price control (as no T1 mechanisms existed to provide allowances in the RIIO-1 period). These discussions were reflected in the RIIO-2 FD for NGET[57] regarding the funding

[56] RIIO-2 Draft Determinations for Transmission, Gas Distribution and Electricity System Operator | Ofgem
[57] https://www.ofgem.gov.uk/system/files/docs/2020/12/final_determination_nget_annex_0.pdf

of these crossover projects, which confirmed the creation of a provisional allowance in the RIIO-2 baseline capex allowance for NGET[58] and our intent to verify the projects and provisional allowance via the RIIO-1 closeout process.

- NGET provided additional information as part of the annual reporting process in July 2021, which provided further detail on elements of the proposed crossover projects.

10.25. We remain of the view that the FD and our engagement with NGET clearly signalled our intent to further consider the applicable projects and to make to take account of costs incurred in the RIIO-1 period. The closeout consultation provided further detail on the nature of the closeout envisaged; to create a PCD for each project, reflecting our assessment of the total efficient costs for the project and the anticipated output delivery timescale.

10.26. In response to the comment raised on the operability of the PCD framework (paragraph 10.16 above), we agree that the T2 licence will need to ensure that the existing uncertainty mechanism operate appropriately ie. no double clawback. We will develop and set out our proposals in the forthcoming statutory consultation on changes to the RIIO-ET2 Licence. The work will reflect the similar points raised by NGET in the context of chapters 4 and 6.

10.27. In our consultation document our proposals were focused only on the list of schemes that formed the basis of the provisional allowance adjustment. This did not include provision for the RIIO-ET1 element of the Bramford Stage 2 project. Through the response and further engagement, NGET has provided a further information on the investment and its drivers which has provided justification for inclusion in the closeout process.

10.28. Following consideration of the points raised in relation to this specific investment, we do not believe leaving the RIIO-ET1 element of the investment unfunded is appropriate as it would be inconsistent with our treatment of similar crossover projects where no T1 mechanisms existed to provide allowances in the RIIO-1 period.

[58] Of the document in footnote 6 above, Pg. 38, Table 7 and footnote 17; Pg. 46: paragraphs 3.35-3.36.

10.29. We have therefore decided to introduce a new RIIO-ET2 PCD to capture this crossover project reflecting our assessment of the total efficient costs for the project and the anticipated output delivery timescale.

10.30. To enable this approach we will also need to make adjustment to special condition 3.38 of NGET's T2 Licence to adjust the value of the offset allowance to reflect the value provided by all PCDs and their associated allowances. We can consider any additional details provided through the performance submission in working groups.

SHET

10.31. We agree that the PCFM adjustment will incorporate the associated indirects allowance using the opex escalator rate. We note that this approach is in accordance with the RIIO-ET2 PCFM Guidance and the Price Control Financial Handbook[59].

Closeout methodology Decision

10.32. Following consideration of the consultation response we are applying the approach to closeout that was consulted on with an adjustment to expand the scope to include the Bramford Stage 2 investment.

10.33. We will continue to engage with NGET to establish the additional information that is required at the closeout implementation stage to incorporate the Bramford Stage 2 works.

[59] Published in April 2022, the RIIO-ET2 PCFM Guidance document and PCFH Handbook are available from the Ofgem website: Notice of proposed modifications to the Regulatory Instructions and Guidance and Regulatory Reporting Packs for RIIO-2 | Ofgem and Proposed direction to make modifications to the ESO and ET2 Price Control Financial Instruments | Ofgem

11. Adjustment for SPT's connection volume driver clawback

This section details our Decision on the methodology for implementing a 'clawback' of RIIO-ET1 baseline allowance through the operation of the SPT's sole-use generation connection volume driver mechanism within the T1 Licence. This chapter applies to SPT only.

Background

11.1. RIIO-ET1 arrangements included a volume driver funding mechanism for SPT which provides additional funding for the connection of generation stations and the associated increase in capacity connected to SPT's network, measured by the increase in megawatt. This investment category was referred to as "sole use infrastructure".[60]

11.2. RIIO-ET1 provided SPT with a baseline allowance for works to connect new generation stations with an associated level of generation capacity (2503MW) .

11.3. If requests for generation connections exceed the specified baseline level, SPT's funding will be automatically adjust the baseline allowance based on the application of an agreed unit cost rate in the T1 Licence. Conversely, if the total capacity of generation connected to SPT's transmission network is less than the baseline level , revenues would be subject a negative adjustment (or 'clawed back') per MW shortfall based on the same unit cost rate.

11.4. The output delivered by SPT under the RIIO-1 mechanism is significantly lower than the baseline output threshold due to the reduction in the number and size of customer connections observed across the period. A clawback of allowance is required. The closeout process will facilitate the clawback adjustment through the PCFM.

[60] A separate volume driver mechanism was designed to provide funding to SPT for transmission infrastructure works associated with the connection of multiple new or additional generating stations, referred to as 'shared use infrastructure' and measured in the resultant increase in network capability or megavolt ampere. The revenue associated with both categories of infrastructure asset (sole and shared use) is included in the calculation of Allowed Revenue and recovered from users of the NETS through TNUoS charges.

Methodology proposed at consultation

11.5. We proposed that as part of the closeout process for RIIO-ET1 we would:

- verify the assets delivered in the sole-use infrastructure category that contribute to the 2503MW output threshold, delivered between 1 April 2013 and 31 March 2021.
- verify the finalised actual costs incurred in the delivery of those assets and validate the MW delivery against the threshold capacity in the T1 Licence.
- verify the calculation method applied to determine the value of the clawback to be authorised through the closeout process.
- adjust allowances for RIIO-ET1 in the ET1 Legacy PCFM for the subsequent AIP process

Consultation responses

11.6. One respondent (SPT) commented on the proposed methodology in the closeout consultation and agreed with the proposals to true-up allowances related to sole-use infrastructure outputs set out in SpC 6F of SPT's T1 Licence.

Our views

11.7. No further action required.

Closeout methodology Decision

11.8. Our Decision is to implement the methodology that we consulted on - see Appendix 9.

12. Adjustments for SHET's VISTA allowance

This section details our Decision on the process applicable to the adjustment of RIIO-ET1 allowed expenditure for costs incurred by SHET on projects under SpC 6G of the T1 Licence. This chapter applies to SHET only.

Background

12.1. RIIO-ET1 provided funding for works to assess and mitigate the visual impact of existing electricity infrastructure on national parks and National Scenic Areas within the SHET network area. For the Scottish ETOs, this is known as VISTA (Visual Impact of Scottish Transmission Assets).

12.2. We approved[61] funding for SHET to deliver three projects (Sloy, Glen Falloch and Killin) to reduce the impact of its electricity transmission infrastructure on the visual amenity of the Loch Lomond and the Trossachs National Park. These projects are expected to be completed within the RIIO-ET2 price control period (ie. after 31 March 2021).

12.3. SHET explained that progress has been delayed in some instances, with failure to deliver during the RIIO-ET1 price control period attributable to delays associated with the COVID-19 pandemic. In these cases, SHET has confirmed that costs have been incurred within the first year of the RIIO-ET2 price control period.

12.4. SHET requested that outperformance in the RIIO-ET1 period be balanced against projected underperformance in the RIIO-ET2 period and the result reflected in the RIIO-ET1 closeout assessment.

Methodology proposed at consultation

12.5. We proposed that the scope of the RIIO-ET1 closeout (and what is permissible in the context of closeout) is determined by the TI Licence and does not accommodate the balancing exercise proposed by SHET.

[61] https://www.ofgem.gov.uk/sites/default/files/docs/2020/07/1_decision_assessmentletterglenfallochsloy.pdf and https://www.ofgem.gov.uk/publications/direction-new-enhancing-pre-existing-infrastructure-projects-she-transmissions-electricity-transmission-licence

12.6. The consultation also stated (paragraph 14.8) that:

- the parameters of the T1 Licence dictated that delayed projects would be the subject of a downward adjustment in respect of costs incurred in the RIIO-ET1 period, and
- projects scheduled for delivery in RIIO-ET2 are out of scope of RIIO- ET1 closeout.

Consultation responses

12.7. One respondent noted a possible misunderstanding in relation to three of the VISTA projects, Sloy, Glen Falloch and Killin, which are designated to be delivered in 2022-2024, and are not T1 deliverables that are subject to delay. This means that the proposal to reduce allowances in RIIO-ET1 to the level of costs incurred is impractical unless it is offset by a corresponding mechanism to adjust allowances up in RIIO-ET2 by the same value (which was not indicated as part of the proposed methodology as such an adjustment is out of scope of the RIIO-ET1 closeout process).

Our views

12.8. We acknowledge that three of the VISTA projects, Sloy, Glen Falloch and Killin, are designated to be delivered in 2022-2024, and are not T1 deliverables that are subject to delay. We have decided that no downward adjustment to RIIO-ET1 allowances will be made as part of ET1 closeout for these projects.

12.9. For the avoidance of doubt, we remain of the view expressed in the consultation (paragraph 14.7) that balancing is out of scope of the RIIO-ET1 closeout process, ie. we will not balance the actual performance in T1 against the forecast performance in T2.

12.10. We also note that there is no indication that there will be any failure to deliver the required outputs for the total allowances determined for the applicable projects.

Closeout methodology Decision

12.11. Our Decision is not to implement the methodology that we consulted on for the reasons stated above. No closeout is required for the three VISTA projects identified in the consultation, Sloy, Glen Falloch and Killin, which are designated to be delivered in 2022-2024.

12.12. We can also confirm that, as stated in the July 2021 decision for the Killin mitigation project, we will adjust SHET's RIIO-T1 allowed expenditure by £1.01m (in 2009/10 prices) for costs incurred on the project in 2020/21 as part of the ET1 closeout.[62] The adjustment will be made to the term Enhancements to Pre-existing Infrastructure (row 20 of the SHET input tab) of the RIIO-ET1 Legacy PCFM.

12.13. We have decided to proceed with the methodology as provided in Appendix 10.

[62] Killin mitigation project licence direction.pdf (ofgem.gov.uk). Due to the timing of the decision there was no provision to make the adjustment to T1 allowances at the time.

13. Adjustments for WHVDC project

This section explains our approach for closing out allowances associated with the delivery of the WHVDC project. This applies to NGET and SPT only.

Background

13.1. The Western high-voltage direct current (WHVDC) link is a project that transports electricity via a subsea cable between the west coast of Scotland and Wales. The project was a joint venture between NGET and SPT to transmit more electricity between Hunterston in Scotland and Deeside in Wales.

13.2. The allowed expenditure, output deliverable and delivery date for the WHVDC project were set out in special licence condition 6I[63] within the T1 Licence of SPT and NGET.

13.3. In January 2020 we launched an investigation[64] into the performance of NGET and SPT in delivering the subsea cable component of the WHVDC link. This has resulted in the licensees agreeing to pay a redress[65] package of £158 million for delay of the delivery of WHVDC link.

Methodology proposed at consultation

13.4. No ET1 closeout methodology was proposed because the outcome of the investigation has meant that all adjustments relating to the WHVDC project, including rephasing allowances, have been made in the 2021 AIP.

13.5. However, the consultation noted our intention to document the changes from the 2019 PCFM as part of a closeout workbook. Specifically, we will record the adjustments to:

- Baseline strategic wider works outputs (WWE)
- Legacy price control adjustments to allowed revenue (LAR)

[63] SpC 6I. Specification of Baseline Wider Works Outputs and Strategic Wider Works Outputs and Assessment of Allowed Expenditure
[64] https://www.ofgem.gov.uk/publications/investigation-national-grid-electricity-transmission-plc-and-sp-transmission-plc-and-their-compliance-obligations-relating-western-hvdc-subsea-link
[65] https://www.ofgem.gov.uk/publications/ps158-million-redress-two-year-delay-major-western-link-subsea-cable

- Adjustment to legacy price control adjustments to RAV (LRAV)

Consultation responses

13.6. Two respondents agreed that there are no further adjustments required to allowances relating to the construction and commissioning of the WHVDC project. The necessary adjustments were incorporated in the respective company submissions for the 2021 regulatory reporting process.

Our views

13.7. No further action required.

Closeout methodology Decision

13.8. The financial revisions have been implemented and no closeout is required.

14. Treatment of innovation allowances

This section details our Decision on the process to be applied to the Network Innovation Allowance mechanism. This process applies to all electricity transmission network owners (ETOs).

Background

14.1. The RIIO-ET1 innovation stimulus included the Network Innovation Allowance (NIA): an annual allowance that each of the RIIO network licensees received throughout RIIO-1 to fund smaller scale innovative projects as part of their price control settlement. Network companies report their spending on innovation funded by the NIA.

14.2. To prevent a "cliff edge", beyond which NIA funding is unavailable, potentially resulting in downturn in innovative activity towards the end of RIIO-ET1 to the detriment of consumers, we decided it was necessary to adjust the end date for spending RIIO-ET1 allowances to allow carry over of any unspent allowance in the final year of RIIO-ET1 into the first year of RIIO-ET2.

14.3. As decided in RIIO-2 Final Determinations[66], we are enabling network companies and the ESO to carry forward unspent 2020/21 NIA allowances into 2021/22 (the 'carry-over Network Innovation Allowance', the CNIA[67]). This allows licence holders to carry any unspent 2020-2021 RIIO-ET1 NIA allowance over into the first year of RIIO-ET2 in 2021/2022, to spend on projects that had already been started by 31 March 2021.[68]

Methodology proposed at consultation

14.4. We proposed that network companies and the ESO would be required to report any costs efficiently incurred against their CNIA. Companies would then be able to recover those efficient costs (provided spending is less than the cap calculated according to the RIIO-ET1 NIA licence condition[69]).

[66] RIIO-2 Final Determinations – Core Document, paragraphs 8.81-8.85.
[67] SpC 5.3 (Carry-over Network Innovation Allowance) of the T2 Licence.
[68] Version 4 of the RIIO-ET1 Electricity NIA Governance was published in March 2021, available here: https://www.ofgem.gov.uk/publications/riio-1-nia-guidance-documents-revision-additional-requirements-riio-2-cnia-0
[69] Provided the spend is less than the cap calculated according to SpC 3H of the Electricity Transmission Licence as was in force until 31 March 2021.

14.5. We also proposed not to do anything with regard to the closeout for projects under the other RIIO-ET1 innovation stimuli (Network Innovation Competition or the Innovation Rollout Mechanism).

Consultation responses

14.6. All respondents agreed with the proposals in relation to the closeout of innovation allowances as set out in the consultation, and noted that the approach is consistent with the RIIO-T2 Licence. However, one respondent sought clarification on the intent of the proposal listed in the consultation (paragraph 15.4) which implies that CNIA will be reported prior to 1 April 2022.

Our views

14.7. In response to the issue in relation to paragraph 15.4 of the consultation publication, we can confirm that costs will be reported in the RIIO-ET2 RRP (due in July 2022) and subsequently input to the RIIO-ET2 PCFM via the AIP and therefore contribute to Allowed Revenue.

Closeout methodology Decision

14.8. No further action is required and no closeout is required.

15. Other considerations

This section details our Decision on other issues raised by electricity transmission network owners (ETOs) for consideration for inclusion as part of the ET1 closeout.

15.1. In our January 2022 consultation, we stated our view of the elements of the RIIO-ET1 price control that we considered needed to be "closed out". The preceding chapters set out our Decisions in relation to the methodology to closeout different elements of the RIIO-ET1 price control. This chapter summarises specific issues identified in the responses to the methodology consultation, where a request has been made for further consideration and inclusion as part the ET1 closeout arrangements of matters not addressed in chapters 2 to 14.

15.2. This chapter provides a summary of each issue and either (i) our reasons for our Decision not to address the issue as part of the RIIO-ET1 closeout arrangements, or (ii) our justification in support of our decision to address the issue at ET1 closeout.

Non-Rechargeable diversions (SPT only)

15.3. Non-rechargeable diversions are triggered by landowners as a result of the ownership of land being transferred or where no current valid land rights exist due to historical land-rights no longer being valid. Whilst in some cases this can be resolved by securing new land rights, the valuation principle for securing those rights is based on the associated loss which, in some cases, is a requirement to re-site the infrastructure.

15.4. SPT explained the general stages and processes involved in securing access to equipment located on third party land.

- An ETO would have originally obtained rights for their equipment through a bilateral agreement with the land owner (also known as a "wayleave"[70]). The rights granted

[70] A "wayleave" is a written agreement which permits the installation or retention of company apparatus on the land. It is typically granted for either a fixed term or contain a right for the landowner to terminate it subject to giving an agreed notice period.

under an agreement will fall away with a change in ownership of the land, unless the new owner enters in to a new wayleave agreement.

- In parallel, negotiations for a voluntary agreement of compensation, and a servitude right (also referred to as an easement[71]) for the equipment to be retained in-situ are started with the land owner. Alternatively, an ETO may seek to replace or divert the equipment, securing land rights as part of that process when a financial settlement cannot be agreed. The most cost-efficient route will be followed if a negotiated settlement can be reached.

- In some instances where a land owner terminates the wayleave agreement to remove their equipment, and where negotiation has failed, this will initiate the application for a "Necessary Wayleave"[72] process to protect the equipment.

15.5. SPT commented that the RIIO-ET1 business plan submission was based on intelligence available at the time based on the historic precedent from the prior price control, which suggested a very low number of claims and associated compensation.

15.6. SPT noted that there has been a material change in this area across the RIIO-ET1 price control period to the business plan forecast position. This has been driven by a number of factors, including recovery in the UK economy (prior to the Covid pandemic), which generated several diversion projects around greater Glasgow area. This resulted in additional investment which was not funded within the provisions of the RIIO-ET1 framework.

15.7. It is SPT's contention that the materiality of change in activity and funding servitudes was not reasonably foreseeable and that the resultant change merits consideration of a review of existing provisions as part of the ET1 closeout process.

[71] An easement creates a permanent right for to keep equipment installed on the land. An electricity company would usually pay compensation in return for the grant of an easement.
[72] The termination of electricity wayleaves is regulated by the Electricity Act 1989. The electricity company enjoys the right to apply to the Secretary of State for a new "necessary wayleave" to be granted.

Our views

15.8. SPT acknowledge that they did not request funding in this area as part of the RIIO-ET1 price control submission and were not provided with any funding for such works as part of the RIIO-ET1 settlement.[73]

15.9. We note that this activity is solely driven by customers and has arisen since the RIIO-ET1 price control settlement was agreed, hence, no funding mechanisms were identified.

15.10. We note that the scope of the RIIO-ET1 closeout (and what is permissible in the context of closeout) is determined by the TI Licence which does not accommodate consideration of a review of existing provisions as part of the ET1 closeout process proposed by SPT.

15.11. Our Decision is not to introduce a methodology to provide explicit funding in this area for the reasons stated above.

Crossover Projects without Volume Driver (SPT only)

15.12. Chapter 10 sets out detail of our methodology in relation to specific crossover LR projects identified by SHET and NGET that are not subject to adjustment through the volume driver arrangements under the T1 Licence.

15.13. The volume driver mechanism that governs the funding of new generation connection schemes was introduced for RIIO-ET1 as Special Condition 6F of the T1 Licence. Whilst there are acknowledged differences in the mechanisms for the three ETO's (due to ETO choice) a number of schemes that are described in the RIIO-ET2 Licence as PCDs[74] incur expenditure across a price control boundary.

15.14. It is SPT's contention that it should not be disadvantaged when delivering investment that is directly driven by individual users where it crosses price control boundaries. It is SPT's view that the rationale for arrangements in relation to investment in specific crossover projects (without volume drivers) applies equally to all ETO's and request

[73] The RIIO-ET1 baseline non-load related allowance for SPT did include provision for conversion of overhead line wayleaves to a servitude. See 2012 FP document paragraph XX
[74] In Special Licence Condition 3.9 of the RIIO-ET2 Licence, for example.

Ofgem's agreement to make a submission on a similar basis as NGET & SHET under the proposed methodology in the closeout consultation (paragraphs 8.13-8.15).

Our views

15.15. We note that in the FD we set baseline funding for the RIIO-ET2 period and set PCDs. Our key consideration remains whether each of the crossover LR projects (upon which the provisional allowance was based) will progress and complete as expected and will deliver the outputs anticipated.

15.16. We also note that our proposed closeout approach seeks to protect consumers from potential reductions in scope or cancellations in the identified crossover projects (and exposure to the associated redundant spend in the RIIO-ET1 period in particular) and to clarify our intention to clawback the appropriate funding in those instances.

15.17. While we agree that the rationale presented in the closeout consultation (paragraph 8.8) is applicable to all ETOs, and consent to SPT's request to submit information for consideration following the agreed methodology listed in the consultation (paragraph 8.14), we note that we have no clarity on the specific projects in question or on the robustness of the supporting information on which to make an assessment. We therefore reserve the right to make no adjustments upon receipt and assessment of the performance assessment submission.

15.18. It is our intention that any projects that cross price control periods that are described as PCDs will indicate the efficient total project cost along with a relevant profile. This will better inform stakeholders on the agreed funding at the point of determination and assist future deliberations.

15.19. We also acknowledge that there is scope for interaction between this area and pre-construction funding arrangements provided for in RIIO-ET1 (see chapter 7). We note that SPT's submissions in each area must be separate and distinct and demonstrate that funding is appropriately allocated.

16. Next steps

16.1. We will engage with ETOs as necessary to implement the closeout methodologies and effect any necessary revenue adjustments as part of the November 2022 AIP.

16.2. All network companies will be required to submit a final performance assessment submission to confirm the value of the closeout adjustment to be made and to provide further information to explain and justify the funding and its profiling in each closeout area.

16.3. The submission will include the following information as a minimum:

- variance analysis to verify the difference between actual LR capex incurred, revenues and/or outputs and the assumptions taken as part of setting the RIIO-ET1 baseline.

- confirmation and explanation of any data quality issues over the RIIO-ET1 Price Control Period which have affected LR capex, revenue and/or outputs.

- detail of changes to activities relative to the activities that were detailed in the ETO's RIIO-ET1 business plan submission (that was used as the basis of setting the RIIO-ET1 baseline).

16.4. We expect to receive the final performance assessment submission from each company on or before 4 July 2022.

16.5. All ETOs have already submitted its 2020/2021 Regulatory Reporting Pack (RRP) and provided an initial indication of the information in support of claims in most areas. In many cases, for example settlement under SpC 3L of the T1 Licence (see chapter 7), Ofgem expects that this information will be sufficient to enable us to undertake a robust assessment of each ETOs' RIIO-ET1 performance and determine the extent of any over or underperformance against its targets and/or allowances. We do not envisage a material update to the relevant information already provided except to include finalised cost data and/or minor narrative updates to aid our understanding of the claim and to reflect the completion of the price control period.

16.6. In some cases, however, more detailed information may be required for submissions to enable our determination as detailed in the relevant chapters. An example includes the information on PSUP (chapter 5) and crossover projects that are not subject to adjustment through the volume driver arrangements under the T1 Licence (chapter 10).

16.7. Where further additional information is required we will engage with ETOs and request this as necessary.

16.8. We will consult separately outside of the closeout process on the licence modifications required to give effect to the closeout decision and we intend to make the necessary licence modifications ahead of the November 2022 AIP.

Appendix 1 – Financial methodologies

Introduction

We will implement RIIO-ET1 closeout methodologies via the Legacy PCFM by revising both variable ("blue box") and non-variable ("yellow box") values or modifying calculations as set out in the closeout methodologies. This provides the greatest transparency about the nature of the ex-post adjustment, a reliable way of calculating the appropriate true-up and provides a useful data source for the final RIIO-ET1 performance in the future.

We will implement the methodologies in the November 2022 AIP, though note that corrections can be made in subsequent AIPs if necessary.

Paragraph 8.14 of the Price Control Financial Handbook already sets out a process where pre-existing RIIO-1 methodologies continue to be used to calculate LAR values in 2021/22 and 2022/23, as well as revise LRAV values and tax pool balances. Paragraph 8.25 of the ET2 Price Control Financial Handbook posited that new methodologies would be implemented to calculate additional true-ups using the same functional process as the RIIO-1 methodologies.

We will modify Chapter 8 of the handbook to include instructions to revise specific legacy values, referencing this closeout decision. We will also set out any additional details necessary to give effect to the process set out below.

While we will document changes from the last published 2019 ET1 PCFM, the starting model for implementing closeout will be the November 2021 ET1 Legacy PCFM; therefore, the values of legacy MOD will be calculated comparing to the "recalculated base revenue" values saved at that time.

Phasing of the impact of closeout

In the current AIP process, the cumulative impact of all changes is included in the MOD value for the following year. We intend to phase the impact, and as a starting assumption will phase over the final three years of RIIO-2. However, we delay our final decision until the statutory consultation, after evaluating the magnitude of the closeout true up.

Methodology

An adjustment calculation will involve the following steps.

1. Ofgem or the licensee will input changes to RIIO-1 values in the Legacy PCFM, aligning to the submitted reporting workbook containing the closeout methodologies.

2. The Legacy PCFM is used to calculate legacy MOD (LMOD) value(s), which is in constant 2009/10 prices.

3. Through working groups, Ofgem and the licensee will determine the phasing of the legacy MOD value, starting with an assumption of the last three years of RIIO-ET2. The November 2021 AIP Legacy PCFM does not include the functionality for the calculation of LMOD values beyond 2022/23, and revisions will be made as required to accommodate this process.

4. Through working groups, Ofgem and the licensees will establish the most straightforward process for inflating these values in to nominal prices using RPI and truing up these values to outturn(such as using the RPIF and TRU terms in the Revenue RRP).

5. Ultimately a LMOD value in £m nominal contributes to the LAR term in the RIIO-2 PCFM.

6. Other inputs to the Revenue RRP are filled in by the licensee as necessary for finalizing the value of LAR

7. The final revenue RRP values and legacy MOD complete the 'LAR' input block in the RIIO-2 PCFM.

8. Legacy RAV additions are input from the legacy PCFM into the RIIO-2 PCFM, after being converted to 18/19 prices.

9. The tax pool balances are input from the legacy PCFM into the RIIO-2 PCFM, after being converted to 18/19 prices.

10. The licensee updates all other variable values in the RIIO-2 PCFM.

11. The RIIO-2 model calculates Allowed Revenue for the following year, which will include the financial impact of closeout via the ADJ, LAR, and K terms (as well as future values of Calculated Revenue).

Appendix 2 - Adjustments to true-up with connection payments

1. Establish the original forecast profile of capital contributions (listed as negative expenditure) included in Baseline Load Related Allowance for the investment categories relevant to sole use entry and sole use exit connection activity categories.

2. Establish the actual profile of capital contributions received (listed as negative expenditure) against the investment categories noted in step 1.

3. Deduct each profile value in step 2 from the value in step 1 to determine the annual profile of the control period connection contributions true-up adjustment.

4. Update the current annual charges forecast values in the PCFM to the actuals for the RIIO-ET1 period.

5. The profiles from steps 3 and 4 will be input to the ET1 Legacy PCFM.

    - Row 84, "Non-variant allowed load related capex expenditure" under the "Expenditure", for the customer contributions component.
    - Row 213, "Excluded services revenue" under the heading "Direct Allowed Revenue Terms (DARTs)[75]", for the connection charges component.

[75] Directly Allowed Revenue Term.

Appendix 3 - Adjustments for terminated wider works projects

Our approach will be to assess each of these projects based on documentation to be submitted by NGET in support of its TPWW claims to evidence:

- the initial needs case to justify the start of the works
- the application of the NDP and how it indicates that the boundary transfer capability increase is no longer in the interest of existing and future consumers
- how the change to the needs case has been taken into consideration in a timely manner and works were concluded in line with the directions received from the System Operator
- the boundary transfer capability increase has not been realised in the original RIIO-ET1 timescales
- that the assets associated with above-mentioned projects are stranded and cannot be used subsequently to contribute to other outputs delivered by NGET in RIIO-ET1 or forecast to be delivered in RIIO-ET2 timescales (and which have not been funded through other mechanisms).
- the extent to which any development work, including surveys, ground works and local engagement, can be re-used or will need to be repeated / redone if the boundary transfer capability increase is required in the future, and
- the costs already incurred in RIIO-ET1 in relation to the construction activities of the project, and that these are economic and efficient.

The evaluation process will apply the cost assessment template established to support the review of NGET's 2017 TPWW claim (the North London Reinforcement Project methodology). The methodology enables NGET to report the construction costs of each project and the effect of spend in the previous price control period and/or any prior funding (where applicable).

Closeout will entail verification of the non-reusable expenditure (ie the costs incurred which cannot be used to deliver a different output) and establish the value of efficiently incurred expenditure on construction activity recoverable through the TPWW mechanism for each claim.

An adjustment calculation will involve the following steps.

1. Establish the total expenditure incurred in progressing construction activities in the delivery of an IWW output up to the point of the cancellation of the project for the period, including expenditure incurred in the previous price control period between 1 April 2014 and 31 March 2021. NGET will source this information directly from its internal financial system.

2. Establish the total income received against the projects noted in step 1, the effect of spend in the previous price control period[76] and/or any prior funding[77] (where applicable).

3. Deduct the cumulative value of step 2 from the cumulative value in step 1 to determine the adjustment across the relevant period.

4. The result will be input to the ET1 Legacy PCFM as an adjustment to the relevant company input tab row 19, "Network development and wider works volume driver (NGET only)" under the heading PCFM Variable Values Table.

[76] The total costs within the RIIO-ET1 business plan submission (both pre-RIIO and during RIIO) were used to create a unit cost allowance (UCA) for each system boundary. When an IWW output is not delivered the volume driver claws back an amount of allowed expenditure for the project by multiplying the size of the megawatt output by the applicable boundary UCA. The mechanism may clawback a value greater than the baseline allowance as a result of expenditure forecast to be incurred in the roll-over year in 2012/13.
[77] Closeout will exclude expenditure provided through the TPCR4 Work In Progress mechanism.

Appendix 4 - Adjustments for Enhanced Physical Site Security Costs

Network companies will provide Ofgem with a complete list of PSUP projects that they have been funded for and confirm whether the projects in question have been completed, partially completed, or cancelled.

Network companies are to state the total allowance they are requesting and to provide any evidence that their costs have been efficiently incurred, as appropriate.

For PSUP projects that ETOs have been funded for but which were only partially delivered, ETOs are to detail why the project was not delivered and provide evidence that costs have been efficiently incurred, as appropriate.

Our methodology:

- requires that each ETO submit a report on any difference between actual costs and outputs for PSUP projects that they have received baseline funding for.

- facilitates critical evaluation of the report mentioned in the first bullet in advance of any Final Decision on the direction of RIIO-T1 closeout and before the end of the calendar year.

- sets out the outcome of our assessment and returns any unspent allowance to consumers.

We will endeavour to conclude our assessment on the relevant information submitted in a timely manner in order to feed into the AIP process in November 2022.

The adjustment will be input to the ET1 Legacy PCFM in the relevant company input tab row 14, "Uncertain costs - enhanced security" under the heading PCFM Variable Values Table.

The methodology will facilitate consideration of costs which have been incurred within RIIO-ET1 as a result of UK Government direction for which network companies have not received an allowance.

Appendix 5 - Adjustments for terminated connection projects

We will assess the relevant terms based on documentation to be submitted by NGET in support of its claims to evidence:

- the costs incurred in relation to all projects where the users have terminated generation and demand bilateral agreements.[78] The data will be derived from NGET's financial system SAP for each project (and confirming any other costs prior to termination that NGET considers have received funding from previous price controls).

- that these costs are economic and efficient, including where costs have been recovered through drawing down of security.

- the income received by NGET from termination payments for all projects where the users have terminated generation and demand bilateral agreements. The income data will be taken from customer invoices paid by the customer. The submission will identify specific invoices which remain unpaid by the customer.

- that the assets associated with the above-mentioned project cannot be used subsequently to contribute to other projects or outputs delivered by NGET, or where NGET can recover costs through subsequent sale or scrappage.

We will seek a level of cost explanation and justification from NGET that is proportionate to material claims only. NGET will therefore provide an Engineering Justification Paper for each scheme as part of our RIIO-T1 close-out submission where the costs incurred are equal to or greater than £2m (2009/10 prices). Claims towards the £1m/£2m level will not require a full EJP but should capture the high-level information surrounding the claim.

An adjustment calculation will involve the following steps.

1. Establish the total expenditure incurred where the users have reduced capacity or terminated generation bilateral agreements (TPG) or users have terminated

[78] This table will not include projects which have terminated since April 2019 when National Grid ESO and National Grid ET became legally separate entities within the National Grid Group.

demand bilateral agreements (TPD) for the period between 1 April 2013 and 31 March 2019[79]. NGET will source this information directly from its internal financial system.

2. Establish the total income received against the projects noted in step 1 (TPRG and TPRD). NGET will source this information from customer invoices paid by the customer for the relevant year that the customer is charged.

3. Deduct the cumulative value of income in step 2 from the cumulative value in step 1 to determine the true-up adjustment across the relevant period.

4. The result will be input to the ET1 Legacy PCFM as adjustments to the relevant company input tab:

   - row 23, "Generation connections volume driver" under the heading "PCFM Variable Values Table" in respect of Generation Connections.
   - row 21, "Demand related infrastructure volume driver" under the heading "PCFM Variable Values Table" in respect of Demand works.

[79] In April 2019, National Grid ESO and National Grid ET became legally separate entities within the National Grid Group. National Grid ET will seek the full cost of projects which terminated since April 2019 from National Grid ESO.

Appendix 6 - Settlement of allowances for pre-construction works

We will assess the relevant terms based on documentation to be submitted by the ETOs in support of its claims to evidence:

- the costs incurred in RIIO-ET1 in relation to all PE Outputs set out in Part A of SpC 3L by the end of the RIIO-ET1 price control period (reflecting the impacts of any agreed PE Output Substitutions), and that these are economic and efficient. The data will be derived from ETO's internal financial system for each project and reflect only pre-construction costs incurred within the RIIO-ET1 period.
- the pre-construction engineering works associated with the above-mentioned PE Outputs that have been:
    - completed and delivered on or before 31 March 2021,
    - partially delivered by 31 March 2021, or
    - not delivered by 31 March 2021.
- that the activities associated with above-mentioned projects cannot be used subsequently to contribute to other pre-construction outputs forecast to be delivered in RIIO-ET2 timescales (and which have been funded through other mechanisms).

Based on the information and justification provided by the ETOs submission, we will implement an adjustment calculation that involves the following steps.

1. Establish the total allowed expenditure associated with the PE Outputs that are confirmed by the ETO to have been partially delivered or not delivered.
2. Establish the total allowed expenditure associated with the PE Outputs that are confirmed by the ETO to have been delivered by 31 March 2021.
3. Deduct the cumulative value of allowed expenditure in step 1 from the total value of allowed expenditure in step 2 to determine the adjustment across the RIIO-ET1 period.

4. This will be input to the ET1 Legacy PCFM as an adjustment to the relevant company input tab row 84, "Non-variant allowed load related capex expenditure" under the heading "Expenditure".

Appendix 7 – Adjustments for asset and land related disposals

For asset and related land disposed of in RIIO-ET1, we propose that RAV is adjusted to reflect the net sale proceeds. The proposed methodology would entail netting off the proceeds of disposals from RAV additions, with tax implications also considered. The proposed formula for this true-up is:

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

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

Appendix 8 – Adjustments for crossover volume driver projects

NGET

We will apply the following assessment and adjustment to true up NGET's allowances against the latest view of projects delivering outputs in T1+2 timescales:

- Where projects were forecast in NGET's RR2017 to deliver output in T1+2 (and thus receiving funding already) but will no longer do so, the amount of revenue already received will be returned to consumers[80]

- For those projects that were forecast in NGET's RR2017 to deliver output in T1+2 and either have already delivered or are still expected to do so:

  - Where the project is being delivered in line with the forecast capacity and timing, NGET will keep the allowances on the basis of its RR2017 forecast under the T1 volume driver during the T1+2 period. If there is also RIIO-ET2 funding provided for the same project, the T1+2 allowance will be offset by anyT2 allowances given for that same project.

  - Where the actual or best available forecast of the project delivery is not in line with NGET's RR2017 forecast capacity and/or timing, the difference between the prior allowance and the revised allowances due under the T1 volume driver during the T1+2 period. This amount may be zero for those projects that have either completed during the T1 period or whose outputs will be delayed beyond T1+2. Again, the resultant sum will be offset as appropriate by any T2 allowances given for that same project.

  - Where projects were not included in the RR2017 forecast but either have delivered or are expected to deliver outputs in T1+2, the allowance due is as under the T1 volume driver, which will be offset as appropriate by any T2 allowances given for that same project.

[80] The value of any allowance received to date will be subject to 'claw back' based on the unit rates set within the T1 Licence.

Adjustments will be made to the NGET input tab of the ET1 Legacy PCFM for the following variable values:

- IWW in row 19, "Network development and wider works volume driver (NGET only)" under the heading "PCFM Variable Values Table".
- DRI row 21, "Demand related infrastructure volume driver" under the heading "PCFM Variable Values Table".
- GCE in row 23, "Generation connections volume driver" under the heading "PCFM Variable Values Table".

SHET

During each reporting year, an allowance provision is estimated under SHET's generation volume driver to reflect the forecast output delivery schedule in the T1+2 period. This calculation applies the agreed unit cost rates and an apportionment using a construction profile[81] to phase the funding provision.

Throughout the RIIO-ET1 period, changing customer requirements and delivery plan updates have led to a revised view of these projects and it is proposed as part of RIIO-ET1 close-out to reconcile allowances against the latest view of projects delivering outputs in T1+2 timescales.

Projects that meet the delivery criteria of a crossover project and which are eligible to receive funding determined by the volume driver unit rates set within the T1 Licence will be remunerated accordingly. We will make appropriate adjustments to the level of funding applicable to the RIIO-ET1 and RIIO-ET2 component to facilitate this approach and to avoid double funding projects that are already included in RIIO-ET2 baseline. Closeout will confirm:

- projects that commenced in T1 but have not yet delivered outputs:
    - Where the project is being delivered during the T1+2 period, the allowances due under the T1 generation connection volume driver during

[81] An equal 25% split across the four years preceding the connection date.

the T1+2 period will be calculated. This allowance will be netted off as appropriate by any T2 allowances given for that same project.

  - Where the project is not scheduled to be completed within the T1+2 period, the T1 volume driver will not apply[82].

- projects that were scheduled to be delivered in the T1+2 period but have delivered by the end of T1. In this case the allowance due under the T1 volume driver will be offset as appropriate by any T2 allowances given for that same project.

Adjustments will be made to the SHET input tab of the ET1 Legacy PCFM for the variable value GCE in row 23, "Generation connections volume driver" under the heading “PCFM Variable Values Table”.

[82] The value of any allowance received to date will be subject to ‘clawback’ based on the unit rates set within the T1 Licence.

Appendix 9 - Adjustment for SPT's Connection Volume Driver Clawback

As part of the closeout process for RIIO-ET1 we will:

- verify the assets delivered in the sole-use infrastructure category that contribute to the 2503MW output threshold, delivered between 1 April 2013 and 31 March 2021.

- verify the finalised actual costs incurred in the delivery of those assets and validate the MW delivery against the threshold capacity in the T1 Licence.

- verify the calculation method applied to determine the value of the clawback to be authorised through the closeout process.

- Adjustments to allowances for RIIO-ET1 will be implemented in the ET1 Legacy PCFM for the subsequent AIP process

Adjustment will be made to the ET1 Legacy PCFM in STP's input tab, row 23, "Generation connections volume driver" under the heading PCFM Variable Values Table.