



Making a positive difference
for energy consumers

To:

Electricity Distribution,
Gas Distribution, Gas
Transmission, Electricity
Transmission; Network
Operators; and
Stakeholders

Date: 14 April 2023

Dear Company Secretaries and Stakeholders,

Proposal to modify the special conditions of the Gas Transporter and Electricity Transmission licence and the Price Control Financial Instruments (PCFIs) for RIIO-GD2, RIIO-GT2 and RIIO-ET2

We¹ are proposing to amend the special conditions and PCFIs and in particular the following documents for Gas Distribution, Gas Transmission and Electricity Transmission licensees:

- RIIO-GD2, RIIO-GT2 and RIIO-ET2 Price Control Financial Model (PCFM)
- RIIO-GD2, RIIO-GT2 and RIIO-ET2 Price Control Financial Handbook (PCFH)
- RIIO-GD2, RIIO-GT2 and RIIO-GT2 Special Conditions

Please find enclosed the Notices setting out our proposed changes issued pursuant to the relevant Licence Conditions and PCFIs for each relevant sector.

As part of the enclosed Notices, we provide the following documents with proposed modifications [marked up]:

- RIIO-GD2 PCFM ;
- RIIO-GD2 PCFH: Version 1.4;
- RIIO-GT2 PCFM ;
- RIIO-GT2 PCFH: Version 1.3;
- RIIO-ET2 PCFM ;

¹ References to 'the Authority', 'GEMA', 'Ofgem', 'we', 'us' and 'our' are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets. Ofgem is the office of the Authority which supports GEMA.

- RIIO-ET2 PCFH: Version 1.3;
- Special Conditions of the Gas Transporter Licences for:
 - Cadent Gas Limited
 - Northern Gas Networks Limited
 - Southern Gas Networks plc
 - Scotland Gas Networks plc
 - Wales and West Utilities Limited
 - National Gas Transmission plc
- Special Conditions of the Electricity Transmission Licences for:
 - National Grid Electricity Transmission Plc
 - SP Transmission Plc
 - Scottish Hydro Electric Transmission Plc

Proposed modifications

We are proposing several amendments to the PCFM, PCFH and Special Conditions. These include:

- Amending the Annual Iteration Process (AIP) timeline to bring the publication date in line with the tariff-setting date for gas distribution and transmission networks.
- Making updates to tax conditions in the PCFH and Special Conditions to align them with RIIO-ED2 and the language used in the Regulatory Financial Performance Reporting (RFPR) Guidance and template²
- Modifying the RIIO-ET2 PCFM to include the new Accelerated Strategic Transmission Investment (ASTI) re-opener terms
- Re-stating the RIIO-GD2 non-variant allowances in the PCFM per the current consultation and amended cost models
- Modifying the FPNES Volume driver (special condition 3.14) and conversely VCMA (special condition 5.4)
- Modifying the unit costs of:
 - Commercial Fleet Price Control Deliverable (special condition 3.13)
 - Domestic Connections Volume Driver (special condition 3.15)

We set out the effect of and the reasons for these modifications below.

General updates

We have also included other housekeeping updates and corrections to the Special Conditions and PCFIs. For further details on the updates and corrections please see the tracked changes within the documents published alongside this Notice.

² [Decision on the proposed modifications to the RIIO-2 Electricity Distribution licences | Ofgem](#)

AIP timeline

The following proposed changes relate to our proposal to amend the AIP timeline and process.

AIP publication date

The AIP is the process by which Ofgem recalculates network licensees' Allowed Revenues by updating the variable input values of the PCFM to reflect actual and updated forecast data, throughout each year of the price control. At the end of each AIP Ofgem publishes the value of Allowed Revenue for each licensee, which they must use when setting their network charges for the coming regulatory year.

We are proposing a change to the AIP timeline to bring the publication date in line with the tariff-setting date for Electricity Transmission (ET) and Gas Distribution (GD) licensees (end of January) and closer to the tariff-setting date for Gas Transmission (GT). Whereas Ofgem currently publishes the AIP on 30 November with an additional AIP re-publication taking place by the end of January, we now propose to publish the AIP at the end of January only, with no additional re-publication process for the ET and GD sectors.³

The reason for this is to streamline the process and have a single publication date that is closer to the networks tariff-setting date, rather than going through two publication processes to set the Allowed Revenues that network companies use to set their tariffs at the end of each January. The impact of this on setting allowed revenues will be the same, it will simply reduce the administrative burden of having multiple publications on networks and Ofgem.

Materiality threshold for AIP January submission and re-publication

For the GT sector, the re-publication process will remain in place, given the gas charging year has its own distinct timeline, however we propose to increase the materiality threshold for updates that we will consider re-publishing from the current threshold of around 1% of Allowed Revenue to 5%. We think it is reasonable to impose a materiality threshold higher than the current level because licensee would have longer to amend its forecasts under the new proposals and the existing threshold is based on the general materiality threshold level as defined in the Special Conditions, which typically applies to individual allowances rather than Allowed Revenue as a whole. As such this has been set at too low a level for the purposes of the re-publication, which is to set Allowed Revenue. In our view, a 5% impact on Allowed Revenue is material enough that it could

³ For the GT sector, the re-publication process will remain in place, given the gas charging year has its own distinct timeline.

meaningfully impact customer bills and the licensee's cashflows and so a re-publication of the AIP would be proportionate if forecasts change to such a degree that the threshold is breached. We do not consider that the current 1% threshold meets this criteria.

This is the same level at which we are proposing to implement a materiality threshold for the GD licensee's final PCFM submission at the end of an AIP. Under the proposed GD process, there will be a final opportunity for licensees to submit an updated PCFM in early January if there is a material change to the forecasts that they provide to Ofgem in December. We think, it is reasonable to impose a 5% materiality threshold for final PCFM submissions for the same reasons, outlined above. As well as this we require a reasonable cut-off date to be able to administer the AIP publication by the end of January and so a very low threshold such as the current level will result in a large number of last-minute changes and would leave Ofgem with little review time.

For all sectors, where any forecasts change between the AIP cut-off date and the tariff-setting date, changes that have not been captured by that cut-off date can and will be included in the following AIP, with a time value of money true-up applied to the difference.

Tax review (Tax Allowance adjustment condition (SpC 2.2 and SpC 2.4) and Tax Reconciliation Assurance Statement Condition (SpC 9.8) and PCFH Chapter 6)

We are proposing to modify the tax-related special conditions and Chapter 6 of the PCFH to align the language with that used elsewhere in our Regulatory Financial Performance Reporting guidance and templates.

The reason for this is to ensure that the terminology used throughout the licence, licence instruments and reporting guidance is consistent and to avoid any potential confusion for users of these documents.

The effect of this is to modify the drafting in the aforementioned special conditions and in Chapter 6 of the PCFH.

Accelerated Strategic Transmission Investment (ASTI) re-opener terms

We are proposing to introduce two ASTI related re-opener terms into the RIIIO-ET2 PCFM.

The reason for this is due to the the recently closed Accelerated Strategic Transmission Investment Informal Licence Drafting Consultation⁴ which contains drafting for two ASTI

⁴ [Accelerated Strategic Transmission Investment Informal Licence Drafting Consultation | Ofgem](#)

related re-opener terms, and to ensure the RIIO-ET2 PCFM aligns with this.

The effect of this is to modify the RIIO-ET2 PCFM, and add in two line items for the two re-opener terms:

- Accelerated strategic transmission investment Pre-Construction Funding Re-opener ($APCF_t$); and
- ASTI re-opener term Accelerated strategic transmission investment Re-opener ($ASTIR_t$).

Re-stating the Non-Variant Allowances in the RIIO-GD2 PCFM

We are proposing to address certain concerns pertaining to the Non-Variant Allowances in RIIO GD2 following the first year of reporting the AIP.

The reason for this is to update and correct figures within the PCFM.

The effect of this is to modify the non-variant totex allowance line items in the RIIO-GD2 PCFM in each licensee input sheet.

Modify the FPNES volume driver (Special condition 3.14) and the VCMA (Special condition 5.4).

We are proposing to repurpose unspent FPNES allowances into the VCMA.

The reason for this is to enable GDNs to utilise unspent allowance in order to support vulnerable consumers.

The effect of this is to modify FPNES and VCMA allowances in order to provide additional support to vulnerable consumers.

Modify the Commercial Fleet Price Control Deliverable (Special condition 3.13)

We are proposing to expand the range of Electric Vehicle (EV) categories that are eligible under the PCD so that all GDNs have consistent options available to them and their associated unit costs.

The reason for this is to allow each GDN the same options of Electric Vehicles categories under the PCD.

The effect of this is to modify expand the EV categories and unit costs within the Commercial Fleet PCD.

Modify the Domestic Connections Volume Driver (Special condition 3.15)

We are proposing to make a correction to the unit costs for the Domestic Connections Volume Driver.

The reason for this is to update the unit costs for Domestic Connections after appropriately reallocating costs based on the workload breakdown between mains and service connections.

The effect of this is to modify the unit costs of the Domestic Connections Volume Driver.

All of the proposed modifications have been discussed with licensees during the PCFM Working Groups and we have considered any views expressed and representations made, as per the requirements of Special Condition 8.1

For further details on changes to the PCFM and PCFH please refer to Appendix 2 and Appendix 3. These changes can also be seen in the tracked changes within the documents.

We welcome representations on our proposed modifications by 12 May 2023, and the details for responding are contained in the enclosed Notice.

Yours faithfully,

Jourdan Edwards
Interim Deputy Director
Onshore Networks
Duly authorised on behalf of the Authority

To:
Cadent Gas Limited
Northern Gas Networks Limited
Scotland Gas Networks plc
Southern Gas Networks plc
Wales and West Utilities Limited
National Gas Transmission Plc - 02006000
Scottish Hydro Electric Transmission plc
SP Transmission Ltd
National Grid Electricity Transmission plc

Electricity Act 1989
Section 11A(2)
Gas Act 1986
Section 23(2)

Notice of statutory consultation on a proposal to modify the special conditions of the Gas Transporter and Electricity Transmission licence held by the licensees listed above

1. The Gas and Electricity Markets Authority ('the Authority')⁵ proposes to modify the special conditions of the Gas Transporter licence held by each of the licensees listed above ('the licensees') granted or treated as granted under section 7 of the Gas Act 1986 and the electricity transmission licence held by each of the licensees listed above ('the licensees') granted, or treated as granted, pursuant to section 6(1)(b) of the Electricity Act 1989 ('the Electricity Act') by:
 - amending Part B of Special Condition 1.1 (Interpretation and definitions) for housekeeping;
 - amending Special Condition 2.1 (Revenue Restriction) for housekeeping⁶;
 - amending Special Condition 2.2 (Tax allowance adjustment)⁷, Special Condition 2.4 (System operator tax allowance adjustment)⁸, and Special Condition 9.8 (Tax Reconciliation assurance statement) to align with the wording used elsewhere in our reporting guidance and templates;
 - aligning Special Condition 8.1 (Availability and updating of [XX]2⁹ Price Control Financial Instruments) to the wording in the RIIO-ED2 Special Conditions and the language used in the Regulatory Financial Performance Reporting (RFPR) Guidance and template; and
 - making amendments to the timeline of the Annual Iteration Process in Special Condition 8.2 (Annual Iteration Process for the Price Control Financial Model).
2. In addition, Appendix 1 contains details on the proposed modifications to the Gas Transporter Licence for RIIO-GD2 companies only. The proposed modifications relate to:
 - Special Condition 3.13 (Commercial Fleet Price Control Deliverable);
 - Special Condition 3.14 (Fuel Poor Network Extension Scheme (FPNES) Volume driver);

⁵ The terms "the Authority", "we" and "us" are used interchangeably in this document.

⁶ For RIIO-GD2 and RIIO-ET2 only

⁷ Special Condition 2.2 (Transportation owner Tax allowance adjustment) for RIIO-GT2

⁸ For Special Conditions of the Gas Transporter Licence for RIIO-GT2 only

⁹ 'ET2', 'GT2' and 'GD2'

- Special Condition 3.15 (Domestic Connections Volume Driver); and
 - Special Condition 5.4 Vulnerability and carbon monoxide allowance (VCMA) (5.4).
3. The purpose, reasons for, and effect of these proposed modifications are described in the cover letter to this Notice.
 4. Schedule 1 to this notice contains the proposed modifications to the special conditions of the Gas Transporter licence held by National Gas Transmission Plc¹⁰. Schedule 2 to notice contains the proposed modifications to the special conditions of the Gas Transporter Licence held by Cadent Gas Limited, Northern Gas Networks Limited, Southern Gas Networks plc, Scotland Gas Networks plc, and Wales and West Utilities Limited. Schedule 3 to this notice contains the proposed modifications to the special conditions of the Electricity Transmission licence held by Scottish Hydro Electric Transmission plc, SP Transmission Ltd and National Grid Electricity Transmission plc.
 5. In addition, we are also proposing modifications to the ET2, GT2 and GD2 Price Control Financial Instruments (PCFIs).
 6. The reasons for the proposed modifications, and an overview of the proposed modifications being made to both the ET2, GT2 and GD2 Price Control Financial Models (PCFM) are set out below:
 - a. to align the PCFM inputs with the inputs to the Regulatory Instructions and Guidance (RIGs) reporting we have updated the price base of certain pass-through terms to nominal from 18/19 prices.
 7. There are some proposed modifications that relate to the GD2 PCFM only. The reasons for and overviews of the proposed modifications are set out below:
 - a. we have amended the yellow-box non-variant allowances in the licensee input sheets for each licensee. The reasons and effect can be seen in the covering letter to this notice;
 - b. we have amended the "SavedResults" sheet to enable the correct calculations on the AR sheet to split Allowed Revenue into the three sub-components that gas distribution licensees need to input into their charging model. This was previously done offline and so licensees requested that we include the calculation in the PCFM to automate this process. This split is for presentational purposes only and has no impact on the calculation of Allowed Revenue; and
 - c. we have added a label for the SIU cross-subsidy adjustment for clarity.
 8. There are some proposed modifications that relate to the GT2 PCFM only. The reasons for and overviews of the proposed modifications are set out below:
 - a. we have corrected a formula that checks the totex allocations rates sum to 100%;
 - b. we have corrected a formula to link to the assumed cost multiplier to the Strategic Innovation Fund (SIF_t); and
 - c. we have corrected the assumed cost multiplier value for SIF_t to 100% from 111.11%.

¹⁰ Company number 02006000

9. There are some proposed modifications that relate to the ET2 PCFM only. The reasons for and overviews of the proposed modifications are set out below:
- a. we have added re-opener PCFM Variable Value line items to each licensee input sheet in-line with the Accelerated Strategic Transmission Investment (ASTI) Informal Licence Drafting Consultation.¹¹
10. Please see Appendix 2 to this notice for a list of the proposed PCFM modifications.
11. The reasons and effect of the proposed modifications for the ET2, GT2 and GD2 PCFH can be seen in the covering letter to this notice. An overview of the proposed modifications being made to both the ET2, GT2 and GD2 Price Control Financial Handbook (PCFH) are set out below:
- a. Amending the AIP timeline to bring the publication date in line with the tariff-setting date for gas distribution and transmission networks; and
 - b. Amending Chapter 6 (Tax liability allowances) to align with the equivalent chapter in the RIIO-ED2 PCFH and the language used in the Regulatory Financial Performance Reporting (RFPR) Guidance and template ¹².
12. Please see Appendix 3 to this notice for a list of the proposed PCFH modifications.
13. A copy of the proposed modifications and other documents referred to in this Notice have been published on our website (www.ofgem.gov.uk). Alternatively they are available from foi@ofgem.gov.uk. Appendices 1 and 2 indicate the location of changes within the published PCFI.
14. Any representations with respect to the proposed licence modifications must be made on or before 12 May 2023 to: Michael Smith, Office of Gas and Electricity Markets, 10 South Colonnade, Canary Wharf, London, E14 4PU or by email to Michael.Smith@Ofgem.gov.uk
15. We normally publish all responses on our website. However, if you do not wish your response to be made public then please clearly mark it as not for publication. We prefer to receive responses in an electronic form so they can be placed easily on our website.
16. If we decide to make the proposed modifications they will take effect not less than 56 days after the decision is published.

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Jourdan Edwards
Interim Deputy Director
Duly authorised on behalf of the Gas and Electricity Markets Authority
14 April 2023

¹¹ [Accelerated Strategic Transmission Investment Informal Licence Drafting Consultation | Ofgem](#)

¹² [Decision on the proposed modifications to the RIIO-2 Electricity Distribution licences | Ofgem](#)

Appendix 1 – Updates to the RIIO-GD2 Special Conditions

The Special Conditions containing the proposed modifications are attached as schedules to this consultation detailing changes to the FPNES & VCMA; Commercial Fleet Price Control Deliverable & the Domestic Connections Volume Driver.

Part A: Repurposing the FPNES to the VCMA

FPNES connection targets have been revised downwards for several reasons; a shift in policy towards renewable energy and reducing carbon emissions, the recent spike in energy prices and operational issues. Through discussions with Gas Distribution Networks (GDNs) and relevant consumer groups, Ofgem has decided to re-purpose some unspent GDNs FPNES allowances to support Vulnerable consumers.

To achieve this, we have leveraged GDNs' connection forecasts and allowed for some flexibility in over-delivery. Then, using the remaining funding we have applied the same methodology used in Final Determinations to allocate each GDN a share of the VCMA total funding pot.

Part B: Commercial Fleet Price Control Deliverable

As a result of current global supply issues and the fact that certain types of Electric Vehicles may not be appropriate for the GDNs specific requirements, we have made the decision to expand the range of vehicle categories that are eligible under the PCD so each GDN has consistent options available to them.

Part C: Domestic Connections Volume Driver

Following some corrections to the modelling process, some adjustments were required to ensure accurate unit costs were used in this mechanism. As such, costs have been reallocated based on workload breakdown specifically between 'Mains' and 'Services' to produce updated and accurate unit cost values.

Appendix 2 – Changes to the RIIO-2 Price Control Financial Models (PCFMs)

The PCFMs containing the proposed modifications are attached as schedules to this consultation. The changes have been highlighted with red borders. A summary of the changes follows below.

Part A: Changes to the price base of pass-through terms in the PCFM for GD, GT and ET

The modifications made to the PCFM for all sectors are as follows:

- Amended the price base of numerous pass-through costs for all licensee input sheets in the “Units” column to “£m nominal”;
- Where relevant converted the pass-through blue-box values to £m nominal in the licensee input sheets; and
- Amended the formula in the “Input” and “SystemOperator” sheet to convert the relevant pass-through cost line items to £m 18/19 prices, now that they are recorded as £m nominal in the licensee input sheets.

Part B: Addition of the ASTI re-opener licence terms in the ET2 PCFM

The modifications made to the ET2 PCFM are as follows:

- Inserted a row in all licensee input sheets for the new ASTI re-opener term Accelerated strategic transmission investment Pre-Construction Funding Re-opener (APCF_t); and
- Inserted a row in all licensee input sheets for the new ASTI re-opener term Accelerated strategic transmission investment Re-opener (ASTIR_t).

Part C: Formula corrections and general housekeeping in the GT2 PCFM

The modifications made to the GT2 PCFM are as follows:

- In the “NGGT TO” sheet, added a formula in row 154 to sum the totex allocations rates in order to check the output is 100%;
- In the “Input” sheet amended the formula in cell I107 to ensure it is correctly linked to the assumed cost multiplier for the Strategic Innovation Fund (SIF_t) in the “NGGT TO” sheet, cell AP77; and
- In the “NGGT TO” sheet, corrected the value in cell AP77, the assumed cost multiplier of SIF_t, to 100% from 111.11%

Part D: Amendment to the non-variant allowances and general housekeeping in the GD2 PCFM

The modifications made to the GD2 PCFM are as follows:

- Amended the non-variant allowances in each of the licensee input sheets
- Added a term label for the cross-subsidy line item (WWUACPt and SGNACPt) in row 481 in the 'Wales & West' and 'Scotland' sheets respectively.
- We have changed the Exit and SOLR Calculated Revenue, and Exit and SOLR ADJ line items to blue box inputs in the “SavedResults” sheet to enable the correct calculations on the AR sheet to split Allowed Revenue into the three sub-components that gas distribution licensees need to input into their charging model. This was

previously done offline and so licensees requested that we include the calculation in the PCFM to automate this process. This split is for presentational purposes only and has no impact on the calculation of Allowed Revenue

Appendix 3 – Changes to the RIIO-2 Price Control Financial Handbooks (PCFHs)

The PCFHs containing the proposed modifications are attached as schedules to this consultation. The changes are tracked. A summary of the changes and where they appear follows below.

Part A: Amending the AIP timeline for GD, GT and ET

Proposed modifications to the PCFHs can be seen in the attached schedules. Throughout the PCFH we have made adjustments to dates to account for the proposed amended AIP timeline

The modifications made to the PCFH can be seen in:

- Chapter 2 “The RIIO-[XX]2¹³ PCFM and the Annual Iteration Process”
- Chapter 4 “Cost of debt and cost of equity indexation”
- Chapter 5 “Real Price Effects”
- Chapter 6 “Tax Liability Allowances”

Part B: Updating Chapter 6 to align with RIIO-ED2 and RFPR Guidance and template for GD, GT and ET

In the tax chapter we have made updates to align the language with RIIO-ED2 and the language used in the Regulatory Financial Performance Reporting (RFPR) Guidance and template.¹⁴

The modifications made to the PCFH can be seen in:

- Chapter 6 “Tax Liability Allowances”

Part C: General Housekeeping for GD, GT and ET

Throughout the PCFHs we have made amendments for general housekeeping purposes to improve clarity and additional detail where needed.

The modifications made to the PCFH can be seen in:

- Chapter 2 “The RIIO-XX2 PCFM and the Annual Iteration Process”
- Chapter 4 “Cost of debt and cost of equity indexation”
- Chapter 5 “Real Price Effects”
- Chapter 6 “Tax Liability Allowances”

¹³‘ET2’, ‘GT2’ and ‘GD2’

¹⁴ [Decision on the proposed modifications to the RIIO-2 Electricity Distribution licences | Ofgem](#)