

Decision

Decision on Statutory Consultation: licence modifications to give effect to decision on SPT's 2023 MSIP applications

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This document sets out our¹ decision following a statutory consultation on our proposals to modify the Special Conditions ('SpCs') of the Electricity Transmission Licence ('the Licence') held by SP Transmission plc ('SPT'). The modifications amend Appendix 1 of SpC 3.14 (Medium Sized Investment Projects ('MSIP') Re-opener and Price Control Deliverable ('MSIPRET')) of the Licence to add allowances for three approved MSIP applications and give effect to the decision dated 28 February 2024.

We published a statutory consultation on 28 February 2024, setting out our proposals to amend the Licence, alongside our decision on SPT's 2023 applications relating to three projects under the MSIP Re-opener mechanism ('SPT 2023 MSIP Decision'). The statutory licence modification consultation closed on 2 April 2024. We published non-confidential responses to the consultation on our website on 5 April 2024². This decision document and the corresponding Notice of Modification of the SpCs of the Licence, published alongside it, confirms our decision to make the proposed modifications to SpC 3.14 of the Licence.

¹ The terms 'we', 'us', 'our' refer to the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.

² <https://www.ofgem.gov.uk/publications/statutory-consultation-proposal-modify-special-conditions-electricity-transmission-licence-held-national-grid-electricity-transmission-plc>

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1. Introduction

Context and related publications

1.1. Network companies are natural monopolies. Effective regulation of privatised for-profit monopolies is essential to ensure they cannot unfairly exercise their monopoly power to the detriment of their customers. This is particularly important in the case of essential utilities, such as energy, where consumers have no choice about whether or not to pay what they are charged. It is therefore crucial that an effective regulator protects energy consumers by controlling how much network companies can charge their customers. Ofgem³ does this through periodic price controls that are designed to ensure network companies are properly incentivised to deliver the best possible outcomes for current and future energy consumers. This includes ensuring that consumers only pay for investments that are needed and do not overpay for those investments.

1.2. SPT is the holder of an electricity transmission licence ('the Licence') granted or treated as granted under section 6(1)(b) of the Electricity Act 1989 ('the Act').

1.3. Special Condition ('SpC') 3.14 Medium Sized Investment Projects Re-opener and Price Control Deliverable ('MSIPRE_{tr}') ('MSIP Re-opener') of the Licence is a mechanism that provides Electricity Transmission Owners ('ETOs'), such as SPT, with an opportunity to request additional funding on projects with a value of less than £100m. Applications may only be made on projects where Baseline Allowances have not already been provided in the price control, and subject to other qualifying criteria as set out in SpC 3.14 of the Licence.

1.4. On 28 February 2024, we published our decision on SPT’s 2023 MSIP Re-opener applications ('SPT 2023 MSIP Decision').⁴

1.5. Alongside our SPT 2023 MSIP Decision we published a statutory consultation on 28 February 2024, proposing to modify Appendix 1 of SpC 3.14 (MSIP Re-opener) of the Licence.⁵

1.6. We have considered the responses to the statutory consultation and have decided to proceed with the proposed modifications. We are making these licence changes because adding the Price Control Deliverables ('PCDs') into Appendix 1 of SpC 3.14 gives

³ The terms 'the Authority', 'Ofgem', 'we', 'us' and 'our' are used interchangeably in this document. The Authority is the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.

⁴ <https://www.ofgem.gov.uk/publications/decision-three-sp-transmissions-2023-msip-applications>

⁵ <https://www.ofgem.gov.uk/publications/decision-three-sp-transmissions-2023-msip-applications>

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effect to the decision of the Authority dated 28 February 2024 to approve funding for SPT’s three MSIP projects.

1.7. The effects of the modifications are to set Price Control Deliverables (‘PCDs’) related to SPT’s three MSIP projects and the allowances for the delivery of the projects. If SPT does not deliver the PCDs during the RIIO-ET2 price control, then the price control framework provides for the allowances to be clawed back.

Our decision-making process

Responses to the statutory consultation

1.8. We received two responses to the 28 February 2024 licence modification statutory consultation, one each from National Gas Electricity Transmission plc (‘NGET’) and from SPT. We have carefully considered both responses and taken them into account in our decision-making process.

1.9. The responses mostly focused on the interaction of risk and contingency allowances and the Totex Incentive Mechanism (‘TIM’). SPT also made mention of staged MSIP applications and the Opex Escalator (‘OE’).

1.10. We cover the ETOs’ responses in Chapter 2.

Our decision-making

1.11. The decision-making stages are detailed below:

Date	Stage description
28/02/2024	Stage 1: Licence Modification Statutory Consultation opens
02/04/2024	Stage 2: Licence Modification Statutory Consultation closes (awaiting decision), Deadline for responses
05/04/2024	Stage 3: Responses reviewed and published
29/05/2024	Stage 4: Licence Modification decision and Notice of Modification of the Licence Special Conditions

1.12. In reaching this decision on changes to the Licence, to give effect to our SPT 2023 MSIP Decision, we have had regard to, and have furthered, our principal objective to protect the interests of existing and future consumers. We have also had regard to the other considerations set out in section 3A of the Act.

1.13. We are incorporating the Price Control Deliverables into Appendix 1 of SpC 3.14, to give effect to the decision of the Authority dated 28 February 2024 to approve funding for SPT's three MSIP projects, and in the terms set out in that decision.

1.14. The effect of the modifications is to set PCDs related to SPT's three MSIP projects and the allowances for their delivery. If SPT does not deliver the PCDs during the RIIO-ET2 price control, then the price control framework provides for the relevant PCD allowances to be clawed back.

2. Our Final Determinations

2.1. In coming to our 2023 SPT MSIP Decision, we carefully considered all of SPT's and NGET's responses to the policy consultation on these MSIPs. Some of the ETOs' responses to the licence modification statutory consultation were the same as before, which were considered and taken into account ahead of our 2023 SPT MSIP Decision.

2.2. The SPT response made mention on the followings:

- OE: SPT reiterated that the OE represents an error and will result in underfunding across the portfolio of MSIP projects. SPT welcome the introduction of Ofgem's proposed OE review mechanism to address this issue, but said that it still has significant concerns with the mechanism's proposed parameters. SPT stated that it remains committed to working with Ofgem on the development of the OE review mechanism and that it is looking forward to the reinstatement of OE closeout mechanism working groups. It also said that it reserves its rights to appeal under the Electricity Act 1989 should SPT consider the OE review mechanism is not fit for purpose.
- Risk and contingency allowance: SPT retained the views that application of a 7.5% cap for risk remains arbitrary and non-project specific, and excluding the contractor indirect costs prior to applying the cap further reduced the risk allowance. SPT also disagreed with Ofgem's explanation of sharing of risk between consumers and ETOs through risk allowance and Totex Incentive Mechanism (TIM) (paragraphs 2.10 to 2.14 of SPT 2023 MSIP decision), in which Ofgem considered direct cost allowance covers all efficient cost required and the risk expenditure (if materialised) is overspend. SPT considered efficient project cost should include both direct cost and risk allowance.

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- Staged approach to MSIP application: SPT reiterated its desire to retain the staged MSIP application approach.
- Treatment of survey costs: SPT reiterated its disagreement to treating survey costs as indirect cost.
- The RIIO-ET1 Expenditure: SPT commented that there is no appropriate funding mechanism in place to cover the initial costs within RIIO-ET1 period associated with the development of MSIPs.

2.3. NGET’s response focused on Ofgem’s explanation of sharing of risk between consumers and ETOs through risk allowance and TIM. NGET’s view is the same as that of SPT as described in second bullet of paragraph 2.2 above.

Our consideration of the ETOs’ responses

2.4. The following paragraphs set out our views on and contain our responses to the ETO points summarised above.

Opex Escalator

2.5. SPT’s response on OE is the same as that provided before. We have fully covered our rationale on the application of OE in our previous decision document.⁶ As mentioned in paragraphs 2.18 and 2.19 of the SPT MSIP decision⁷, we will introduce the OE Review Mechanism, which would allow us, should the ETOs provide strong evidence and robust quantification of systematic underfunding versus efficient levels, to apply appropriate adjustments to the ETOs’ RIIO-2 allowances to rectify the issue.

2.6. We will continue working with the ETOs and other stakeholders to finalise the design of the OE Review Mechanism through group workshops and will take ETOs’ representations into account in finalising the Review Mechanism.

Risk and Contingency Allowance

2.7. We maintain our view that aligning the level of risk and contingency allowance in re-opener applications with that provided in the RIIO-ET2 FDs is appropriate at the moment.

⁶ [Decision to modify the special conditions of the electricity transmission licence held by National Grid Electricity Transmission Plc | Ofgem](#)

⁷ [Decision: Three SP Transmission's 2023 MSIP applications | Ofgem](#)

2.8. We are reviewing the suitable approach in risk and contingency allowance for projects in the future RIIO-ET3. We are working with the ETOs to finalise the approach to provide risk and contingency within projects through working group workshops and will take ETOs' representations into account in finalising the approach.

Other Responses

2.9. For the staged approach to MSIP application, we maintain our view that a single MSIP application is in most cases sufficient to achieve the objective to ensure that ETOs have certainty that there is a funding route in RIIO-ET2 for necessary additional work.

2.10. As mentioned in paragraphs 2.22 of the SPT MSIP decision⁸, we allow some flexibility to address concerns on the availability and certainty of cost information at the MSIP submission date. We have seen some ETOs utilise the flexibility to enable them to make MSIP applications in the January 2024 submission window.

2.11. For the treatment of survey costs and RIIO-ET1 expenditure, we are working in accordance with the relevant licence conditions (SpC 3.14) and the latest version of Regulatory Instructions and Guidance (RIGs)⁹.

Our decision and rationale for it

2.12. Following careful consideration of both consultation responses we have decided that our initial proposal remains appropriate.

2.13. We are incorporating the Price Control Deliverables into Appendix 1 of SpC 3.14, to give effect to the decision of the Authority dated 28 February 2024 to approve funding for SPT's three MSIP projects, and in the terms set out in that decision.

2.14. The effect of the modifications is to set PCDs related to SPT's three MSIP projects and the allowances for their delivery. If SPT does not deliver the PCDs during the RIIO-ET2 price control, then the price control framework provides for the relevant PCD allowances to be clawed back.

⁸ [Decision: Three SP Transmission's 2023 MSIP applications | Ofgem](#)

⁹ [Decision on modifications to the Regulatory Instructions and Guidance \(RIGs\), Regulatory Reporting Packs \(RRPs\) and the Price Control Financial Model \(PCFM\) Guidance: RIIO-ET2 Year 3 - Electricity Transmission | Ofgem](#)

3. Next Steps

3.1. We have taken full account of all consultation representations as detailed in Chapter 2.

3.2. We have decided to make and implement the modifications to SPT's Licence on which we previously consulted. Accordingly, we are publishing a Notice of Modification in conjunction with this decision. The Licence modifications will take effect 56 days after the publication of this decision and Notice of Modification.