

# Consultation

## Proposed Guidance for the NARM RIIO-2 Close-out Methodology

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We<sup>1</sup> are consulting on our proposed guidance for the RIIO-2 Network Asset Risk Metric (NARM) close-out methodology. NARM is used to measure the risk reduction delivered by network companies through asset management activities and to support funding adjustments where delivery differs from baseline expectations. This consultation explains how we propose to assess delivery against Baseline Network Risk Outputs and calculate any funding adjustments or penalties at close-out.

We are also consulting separately on proposed modifications to the NARM Regulatory Instructions and Guidance and reporting templates, which will form the basis of companies' close-out submissions. We welcome views on whether the proposed methodology and reporting requirements are clear and workable.

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<sup>1</sup> The terms 'we', 'us', 'our' refer to the Gas and Electricity Markets Authority (the Authority). Ofgem operates under the direction and governance of the Authority.

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## 1. Introduction

This section explains what the Network Asset Risk Metric (NARM) is, why it is used in RIIO-2, and how it supports decisions on asset management and funding. NARM helps measure the risk reduction that network companies deliver through their investment in network assets. This consultation sets out our proposed approach for assessing NARM delivery at RIIO-2 close-out, including how we will compare delivery against baseline expectations, treat changes in risk outside companies' control, and calculate any funding adjustments or penalties. It also explains how the proposed methodology links to the NARM Handbook, licence requirements, sector-specific NARM methodologies, and the NARM RIGs and reporting templates being consulted on alongside this document.

### What is NARM?

- 1.1 Network Asset Risk Metric (NARM) is a framework used by network companies to quantify and manage asset-related risks. It uses a monetised risk approach, combining information on asset condition, likelihood of failure, and the potential consequences of that failure to express risk in financial terms. This typically involves estimating the probability of failure and multiplying it by the monetised value of the impact, such as the cost of supply interruptions, environmental damage, or other societal impacts.
- 1.2 NARM provides a consistent and structured way to assess and compare risks across different asset groups and sectors. It supports decision-making by linking asset condition and performance to quantified risk outcomes, enabling companies to prioritise interventions and justify asset management activities. The approach has evolved over time and continues to be refined as data quality, methodologies, and understanding of risk improve.

### Approach and principles for RIIO-2 NARM close-out

- 1.3 This document sets out our proposed methodology for implementing the RIIO-2 NARM close-out process. The methodology is designed to assess licensees' delivery of network risk outputs and to apply funding adjustments in a way that is transparent, proportionate, and aligned with the interests of current and future consumers.
- 1.4 The proposed approach to close-out is guided by a set of overarching principles that underpin both the assessment of delivery and the operation of the NARM Funding Adjustment and Penalty Mechanism. These principles are intended to

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ensure that the close-out process operates consistently with the objectives of NARM and supports efficient, risk informed decision-making.

1.5 In particular, we propose that:

- Consumer value and efficiency remain central. Licensees' asset management decisions should be made in the interests of current and future consumers, delivering efficient and risk informed outcomes.
- Delivery is assessed against a clear and consistent baseline. Performance will be assessed against the Baseline Network Risk Output (BNRO), adjusted where appropriate for validated Non-Intervention Risk Changes, to ensure a like for like comparison with the Outturn Network Risk Output (ONRO).
- Licensees are incentivised to deliver agreed outputs. The framework should provide appropriate incentives for licensees to deliver their agreed BNRO, including:
  - recognition of justified over delivery through funding adjustments; and
  - the application of penalties where unjustified under delivery occurs.
- Proportionate treatment of delivery variation is applied. Sector specific Deadbands are used to distinguish between immaterial variation and material deviation, ensuring that only significant differences from baseline outputs are subject to detailed justification.
- Flexibility in delivery is maintained, with appropriate scrutiny. Licensees are not constrained to deliver exactly the same set of projects assumed at baseline, provided they can demonstrate that any deviation from BNRO is justified and continues to deliver value for consumers.
- Assessment is applied at an appropriate level of aggregation. Delivery performance will be assessed at Risk Sub-Category level (or network level for GD), ensuring consistency with how outputs were originally set while allowing supporting evidence at project or programme level to explain performance drivers.
- Valuation approaches reflect the nature of delivery. The methodology distinguishes between:
  - delivery assessed through the standard Unit Cost of Risk approach; and
  - delivery elements that qualify as Clearly Identifiable, which are assessed through a bespoke approach where appropriate.

- 1.6 These principles underpin the proposed three-stage close-out process; Delivery Assessment, Justification Assessment; and Incentive Value Calculation, which we described in detail in the following sections of this document.

## **NARM Objectives**

- 1.7 NARM was developed to allow us to quantify the benefit, to consumers, of the network companies' asset management activities. In RIIO-2, this is used as the output to hold the network companies accountable for their investment decisions. NARM is intended not only as a regulatory reporting and monitoring tool, but also as a decision-supporting tool for network companies' asset management investments, and as a way for the network companies to justify past and future investments to Ofgem.
- 1.8 The NARM Objectives are set out in SpC 9.2 of each network company's RIIO-2 licence. The network companies' NARM Methodologies should facilitate the achievement of the objectives. However, the NARM Methodologies may not be the only tool needed to achieve the NARM Objectives. The network companies should be continually striving to better achieve the NARM Objectives. Part B of SpC 9.2 sets out eight NARM Objectives (a to h). These objectives are summarised as follows<sup>2</sup>:
- a) To allow Ofgem and other stakeholders to understand the links between the data that a network company collects and utilises and the asset management and investment decisions it makes. The NARM Methodology will therefore help provide assurance that any investment decisions are based on solid evidence and sound reasoning.
  - b) To enable Ofgem to set outputs for the network company to deliver over a price control period and to ensure that what the network company actually delivers can be compared to the targets on a like-for-like basis.
  - c) To enable the network company to estimate the Monetised Risk of its network assets both now and in the future.

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<sup>2</sup> Please note that this summary is intended to provide the reader with an understanding of the NARM Objectives and their intent. They are not comprehensive and readers are referred to SpC 9.2 for the full list of the objectives.

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- d) To enable the network company to estimate the Monetised Risk Benefit that would be delivered by different types of interventions on any given asset or group of assets. The objective is to be able to estimate both single-year snapshot risk benefit and long-term risk benefit.
- e) The estimated Monetised Risk Benefits should be suitable for use as inputs in Cost Benefit Analyses (CBA) in order to help network companies choose the best value for money investments, and to demonstrate to Ofgem, consumers, and other stakeholders that any investment plans have been optimised. This means that the Monetised Risk Benefits should be realistic with robust probability estimates and correctly valued consequences.
- f) To enable the identification and quantification of drivers of changes in Monetised Risk over time.
- g) To allow Monetised Risk comparisons to be made between different assets and different networks. In order for this objective to be achieved, the methodologies used for estimating Monetised Risk should be based as little as possible on subjectivity.

To enable the network company to report to Ofgem and other stakeholders in a way that can be easily understood and unambiguously interpreted.

## **NARM Methodologies**

- 1.9 All network companies are required under SpC 9.2 of their licences to have a NARM Methodology in place. The NARM Methodology must be approved by Ofgem.
- 1.10 Ofgem and network companies work closely together on the development and subsequent review of the NARM Methodologies to ensure that the methodologies align with how the companies should make investment decisions and that they comply with the relevant regulatory requirements.
- 1.11 The NOMs methodologies that were in place at the end of RIIO-1 were deemed to be the NARM Methodologies in effect at the start of RIIO-2 until they are superseded. Licensees are required to keep their methodologies under review to ensure they facilitate the achievement of the NARM Objectives. Ofgem conducts a public consultation before approving any revisions to a NARM Methodology.

## General Principles

1.12 Due to the different nature of their network assets and the way the companies operate, each sector has individual NARM Methodologies as well as company-specific elements:

- The Gas Distribution sector has a NARM Methodology that is largely common to the gas distribution networks (GDNs)<sup>3</sup>.
- In the electricity sector, the electricity transmission operators (ETOs) have a common NARM Methodology and company-specific Network Asset Risk Annexes (NARA)<sup>4</sup>. National Grid Electricity Transmission has its own NARA, and SP Transmission and Scottish Hydro Electric Transmission have developed a joint NARA. Both NARAs provide specific detail of the arrangements as they apply to the relevant licensees.
- For Gas Transmission<sup>5</sup>, as there is only one network company in the sector (National Gas Transmission (NGT)), commonality is not an issue.

1.13 Regardless of the detailed approaches adopted, all of the NARM Methodologies apply the principle that risk of asset failure is a combination of the probability of asset failure and monetary valuations of the consequence of the asset failing.

In general terms:

$$\left[ \begin{array}{c} \textit{Risk of Asset} \\ \textit{Failure} \end{array} \right] = \left[ \begin{array}{c} \textit{Probability of} \\ \textit{Failure (PoF)} \end{array} \right] \times \left[ \begin{array}{c} \textit{Consequence of} \\ \textit{Failure (CoF)} \end{array} \right]$$

1.14 In practice, it is usually not as simple as estimating single probability and consequence values related to a given asset, as it is usually necessary to build up the asset risk from a number of sub-components, failure modes, conditional probabilities, and different types of failure consequences.

1.15 The ETOs and NGGT also have a particular focus on Long-term Risk Benefit (LTRB). When an intervention takes place, the asset's monetised risk will be

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<sup>3</sup> <https://www.ofgem.gov.uk/publications/notice-intention-not-reject-modified-gas-distribution-network-output-measures-noms-methodology>

<sup>4</sup> <https://www.ofgem.gov.uk/publications/decision-not-reject-modified-electricity-transmission-network-output-measures-noms-methodology-issue-18>

<sup>5</sup> <https://www.nationalgrid.com/uk/gas-transmission/uk/electricity-transmission/document/135626/download>

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reduced in all years after the intervention up to the expected next replacement or refurbishment intervention. The LTRB is the sum of those risk reductions across a specified horizon. We expect the GDNs to further develop, and progress towards using, LTRB.

1.16 When considering consequences of failure there are four broad categories that all the methodologies consider. The four consequence categories are:

- System/network consequences – these are consequences that are a result of service disconnection following an asset failure. They include, for example, a valuation of the cost to consumers of being without electricity or gas supply for the period until supply can be restored, and as such are dependent on the numbers and type of customer that would be disconnected for a given asset. The methodologies also need to account for any mitigation measures, such as asset redundancy built into the system, or actions that the network company or third parties will take in the event of a loss of supply.
- Safety consequences – these are the direct consequences on the individuals expected to be in the vicinity of an asset when it fails. When estimating safety consequences, the methodologies must consider the number of individuals that might suffer injury or death in the event of an asset failure, and place values on these consequences. The failure mode is important in this regard as sudden catastrophic failures, such as a gas pipeline explosion, are likely to have much worse safety consequences than other more slowly developing failures.
- Environmental consequences – these are related to the impact on the natural environment of an asset failure, such as the leakage of oil from a failed transformer into a nearby watercourse, or the leakage of gas into the atmosphere from a failed gas valve.
- Financial consequences – e.g. these are the direct costs incurred by the licensee as a result of the asset failure. These might include the cost of emergency replacement of a failed asset, or the cost associated with securing the system following an asset failure.

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1.17 It is not always easy to value consequences, as many consequences do not have direct monetary impacts, or the monetary impacts do not cover the full scale of the losses experienced by all parties. An example of this is injury or death resulting from an asset failure. In such cases, as much as possible, the methodologies utilise commonly recognised valuations or industry standards, such as Government Green Book valuations, with full referencing to the valuation sources. Risk Pounds (R£) is the unit used to denote Monetised Risk values.

### **Purpose of this consultation**

1.18 We are consulting on our proposed approach to closing out the RIIO-2 NARM Funding Adjustment and Penalty Mechanism. This consultation explains how we propose to assess licensees' delivery against their BNROs, and the information we expect licensees to provide as part of the NARM Close-out Report.

1.19 We set out our proposed close-out methodology, including our approach to assessing over- and under-delivery, the treatment of Non-Intervention Risk Changes, and the calculation of any funding adjustments or penalties. We welcome views on whether this approach is clear, proportionate and provides an appropriate basis for determining RIIO-2 close-out outcomes.

1.20 We are also consulting separately, through statutory consultation notices, on proposed modifications to the RIIO-2 NARM Regulatory Instructions and Guidance (RIGs) and associated reporting templates. These documents are being published alongside this consultation and are intended to form the basis of licensees' NARM close-out submissions. We are consulting on the methodology and the RIGs together because the methodology explains how we propose to assess close-out delivery, while the RIGs and templates set out the information licensees would need to submit to support that assessment.

### **Context and related publications**

1.21 The scope of this consultation is limited to the methodology we propose to use to assess RIIO-2 NARM delivery at close-out. It should be read alongside the RIIO-2 NARM framework, the relevant licence conditions, the NARM Handbook Version 4.0 'the NARM Handbook' and the sector-specific NARM methodologies.

1.22 This document is intended to be read alongside:

- NARM RIGs and reporting templates being consulted on alongside this document
- Relevant RIIO-2 licence conditions, including Special Condition 3.1 on Baseline Network Risk Outputs and Special Condition 9.2 on the Network Asset Risk Metric methodology.

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- NARM Handbook Version 4.0, which sets out the NARM Funding Adjustment and Penalty Calculation Methodology, guidance on over-delivery and under-delivery, Non-Intervention Risk Changes, and the NARM Close-out Report requirements.
- RIIO-2 Final Determinations – NARM Annex, which set out the RIIO-2 NARM arrangements for electricity transmission, gas transmission and gas distribution licensees

## **Consultation stages**

**Stage 1** Consultation open: 22 May 2026

**Stage 2** Consultation closes (awaiting decision). Deadline for responses: 24 June 2026

**Stage 3** Responses reviewed and published: July 2026

**Stage 4** Consultation outcome (decision or policy statement) July 2026

## **How to respond**

- 1.23 We want to hear from anyone interested in this consultation. Please send your response to the person or team named on the front page of this document.
- 1.24 We have asked for your feedback in question at the end of section. Please respond to it as fully as you can.
- 1.25 We will publish non-confidential responses on our website.

## **Your response, data, and confidentiality**

- 1.26 You can ask us to keep your response, or parts of your response, confidential. We will respect this, subject to obligations to disclose information. For example, under the Freedom of Information Act 2000, the Environmental Information Regulations 2004, statutory directions, court orders, government regulations, or where you give us explicit permission to disclose. If you do want us to keep your response confidential, please clearly mark this on your response and explain why.
- 1.27 If you wish us to keep part of your response confidential, please clearly mark those parts of your response that you do wish to be kept confidential and those that you do not wish to be kept confidential. Please put the confidential material in a separate appendix to your response. If necessary, we will contact you to discuss which parts of the information in your response should be kept confidential and which can be published. We might ask for reasons why.
- 1.28 If the information you give in your response contains personal data under the General Data Protection Regulation (Regulation (EU) 2016/679) as retained in

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domestic law following the United Kingdom's withdrawal from the European Union ("UK GDPR"), the Gas and Electricity Markets Authority will be the data controller for the purposes of GDPR. Ofgem uses the information in responses in performing its statutory functions and in accordance with section 105 of the Utilities Act 2000. Please refer to our Privacy Notice on consultations, see Appendix 5.

- 1.29 If you wish to respond confidentially, we will keep your response confidential, but we will publish the number, but not the names, of confidential responses we receive. We will not link responses to respondents if we publish a summary of responses, and we will evaluate each response on its own merits without undermining your right to confidentiality.

### **How to track the progress of a consultation**

1. Find the web page for the call for input you would like to receive updates on.
2. Click 'Get emails about this page', enter your email address and click 'Submit'.
3. You will receive an email to notify you when it has changed status.

A consultation has three stages: 'Open', 'Closed (awaiting decision)', and 'Closed (with decision)'.

## 2. Overview of the NARM Funding Adjustment and Penalty Mechanism and proposed implementation

This section provides an overview of the NARM Funding Adjustment and Penalty Mechanism and explains how we propose to apply it at RIIO-2 close-out. It sets out how delivery is assessed against the BNRO, how funding adjustments are derived using pre-determined UCR, and how Clearly Identifiable delivery elements are treated separately where appropriate. This section also explains the three main stages of the close-out assessment process, Delivery Assessment, Justification Assessment and Incentive Value Calculation, and how these stages interact to determine final allowed NARM expenditure and any applicable penalties.

### NARM Funding Adjustment and Penalty Mechanism

- 2.1 The NARM Funding Adjustment and Penalty Mechanism is principally designed to work by anchoring ex-post funding adjustments to pre-determined ratios between funding (£m) and the network risk output this funding is expected to deliver (R£m). This is what we will refer to in this document as the ‘automatic’ funding adjustment mechanism.
- 2.2 Elements of over- and under-delivery on network risk output that qualify as ‘clearly identifiable’<sup>6</sup> are intended to be separated out of this ‘automatic’ adjustment mechanism, with appropriate funding adjustments for these delivery elements then applied on a case-by-case basis.
- 2.3 In effect, there are two channels to determining the final allowed NARM expenditure for a licensee at close out:
  - the ‘automatic’ funding adjustment mechanism which uses the baseline ratio between allowed funding and network risk output to adjust funding in cases where the delivered network risk output deviates from baseline; and
  - the ‘clearly identifiable’ mechanism which enables bespoke funding adjustments for qualifying over- or under-delivery elements.

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<sup>6</sup> Elements of over- and under-delivery on network risk output that qualify as ‘clearly identifiable’ ie specific, separable projects, schemes or programmes of work with quantifiable outputs and costs, are intended to be separated out of this ‘automatic’ adjustment mechanism, with appropriate funding adjustments for these delivery elements then applied on a case-by-case basis. Please see Appendix 4 for the full definition and the NARM handbook for the clearly identifiable qualifying criteria.

## **Baseline Network Risk Output (BNRO)**

- 2.4 The Baseline Network Risk Output (BNRO) represents the expected level of monetised network risk that a licensee is required to deliver by the end of the RIIO-2 price control period. It is derived from the licensee’s agreed investment plan and reflects the risk reduction expected from funded asset interventions. BNRO serves as the benchmark against which actual delivery, measured as the Outturn Network Risk Output (ONRO), is assessed. It is expressed in monetised risk units and segmented by Risk Sub-Category for Electricity and Gas Transmission, while Gas Distribution uses a single network-level value.
- 2.5 Network companies’ RIIO-2 business plans included a mix of investments—some delivering Monetised Risk Benefits (e.g. asset replacement/refurbishment) and others that do not (e.g. new or non-network assets). Ofgem assessed these proposals and allocated approved investments to one of three NARM Funding Categories: A1, which contributes to a company’s BNRO and is subject to the NARM Funding Adjustment and Penalty Mechanism; A2, which is funded under separate mechanisms but may contribute to ONRO if the original funding case falls away; and A3, which is ring-fenced and excluded from ONRO.
- 2.6 For Electricity and Gas Transmission, A1 is further divided into seven and three Risk Sub-Categories respectively, each assessed independently. While automatic trading between sub-categories is not permitted, companies may justify over-delivery in one area by referencing under-delivery in another. In Gas Distribution, BNRO is set at the network level with no sub-categories, so the terms Risk Category and Risk Sub-Category are used interchangeably.

## **Unit Cost of Risk (UCR)**

- 2.7 The relationship between funding and risk output is formalised as the Unit Cost of Risk (UCR), defined as the average funding per unit of network risk output delivered (£/R£). This UCR is applied at aggregate levels, rather than on a project-by-project (or programme of work) basis, with the specific application for each sector as follows:
- For Electricity Transmission, a unique UCR is defined for each of seven different asset sub-categories.
  - For Gas Transmission, a unique UCR is defined for each of three different risk levels (low, medium and high).
  - For Gas Distribution, a single UCR is defined for each licensee as a whole.
- 2.8 While there are these differences by sector, going forward we use the phrase ‘risk sub-category’ to refer to all such scenarios for simplicity.

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2.9 For all sectors, the UCR forms the basis for adjusting funding allowances in line with deviations in the delivered network risk output from baseline expectations. As such, UCRs are critical in determining the final funding allowances that licensees receive.

### **Overview of how the Mechanism will be implemented at close-out**

2.10 The proposed process for implementing the NARM Funding Adjustment and Penalty Mechanism at RIIO-2 close-out can be separated into three main stages. These stages do not necessarily need to be distinct from each other. It may be possible for there to be some overlap in terms of stage timings and activities. The three stages are:

1. Delivery Assessment
2. Justification Assessment
3. Incentive Value Calculation

2.11 The precise approaches, that we propose to use to carry out our assessment under the NARM Funding Adjustment and Penalty Mechanism, including licensees' submission requirements and timeframes for implementation, are set out in each of the relevant sections below. This has been informed by the development work, learning, or issues identified during RIIO-2.<sup>7</sup>

#### **Delivery Assessment**

2.12 This involves comparison of the licensee's ONRO against its BNRO. In order to be able to make a like-for-like comparison between the ONRO and BNRO, it will likely be necessary to 'normalise' the BNRO data to account for Non-Intervention Risk Changes, such as data cleansing, changes to the methodology, and slower or faster deterioration of assets.<sup>8</sup>

2.13 The licensee will be required to submit data to enable the Delivery Assessment in a format to be specified and issued under Standard Condition B15 (Regulatory Instructions and Guidance) for electricity transmission and under Standard

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<sup>7</sup> <https://www.ofgem.gov.uk/decision/narm-handbook-updates-threshold-justifying-clearly-identifiable-over-or-under-delivery-and-related-amendments>

<sup>8</sup> Risk changes resulting from revision of the NARM Methodology are addressed through a rebasing exercise (see section 2) and therefore will not need to be addressed during the delivery assessment. Guidance on the application of Non-Intervention Risk Changes is provided in NARM Handbook

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Condition A40 (Regulatory Instructions and Guidance) for gas transmission and gas distribution.

- 2.14 The Delivery Assessment will result in a decision from Ofgem on the extent to which it considers the licensee has Over-Delivered or Under-Delivered, or whether it has delivered its baseline for each Risk Sub-Category.

### **Justification Assessment**

- 2.15 The purpose of the Deadband around the BNRO is to determine whether justification is required for an Over-Delivery or Under-Delivery. For an Over-Delivery or Under-Delivery within the Deadband, no justification is required and it will be treated as 100% justified. For an Over-Delivery or Under-Delivery outside the Deadband, the licensee will be required to provide justification for the full amount of any Over-Delivery or Under-Delivery.
- 2.16 During this stage, Ofgem will consider the justification provided by the licensee for any Over-Delivery or Under-Delivery, as set out in section 5 of this document, along with the cost and other data that will be needed to calculate the value of any funding adjustments or penalties.
- 2.17 Ofgem will take a view on the proportion of Over-Delivery or Under-Delivery that has been justified, details of how this will be done are set out in section 5. If the licensee delivers within the Deadband<sup>9</sup> for a particular Risk Sub-Category, then the delivery will be considered justified for these purposes. Guidance on justification requirements can be found in section four of this document.
- 2.18 The licensee will also identify the delivery elements (e.g. specific projects) that, in its view, can be considered as Clearly Identifiable Over-Delivery and Clearly Identifiable Under-Delivery. The NARM Handbook sets out the criteria for Clearly Identifiable Over-Delivery and Clearly Identifiable Under-Delivery.<sup>10</sup> Ofgem's decision on any elements to be treated as Clearly Identifiable Over-Delivery and Clearly Identifiable Under-Delivery will determine the valuation approach for the purpose of the Incentive Value Calculation.

### **Incentive Value Calculation**

- 2.19 In calculating the value of the incentive under the NARM Funding Adjustment and Penalty Mechanism, Ofgem proposes to:

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<sup>9</sup> Defined in Appendix 1 – Glossary.

<sup>10</sup> [NARM-Handbook-v4.0.pdf](#)

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1. Determine the licensee's final allowances to reflect the licensee's level of delivery relative to its BNRO as well as the associated cost of delivery. Ofgem will use two valuation approaches:
  - a) Any delivery considered by Ofgem not to qualify as Clearly Identifiable Over-Delivery or Clearly Identifiable Under-Delivery will be assessed using a Unit Cost of Risk Benefit (UCR) approach. This assessment is carried out for each portion of delivery, i.e.,
    - Baseline (all cases)
    - Justified Under-Delivery (if relevant)
    - Unjustified Under-Delivery (if relevant)
    - Justified Over-Delivery (if relevant)
    - Unjustified Over-Delivery (has a value of zero)
  - b) Any delivery considered to qualify as Clearly Identifiable Over-Delivery or Clearly Identifiable Under-Delivery will be subject to a bespoke assessment of the efficient cost based on consideration of the fundamental underlying project components. For an Under-Delivery element, the adjustment of BNRO (i.e. claw-back) will be valued equal to the assessed value of that specific element/project we made at RIIO-2 Final Determinations. This may also include addressing partial delivery of a specific element or project.

These assessments will result in a final allowance for each Risk Sub-Category, which is calculated as follows<sup>11</sup>:

$$\left[ \begin{array}{c} \textit{Final} \\ \textit{Allowance}^* \end{array} \right] = \left[ \begin{array}{c} \textit{UCR} \times \textit{NRO} \\ \textit{(For each portion of delivery)} \end{array} \right] + \left[ \begin{array}{c} \textit{Adjustment for Clearly Identifiable} \\ \textit{Over Delivery and Under Delivery} \end{array} \right]$$

○ \* For a given Risk Sub-Category

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<sup>11</sup> The NRO in the formula refers to the Outturn Network Risk Output adjusted for Non-Intervention Risk changes and Clearly Identifiable Over-Delivery or Under-Delivery.

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2. Determine the value of any applicable penalty for Unjustified Under-Delivery.

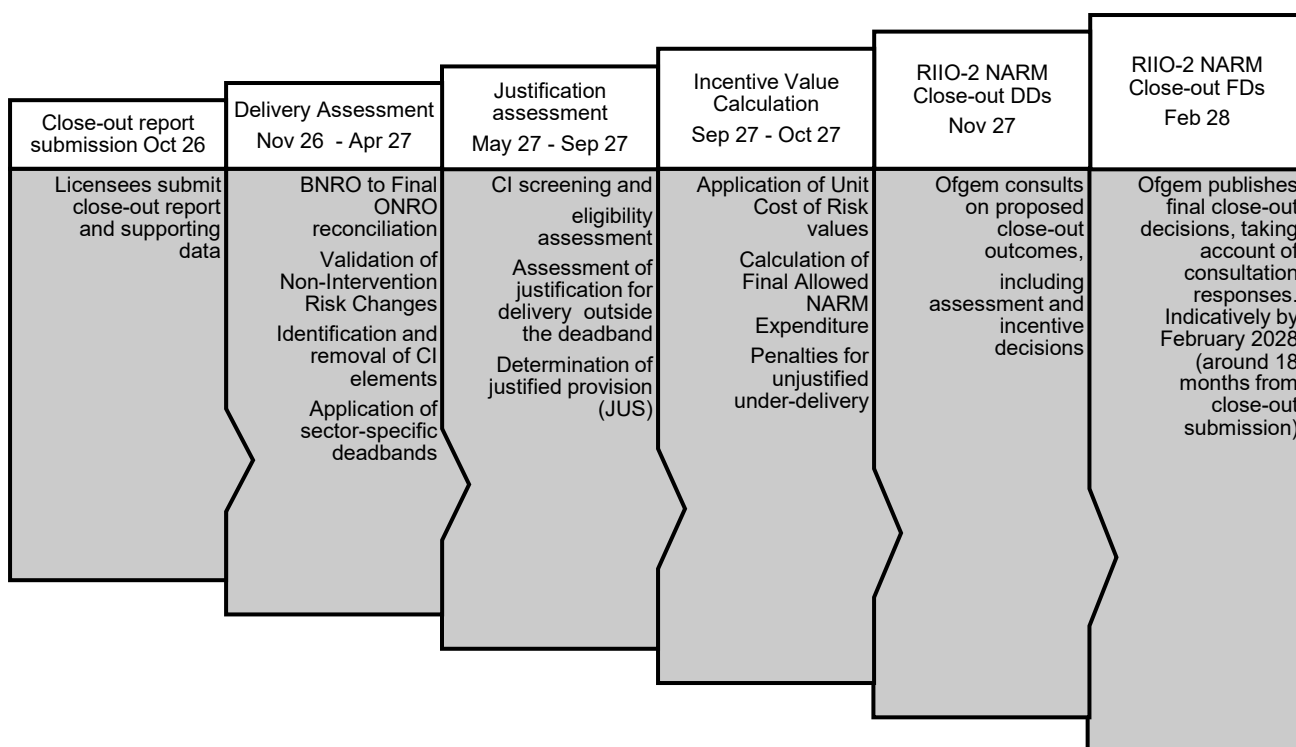
Any Unjustified Under-Delivery will be subject to a penalty. The penalty will be equal to 2.5% of the clawed back allowance associated with the Unjustified Under-Delivery.

2.20 Both the funding adjustment and penalty will be applied in the next price control through the Price Control Financial Model (PCFM).

## Timeline and submission requirements

2.21 The figure below illustrates the sequence of assessment stages following submission of the RIIO-2 NARM Close-out Report, leading to consultation on Draft Determinations and Final Determinations. Timings are indicative and remain subject to change.

Figure 1: Indicative RIIO-2 NARM close-out timeline and assessment stages.



### 3. Delivery Assessment

This section sets out the proposed process for assessing a licensee's delivery against its BNRO at the end of the RIIO-2 period. The aim is to determine whether the licensee has Over-Delivered, Under-Delivered, or delivered in line with expectations. To ensure a fair and like-for-like comparison, the assessment accounts for changes in risk not driven by licensee interventions (Non-Intervention Risk Changes) and separates out any Clearly Identifiable Over- or Under-Delivery elements. We propose to use the result of this assessment to determine whether the licensee's performance falls within the sector-specific Deadband, which in turn informs whether further justification is required.

- 3.1 As set out in the NARM Handbook, Delivery Assessment is undertaken at Risk Sub-Category level (or, for Gas Distribution, at network level), consistent with the structure of BNRO and ONRO within the NARM framework. While licensees may present supporting evidence at project or programme level, this is to explain the drivers of performance rather than to define separate units of assessment.
- 3.2 To ensure that appropriate funding adjustments are made, it is important that Ofgem has visibility at the project or programme level so it can decide whether a given delivery element should be treated through the 'automatic' or 'clearly identifiable' mechanisms. Without outturn data being made available at this level, Ofgem would not have the necessary data to check whether licensees have nominated the correct projects/programmes of work for the 'clearly identifiable' mechanism (based on the defined criteria in Section 10 of the NARM Handbook).

### **Preparatory steps for the Close-out process**

#### CI threshold decision

- 3.3 As detailed in our CI decision,<sup>12</sup> the NARM mechanism is working as intended and we therefore took the decision to set the CI threshold as 5%. While we accept the low CI UCR threshold could potentially result in projects or programmes of work being considered for CIOD/CIUD, compared to what was originally envisaged at FDs, we maintain confidence in our decision that a lower CI threshold is needed to mitigate against non-cost reflective outcomes.

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<sup>12</sup> <https://www.ofgem.gov.uk/decision/narm-handbook-updates-threshold-justifying-clearly-identifiable-over-or-under-delivery-and-related-amendments>

## Consideration of Year 4 RRP evidence and approach to CI materiality

- 3.4 As set out in our earlier decision on Clearly Identifiable Over-Delivery and Under-Delivery<sup>13</sup>, we indicated that we would consider the information submitted by licensees as part of their Year 4 Regulatory Reporting Pack (RRP) before providing any further guidance on how we would apply a pragmatic approach to CI outside of the immediate qualifying criteria. In particular, we signalled that this review would inform whether additional direction was required on the level of justification expected at close-out and on the potential benefits of fixing specific materiality thresholds.
- 3.5 We have now reviewed the Year 4 RRP data submitted by licensees, including the range, scale and distribution of projects that may potentially meet the CI qualifying threshold. In doing so, we considered whether the introduction of fixed or sector-specific materiality thresholds would improve the quality, consistency or proportionality of the projects proposed by licensees as Clearly Identifiable at close-out.
- 3.6 On balance, based on our review of the Year 4 RRP data, we do not consider that establishing definitive materiality thresholds would be appropriate. We do not consider there to be sufficient evidence that fixed thresholds would result in licensees providing a clearer or more effective view of the projects they propose for CI treatment. We also consider that the use of fixed thresholds could risk excluding relevant edge cases that may warrant CI consideration, given the diversity of project types, scales and risk impacts observed.
- 3.7 Instead, we consider that the guidance set out in this methodology, together with the CI qualifying criteria and evidencing requirements already established in the NARM Handbook, provides sufficient clarity for licensees. We therefore expect companies to be in a good position to identify projects or programmes of work that may warrant consideration as Clearly Identifiable at close-out, supported by the following guiding principles:
- Mechanistic distortion: Licensees should consider whether leaving a delivery element within the automatic FAPM, by virtue of the Risk Sub-Category it falls into, would produce outcomes that are materially driven by mechanical features of the funding model rather than by delivery performance. Where a

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<sup>13</sup> *ibid*

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project's impact on funding arises primarily from its interaction with sub-category UCRs or the structure of the mechanism such that it risks producing disproportionate, non-cost-reflective adjustments or undermines the operability of the mechanism, the project may be appropriate for consideration as Clearly Identifiable

- **Material contribution:** CI nomination should be focused on projects that make a material contribution to overall over- or under-delivery within a Risk Sub-Category (or at network level where applicable), rather than marginal contributors.
- **Attribution and separability:** The delivery element should be clearly separable from wider delivery activity, with risk and cost impacts that can be robustly attributed to that specific project or programme.
- **Proportionality:** Licensees should consider whether CI treatment is proportionate to the scale and impact of the delivery element, having regard to the level of additional justification and assessment effort that CI treatment entails.
- **Clarity of underlying drivers:** CI proposals should be grounded in clear delivery-driven outcomes. Where changes in assessed risk arise from Non-Intervention Risk Changes or broader system effects, these should be treated in accordance with the NIRC provisions and not nominated for CI treatment.
- **Clearly Identifiable Delivery: Screening, Qualification and Evidence Requirements.** As part of the Justification Assessment, licensees may identify delivery elements that they consider to be Clearly Identifiable Over Delivery or Clearly Identifiable Under Delivery. These elements must meet the qualifying criteria set out in the NARM Handbook and must be screened and evidenced in accordance with the requirements below.

3.8 We believe these principles support consistent and pragmatic identification of CI delivery elements at close-out alongside the formal qualifying criteria. They do not introduce additional tests or thresholds but provide a framework to help licensees

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exercise judgement in determining which projects warrant nomination as Clearly Identifiable.

### Project status definitions

3.9 Based on our assessment of Year 4 RRP submissions we found what we view as variance in how project statuses were applied across companies. We have therefore set out some standardised definitions and provide examples of when to use these in the table below. These project status definitions are intended to support consistent reporting and delivery assessment at close-out; the regulatory treatment of delayed or partially delivered projects, including where delivery extends into RIIO-3, is addressed separately in the section on NARM RIIO-2 / RIIO-3 crossover projects.

Table 1: Standardised Project Status Reporting Definitions (for RIIO-2 NARM Close-out)

Project Label	Definition	When to report	Optional Sub-Status / Notes
<b>Delayed</b>	A project that has started delivery activity in RIIO-2 but is not fully complete by the end of Year 5.	Use where one or more of the following apply: <ul style="list-style-type: none"><li>• Physical works, procurement, engineering design, or enabling works have started.</li><li>• Some risk reduction may have been delivered, but the scheme is not complete in RIIO-2.</li></ul>	Use where delivery has begun but the scope has materially changed relative to baseline assumptions (e.g. change in intervention type, asset count, or technical solution) and is now expected to be delivered in RIIO-3.
<b>Deferred</b>	A project planned in RIIO-2 and included in BNRO that will not be delivered in RIIO-2 and is proposed to continue into	Use where one or more of the following apply: <ul style="list-style-type: none"><li>• Required outages, consents or access were not available within RIIO-2.</li><li>• Delivery is delayed, but the intervention and intended risk reduction remain</li></ul>	Use where the baseline scope has changed prior to deferral to RIIO-3 (e.g. full replacement changed to partial refurbishment).

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	RIIO-3, subject to Ofgem's assessment and decision.	fundamentally required. <ul style="list-style-type: none"> <li>• The scheme continues into RIIO-3 under the same or a revised scope.</li> </ul>	
<b>Delivered</b>	A project that has been fully completed within RIIO-2, with the delivered risk reduction reflected in ONRO.	Use where both of the following apply: <ul style="list-style-type: none"> <li>• All intended physical works within scope are complete and operational.</li> <li>• Delivered risk aligns with the intervention as reported at close-out.</li> </ul>	Use where the final delivered solution does not differ materially from the baseline scope (e.g. part-delivery only or an alternative intervention approach).
<b>Not Delivered (including Cancelled)</b>	A project included in RIIO-T2 BNRO where no material delivery occurred in RIIO-2 and the scheme will not proceed in its baseline form in RIIO-3.	Use where one or more of the following apply: <ul style="list-style-type: none"> <li>• The project has been cancelled, abandoned, superseded, or replaced by a fundamentally different programme.</li> <li>• No significant RIIO-T2 risk reduction has been delivered.</li> <li>• Baseline BNRO must be removed unless justified under CI rules (CIUD).</li> </ul>	This status should trigger explicit consideration of CIUD treatment where BNRO was included at Final Determinations.

## Treatment of Non-Intervention Risk Changes

3.10 This summary is provided for ease of reference. Licensees should consult the Handbook directly for the full definitions, reporting expectations, and treatment methodology.<sup>14</sup>

### Classification and Evidencing of Non-Intervention Risk Changes

- 3.11 As part of the Delivery Assessment, the Authority distinguishes between Non-Intervention Risk Changes that arise at the level of individual projects and those that arise at a broader asset category or network level. This distinction, together with clear evidencing requirements, is necessary to ensure that adjustments to the Baseline Network Risk Output and the Outturn Network Risk Output are applied consistently, transparently, and can be robustly validated at close-out.
- 3.12 The Consolidated Non-Intervention Risk Change Summary and Normalisation Log forms the primary record through which the Authority will validate the identification, classification, and application of Non-Intervention Risk Changes at close-out. Licensees must ensure that the log is complete, internally consistent, and reconcilable to the adjustments reflected in the Adjusted Baseline Network Risk Output and Adjusted Outturn Network Risk Output.
- 3.13 Where the application of a Non-Intervention Risk Change results in movements that may appear counter-intuitive, including increases in assessed risk, negative values, or reversals from previously reported trends, licensees must provide a clear explanation linking the observed movement to the underlying evidence and the corresponding entry in the Consolidated Non-Intervention Risk Change Summary and Normalisation Log. This explanation must demonstrate that the movement arises from non-intervention factors rather than delivery decisions.
- 3.14 The Authority will use the Consolidated Non-Intervention Risk Change Summary and Normalisation Log, together with the supporting evidence provided, to determine whether Non-Intervention Risk Changes are valid and whether they should be reflected in the close-out assessment. Non-Intervention Risk Changes that are not appropriately evidenced or cannot be clearly reconciled through the log will not be validated for the purposes of adjusting the Baseline Network Risk Output or Outturn Network Risk Output.

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<sup>14</sup> Section 9 – Guidance on the treatment of Non-Intervention Risk Changes of the NARM Handbook v4.0.

## Project-level Non-Intervention Risk Changes

- 3.15 These are changes in assessed risk that arise from new or revised information specific to an individual asset or scheme, and which are not the result of the intervention itself. These may include, for example, updated condition information identified through inspection or survey, or asset faults discovered during the course of planned works that alter the assessed risk position independent of delivery choices.
- 3.16 Where such changes occur, they must be recorded as project-level Non-Intervention Risk Changes and reflected explicitly in the adjustment of the relevant project's baseline and outturn risk values. Licensees must provide clear supporting evidence demonstrating the nature of the change, the source of the information, and the resulting impact on assessed risk.
- 3.17 For the avoidance of doubt, changes in risk outputs or assumptions arising from revisions to the NARM Methodology are not treated as Non-Intervention Risk Changes. In line with the NARM Handbook (see in particular Chapter 4 on rebasing and Chapter 9.6 on Non-Intervention Risk Changes), such changes are addressed through rebasing of the BNRO to ensure comparability between BNRO and ONRO, rather than through NIRC normalisation as part of the Delivery Assessment.

## Category-level Non-Intervention Risk Changes

- 3.18 Category-level Non-Intervention Risk Changes are changes in assessed risk that arise from factors affecting a broader asset group, risk sub-category or network, rather than an individual project. These may include changes to underlying risk modelling assumptions, systematic data cleansing exercises, or re-parameterisation of consequence or deterioration inputs applied consistently across an asset category.
- 3.19 Category-level Non-Intervention Risk Changes will be reflected through aggregate adjustments to the Baseline Network Risk Output at the relevant level and must be supported by clear documentation explaining the rationale for the change, the scope of assets affected, and the quantified impact on risk outputs.
- 3.20 To support effective validation and audit of Non-Intervention Risk Changes, licensees must provide a Consolidated Non-Intervention Risk Change Summary and Normalisation Log as part of their close-out submission. This log must, as a minimum:
- identify each Non-Intervention Risk Change applied during RIIO-2;
  - state whether the change is project-level or category-level;

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- describe the underlying driver of the change and the evidence source relied upon;
- quantify the impact of the change on Network Risk Output; and
- clearly link the change to the corresponding adjustment reflected in the Adjusted Baseline Network Risk Output and Adjusted Outturn Network Risk Output.

3.21 Licensees must apply this classification and evidencing approach consistently and ensure that Non-Intervention Risk Changes are not conflated with delivery outcomes or with Clearly Identifiable Over-Delivery or Under-Delivery. Only validated and appropriately evidenced Non-Intervention Risk Changes will be reflected in the calculation of the Adjusted Baseline Network Risk Output and the Adjusted Outturn Network Risk Output used for close-out assessment.

### Licensees submission of Non-Intervention Risk Changes and Impacts

3.22 The BNRO was established using the best available asset risk data at the start of RIIO-2, reflecting the expected impact of licensees' funded interventions. However, over the course of the price control period, changes may occur that affect the measured risk position but are not the result of licensee interventions. These are referred to as Non-Intervention Risk Changes (NIRCs) and must be transparently reported and evidenced in the NARM Close-out Report and annual RIGs submissions.

3.23 As outlined in the NARM Handbook, Ofgem will normalise the BNRO to account for valid NIRCs, resulting in an Adjusted BNRO (NROBLAD). The ONRO must always reflect the latest available asset data. Examples of NIRCs include:

- Data cleansing (e.g. correcting asset records or condition scores)
- Note: excessive data cleansing beyond a 0.5% guide level may be subject to investigation
- Methodology changes that do not trigger formal rebasing
- Changes in consequence of failure (CoF), including:
  - Fixed network parameters (no adjustment)
  - Financial parameters (adjusted for neutrality)
  - Indirect interventions (may retain benefit)
- Differences in asset deterioration rates compared to forecasts
- Pre-RIIO-2 true-ups or legacy adjustments
- Changes in the asset base not linked to funded interventions

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- External factors covered by other regulatory mechanisms

3.24 These changes may increase or decrease the measured risk and could influence delivery outcomes. Ofgem will assess whether these changes are within the licensee's control and whether they should be excluded from the incentive assessment.

### **Ofgem Assessment of Non-Intervention Risk and Impacts**

3.25 Ofgem will review the reported changes to determine whether they are valid and material. Where appropriate, Ofgem will adjust the BNRO to remove the effects of these changes before comparing it to the ONRO. This ensures that the assessment of delivery is based on a like-for-like comparison and that licensees are not held accountable for risk movements outside their control.

3.26 This review may involve engagement with the licensee through Supplementary Questions (SQs) to clarify the nature, source, and materiality of the reported changes. If SQ responses materially affect the interpretation of risk changes, licensees may be asked to resubmit relevant parts of their submission.

3.27 Only after this adjustment process is complete will Ofgem proceed to assess whether the adjusted ONRO falls within the sector-specific Deadband and whether further justification or valuation is required.

### **Establishing the Final Delivery Position for RIIO-2**

3.28 Delivery performance will be assessed with reference to outcomes relating to the RIIO-2 period. Licensees are expected to reflect final delivery positions, including any projects completed or evidenced up to the point of close-out submission.

3.29 For the avoidance of doubt, this does not imply an open-ended delivery period. The close-out process is intended to capture the final position for RIIO-2, i.e. projects that have been delivered at the point of close-out submission.<sup>15</sup> Delivery extending beyond this point may not be reflected in the assessment where it would not be reasonable or proportionate to do so.

### **Treatment of Clearly Identifiable Over-Delivery and Under-Delivery**

3.30 As part of the Delivery Assessment, licensees are required to identify any delivery elements that they consider to be Clearly Identifiable Over-Delivery (CIOD) or

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<sup>15</sup> This reflects the Final Determinations position to allow project delivery to be finalised beyond 31 March 2026 up to the point of close-out submission, while maintaining a bounded close-out process.

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Clearly Identifiable Under-Delivery (CIUD). Eligibility and justification of CI proposals are assessed through the CI Screening and Justification process set out in section 5 of this document. These are specific projects or programmes of work that are separable from the wider delivery programme and meet the qualifying criteria set out in Chapter 10 of the NARM Handbook.

- 3.31 For the avoidance of doubt, the identification of Clearly Identifiable elements does not alter the level at which delivery performance is assessed. Consistent with the NARM framework, delivery performance at close-out is assessed at Risk Sub-Category level (or, for GD, at network level), with such elements contributing to those aggregated outcomes rather than being assessed separately.<sup>16</sup>
- 3.32 Before comparing ONRO to the Adjusted BNRO (NROBLAD), Ofgem removes any delivery elements that it determines to be Clearly Identifiable. This is done by subtracting the value of these elements (CLOOD) from the reported ONRO (NROOR), resulting in an adjusted ONRO (NROOAD). This ensures that the comparison reflects only the portion of delivery that is not subject to separate treatment, allowing for a fair and consistent assessment against the adjusted baseline.
- 3.33 The CIOD and CIUD elements are then assessed independently through a bespoke valuation process. Ofgem will determine whether each element meets the qualifying criteria and whether it is justified. Only those elements that are both clearly identifiable and justified will be included in the final funding calculation. Unjustified CIUD elements may also be subject to a penalty.

### Comparison of ONRO to BNRO (ONRO vs. BNRO)

- 3.34 Once the ONRO has been adjusted to exclude any Clearly Identifiable delivery elements (i.e.  $NROOAD = NROOR - CLOOD$ ), it is compared to the Adjusted BNRO (NROBLAD). This is the core quantitative step in the Delivery Assessment process, as set out in this document, this comparison determines whether the licensee has delivered more or less Network Risk Output than was expected at the outset of RIIO-2.
- 3.35 If the adjusted ONRO (NROOAD) is greater than the NROBLAD, this is classified as Over-Delivery. If it is lower, it is classified as Under-Delivery. The magnitude and direction of this difference inform whether the licensee's performance falls within the sector-specific Deadband or requires further justification. This comparison is

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<sup>16</sup> The criteria for Clearly Identifiable Over-Delivery and Clearly Identifiable Under-Delivery are set out in Chapter 10 of the NARM Handbook.

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conducted independently for each Risk Sub-Category (or at the network level for GD), ensuring a consistent and transparent assessment of delivery across all sectors.

### **BNRO to Final ONRO Reconciliation**

- 3.36 Once the ONRO has been adjusted to exclude any Clearly Identifiable delivery elements (i.e.  $NROOAD = NROOR - CLOOD$ ), it is compared to the Adjusted BNRO (NROBLAD). This comparison is the core quantitative step in the Delivery Assessment process and determines whether the licensee has delivered more or less Network Risk Output than was expected at the outset of RIIO-2.
- 3.37 As part of this process, licensees must provide a clear and auditable reconciliation showing how the final Network Risk Output position used for RIIO-2 close-out has been derived from the BNRO.
- 3.38 This reconciliation must set out, in a transparent and sequential manner:
- the Baseline Network Risk Output (BNRO) as set at RIIO-2 Final Determinations;
  - any adjustments to BNRO arising from validated Non-Intervention Risk Changes, resulting in an Adjusted BNRO; and
  - the Final Outturn Network Risk Output (Final ONRO) following the removal of any delivery elements determined by the Authority to be Clearly Identifiable and therefore subject to separate treatment.
- 3.39 The purpose of this reconciliation is to ensure that the final delivery position assessed at close-out can be clearly traced back to the original BNRO, with each adjustment step explicitly identified, quantified, and supported by appropriate evidence.
- 3.40 Licensees must present this reconciliation at the level of granularity required to support the Delivery Assessment, including by Risk Sub-Category where applicable. The reconciliation must distinguish clearly between changes in risk attributable to delivery, changes attributable to Non-Intervention Risk Changes, and changes attributable to the identification and removal of Clearly Identifiable delivery elements.
- 3.41 Only the Final ONRO derived through this reconciliation will be used by the Authority for the purposes of applying the sector-specific Deadband, determining the extent of any Over-Delivery or Under-Delivery, and informing subsequent stages of the NARM Funding Adjustment and Penalty Mechanism.

### **Presentation of BNRO to Final ONRO Variance**

3.42 Following completion of the BNRO to Final ONRO reconciliation, licensees must present the variance between the Adjusted BNRO and the Final ONRO in both:

- **absolute terms**, expressed as Network Risk Output (R£m); and
- **relative terms**, expressed as a percentage of the Adjusted BNRO.

3.43 This information must be provided for each relevant Risk Sub-Category (or at network level where applicable) and must be consistent with the reconciled values used for the Delivery Assessment.

3.44 The presentation of variance in both absolute and percentage terms is required to support transparent application of the sector-specific Deadband, to inform the assessment of the scale of any Over-Delivery or Under-Delivery, and to provide a clear evidential basis for subsequent stages of the NARM Funding Adjustment and Penalty Mechanism.

3.45 Only variances derived from the reconciled Final ONRO will be used by the Authority for the purposes of determining whether delivery falls within the Deadband, assessing justification, and calculating any funding adjustments or penalties.

### **Key Calculation Terms Used in the NARM Close-out Assessment**

3.46 The Authority applies the NARM Funding Adjustment and Penalty Mechanism using the calculation terms and relationships set out in the NARM Handbook and the licence. For clarity, the proposed key calculation terms referenced in this methodology are summarised below.

3.47 In the Delivery Assessment stage:

- NROBLAD (Adjusted Baseline Network Risk Output) represents the Baseline Network Risk Output adjusted to reflect validated Non-Intervention Risk Changes.
- NROOAD (Adjusted Outturn Network Risk Output) represents the Outturn Network Risk Output following the removal of any delivery elements determined by the Authority to be Clearly Identifiable and therefore subject to separate treatment.

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3.48 The comparison between NROOAD and NROBLAD forms the basis for the Deadband test and the determination of Over-Delivery or Under-Delivery.

3.49 In the Incentive Value Calculation stage:

- UCRBLAD (Adjusted Baseline Unit Cost of Risk) represents the unit cost of delivering Network Risk Output, derived in line with the baseline outputs used for close-out assessment.
- UCROAD (Adjusted Outturn Unit Cost of Risk) represents the unit cost of delivering the Outturn Network Risk Output.
- NXPFAC (Final Allowed NARM Expenditure) represents the final allowed expenditure determined under the NARM Funding Adjustment and Penalty Mechanism, following application of justification decisions and any penalties for Unjustified Under-Delivery.

3.50 These calculation terms will be applied by the Authority in accordance with the NARM Handbook. The proposed methodology does not amend the underlying calculation approach but sets out how the inputs to these calculations are derived and evidenced through the close-out assessment process.

## **Application of Deadbands**

3.51 Once ONRO is compared to the adjusted BNRO (NROBLAD), the result is assessed against the sector-specific Deadband. The Deadband is a tolerance range applied to each Risk Sub-Category (or network level for GD). For RIIO-2, the Deadband has been set at  $\pm 2\%$  for ET and  $\pm 5\%$  for GT and GD. If the ONRO falls within this range, the delivery is deemed to be within acceptable bounds and is automatically considered 100% justified. This means that no further justification is required from the licensee, and the full value of the delivery is recognised for the purposes of the NARM Funding Adjustment and Penalty Mechanism.

3.52 If the ONRO falls outside the Deadband, either above or below the NROBLAD, then the licensee must provide a justification for the full extent of the deviation. This justification is assessed by the Authority to determine the proportion of the over- or under-delivery that should be treated as justified. The outcome of this assessment directly informs the calculation of the licensee's final allowed expenditure and, in the case of unjustified under-delivery, the application of any penalties. The Deadband therefore acts as a threshold mechanism, ensuring that only material deviations from baseline expectations are subject to further scrutiny, while providing regulatory certainty for delivery within a reasonable range.

## 4. Treatment of NARM RIIO-T2/RIIO-T3 crossover projects

This section relates only to TOs and the 'NARM Crossover' term in Special Licence condition 3.10 of their licence. It sets out how the Authority will treat NARM projects that were included in RIIO ET2 but are delivered later than originally expected and, in whole or in part, extend into RIIO ET3. It explains how such projects will be assessed at RIIO ET2 close out through the NARM Funding Adjustment and Penalty Mechanism (FAPM), and how, where appropriate, allowances and outputs associated with delayed delivery may be considered for carry over into RIIO ET3 through the Non load Re opener established under Special Condition 3.10 of the electricity transmission licence.

This section does not create new policy and should be read alongside the proposed close out arrangements set out elsewhere in this methodology and the relevant provisions of the licence.

### **Treatment of RIIO-ET2 NARM Projects Delayed into RIIO-ET3**

- 4.1 In this section we set out the proposed guidance on the application of Special Condition 3.10 'Non-load re-opener' for the purposes of the NARM close-out process. This guidance does not form part of the licence condition and therefore does not have licence condition status, but rather is intended to provide additional detailed information to support licensees through the process.

#### **Assessment at RIIO-ET2 Close-out**

- 4.2 All NARM projects included in RIIO-ET2 are assessed at close-out on the basis of delivery achieved by the end of the RIIO-ET2 price control period. Where a project is delayed and the associated Network Risk Output has not been delivered by close-out, the Authority will assess that project through the RIIO-ET2 NARM Funding Adjustment and Penalty Mechanism (FAPM), in line with the methodology set out in this document.
- 4.3 Where delivery has not occurred, subject to the guidance outlined above, this may result in a downward funding adjustment under the FAPM. The close-out assessment will reflect the outputs delivered within RIIO-ET2 only and will not take account of forecast delivery beyond the close-out date.

#### **Consideration of Carry-Over into RIIO-ET3**

- 4.4 In circumstances where the Authority considers that the delivery of a delayed RIIO-ET2 NARM project remains beneficial for consumers despite the delay, and where delivery is expected to occur after the RIIO-ET2 FAPM assessment has been completed, the Authority may consider whether allowances and outputs associated with that project should be taken forward into RIIO-ET3.

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4.5 This consideration does not alter the RIIO-ET2 close-out assessment. Instead, it provides a separate route through which eligible projects may be remunerated in RIIO-ET3, using the Non-load Re-opener mechanism under Special Condition 3.10 of the ET licence, where the relevant criteria are met. This means that a delayed project may be considered for RIIO-ET3 carry-over while the associated RIIO-ET2 under-delivery is assessed as justified or unjustified. Equally, justified RIIO-ET2 under-delivery does not automatically make a project eligible for RIIO-ET3 carry-over.

### Use of Special Condition 3.10 (Non-load Re-opener)

- 4.6 Following completion of the RIIO-ET2 NARM close-out process, the Authority will determine which delayed NARM projects it considers continue to deliver consumer benefit despite the delay. For those projects:
- the allowances and outputs determined at RIIO-ET2 close-out may be listed in Appendix 4 to Special Condition 3.10 of the licence as NARM crossover projects; and
  - licensees may apply for adjustments under the Non-load Re-opener in respect of those projects, subject to the requirements and constraints of Special Condition 3.10.
- 4.7 Applications relating to NARM crossover projects listed in Appendix 4 may only be made during the first five working days of October 2028, in accordance with the licence.
- 4.8 The Authority will assess any such application in line with the requirements of Special Condition 3.10 and will consider whether the proposed allowances, outputs and delivery dates remain appropriate and continue to represent value for consumers.

### Information Required to Assess Carry-Over Projects

- 4.9 To support the Authority's assessment of delayed or partially delivered NARM projects for the purposes of RIIO-ET2 close-out and potential carry-over into RIIO-ET3, licensees will be required to provide additional information alongside their close-out submissions. This will include, as a minimum:
- Delivery status, clearly identifying which elements of the project have been completed by RIIO-ET2 close-out and which remain undelivered;
  - Delivered Network Risk Output, quantified and evidenced in line with the NARM methodology;

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- Remaining scope and outputs, identifying the elements proposed to be taken forward as a NARM crossover project;
- Updated cost and allowance information, consistent with the values determined at RIIO-ET2 close-out;
- Revised delivery timelines for any undelivered outputs; and
- Evidence of continued consumer benefit, demonstrating why delivery of the remaining outputs is still considered appropriate despite the delay.

4.10 This information will be used by the Authority to:

- complete the RIIO-ET2 close-out assessment;
- determine whether projects should be listed in Appendix 4 to Special Condition 3.10; and
- assess any subsequent application made under the Non-load Re-opener in RIIO-ET3.

## 5. Justification Assessment Process

This section outlines the proposed process and requirements for licensees to justify any Over-Delivery or Under-Delivery that falls outside the sector-specific Deadband. The purpose of this process is to determine the extent to which deviations from the Baseline Network Risk Output (BNRO) are justified, and therefore eligible for recognition in the final funding adjustment. Where delivery is within the Deadband, it is automatically considered 100% justified and no further evidence is required. However, for material deviations beyond the Deadband, licensees must provide a robust justification to support the proportion of delivery they believe should be recognised. This process also applies to delivery elements that meet the criteria for Clearly Identifiable Over-Delivery or Under-Delivery (CIOD/CIUD), which are subject to a separate valuation route but must still be justified.

### Criteria for Justified Over-Delivery and Under-Delivery

- 5.1 Following the completion of the Delivery Assessment, justification is applied to assess whether any identified deviations from the adjusted baseline position should be accepted.<sup>17</sup>
- 5.2 To be considered justified, the licensee must demonstrate that the deviation from the Adjusted BNRO (NROBLAD) was reasonable, necessary, and in the interest of consumers. Justification is assessed at the Risk Sub-Category level (or network level for GD) and must be supported by evidence that the variation could not reasonably have been anticipated or avoided at the time of setting the RIIO-2 plan.<sup>18</sup>
- 5.3 Justification is required only when:
  - The licensee's adjusted ONRO (NROOAD) falls outside the Deadband range around the adjusted BNRO (NROBLAD); and/or
  - The licensee has identified Clearly Identifiable Over-Delivery or Under-Delivery (CIOD/CIUD) elements.

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<sup>17</sup> while presented sequentially, the Delivery Assessment and Justification processes are not strictly linear and may operate iteratively in practice, with evidence and analysis refined as part of the overall close-out assessment.

<sup>18</sup> See NARM Handbook v4.0, Chapter 8, paragraph 8.3(b), which requires licensees to explain why the factors driving Over-Delivery or Under-Delivery could not reasonably have been forecast as part of the price control setting process and factored into the final NARM Workbook; and paragraph 8.4(d), which requires engineering justification papers to explain why the work that led to the Over-Delivery or Under-Delivery could not reasonably have been deferred or carried out.

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5.4 Delivery within the Deadband is automatically considered 100% justified and does not require further justification from the licensee for the purposes of the NARM Funding Adjustment and Penalty Mechanism.

### **CI Screening and Justification Pack**

5.5 For each proposed Clearly Identifiable delivery element, licensees must complete a standardised CI Screening and Justification Pack. This pack must, as a minimum:

- identify the relevant project or programme of work;
- set out the associated Baseline Network Risk Output and Outturn Network Risk Output;
- present the Baseline and Outturn Unit Cost of Risk values;
- show the resulting Unit Cost of Risk deviation; and
- summarise the justification for CI treatment with clear reference to supporting evidence.

5.6 The CI Screening and Justification Pack provides the primary means by which the Authority will assess whether the qualifying criteria for CIOD or CIUD are met. This assessment relates to the eligibility and justification of specific elements and does not alter the level at which delivery performance is assessed, as set out in Section 3.

### **UCR Screening and Precision**

5.7 An element may only qualify as Clearly Identifiable where the Outturn Unit Cost of Risk is either greater than 105% or less than 95% of the corresponding Baseline Unit Cost of Risk for the relevant Risk Sub-Category. Licensees must apply this screening test prior to proposing CI treatment.

5.8 To ensure consistent application of the UCR screening threshold, licensees must present Unit Cost of Risk values using sufficient decimal precision to avoid rounding effects that could incorrectly bring an element within or outside the  $\pm 5\%$  threshold.

### **Interaction with Non-Intervention Risk Changes**

5.9 Delivery elements will not qualify as Clearly Identifiable Over-Delivery or Under-Delivery where the underlying change in assessed risk is driven by a

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validated Non-Intervention Risk Change rather than by delivery choices.<sup>19</sup> Where risk movements associated with a project arise from Non-Intervention Risk Changes, these must be treated and evidenced in accordance with the NIRC provisions of this methodology and excluded from CI consideration.

### **Evidence Requirements**

5.10 Licensees must provide proportionate supporting evidence for each proposed Clearly Identifiable delivery element. This evidence must demonstrate that:

- the delivery element is separable and attributable;
- the observed cost and risk outcomes arise from delivery decisions; and
- the CI qualifying criteria are met.

5.11 Evidence may include, where relevant, engineering assessments, asset condition information, cost records, outage documentation, or other contemporaneous material. Assertions that are not supported by evidence will not be accepted for CI treatment.

5.12 The Authority will assess all proposed Clearly Identifiable delivery elements in accordance with the NARM Handbook. Elements that fail to meet the qualifying criteria or evidencing requirements will be treated through the standard delivery assessment.

### **Required Justification Evidence**

5.13 Licensees must ensure that all values, classifications and claims presented in the close-out narrative are consistent with the corresponding values submitted in the NARM close-out workbook. This includes, but is not limited to, Baseline and Outturn Network Risk Outputs, NIR Changes, CI delivery elements, UCR values and project status classifications.

5.14 Licensees must provide an explicit confirmation that the close-out narrative is consistent with the final submitted workbook. Where material inconsistencies are identified, the Authority may disregard the narrative position and rely on the workbook values for the purposes of the close-out assessment.

5.15 Where licensees provide supporting evidence to justify NIR Changes or CI delivery elements, this evidence must be presented in a structured and traceable manner.

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<sup>19</sup> Non-Intervention Risk Changes must be identified and validated in accordance with the Treatment of Non-Intervention Risk Changes section of this methodology.

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Licensees must provide a scheme-level evidence index that clearly links each item of evidence to the relevant project, adjustment or justification claim.

5.16 The evidence index must enable the Authority to readily identify, locate and review the material relied upon in support of close-out positions. Failure to provide a clear and complete evidence index may result in the Authority being unable to validate the relevant claim for the purposes of the close-out assessment.

5.17 The following evidence must be submitted as part of the licensee's NARM Close-out Report to support any claim of justified Over-Delivery or Under-Delivery. The following should be read with provisions in the NARM Handbook for the full and detailed requirements.<sup>20</sup>

a) Quantification and Attribution

- Identify the proportion of Over-/Under-Delivery considered justified
- Attribute delivery to specific projects or drivers

b) Explanation of Forecasting Limitations

- Why the deviation could not have been reasonably forecast at the time of Final Determinations
- Examples: new safety regulations, asset faults, obsolescence, or external constraints

c) Early Notification

- Evidence of early communication with Ofgem (e.g. via RRP's or correspondence)

d) Change in Intervention Plans

- Clear explanation of how and why the delivery plan changed from the assumptions underpinning the original BNRO
- Include deferrals, accelerations, substitutions, and cost impacts

e) Engineering Rationale

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<sup>20</sup> NARM Handbook v4, Section 8

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- Explain the technical drivers behind the deviation, including changes in asset condition, obsolescence, or safety requirements
- f) Cost-Benefit Analysis (CBA)
  - Provide a lifetime CBA comparing actual delivery to BNRO-aligned delivery
  - Demonstrate that the delivered outcome represents value for money
  - The analysis should:
    - Include direct and indirect benefits, including wider network impacts
    - Use consistent valuation assumptions (e.g. WACC, discount rates)
    - Reference relevant RIGs tables and NARM reporting data
    - Include sensitivity analysis to test key assumptions
- g) Broader Impacts
  - Explain any interactions with other outputs, PCDs, or obligations
- h) Stakeholder Engagement
  - Provide evidence of engagement with stakeholders (e.g. consumers, system operators, regulators)
  - Include consultation outcomes, safety reviews, or coordination with other programmes.

## **Ofgem's Evaluation Criteria**

5.18 In addition to the evidence requirements set out above, Ofgem will assess the justification against the following overarching principles:

- Whether the delivered outcome provides better value for consumers than the original BNRO target.
- The internal consistency of any submitted CBA, including alignment between assumptions, inputs, and outputs.

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- The presence of a credible alternative justification where a CBA is not feasible, such as legal, safety, or operational constraints.
- Evidence that the licensee has taken a balanced approach to risk across the network, considering the impact of delivery decisions on overall network performance and resilience.

## **Role of the JUS Percentage**

**5.19** Ofgem will assess the justification case and determine the proportion of Over- or Under-Delivery that is considered justified. This is expressed as the Justification Percentage (JUS). The JUS value is then used in the funding adjustment calculation to determine how much of the delivery is recognised for financial purposes.

If  $NROOAD > NROBLAD$  (Over-Delivery), then:

Justified Over-Delivery =  $JUS \times (NROOAD - NROBLAD)$

If  $NROOAD < NROBLAD$  (Under-Delivery), then:

Justified Under-Delivery =  $JUS \times (NROBLAD - NROOAD)$

## 6. Incentive Value Calculation

This section sets out the proposed process for determining the Incentive Value Calculation. The Incentive Value Calculation is the final stage of the NARM Funding Adjustment and Penalty Mechanism. It determines the Final Allowed Expenditure (NXPFAC) for each licensee based on their delivery performance relative to the BNRO, adjusted for Non-Intervention Risk Changes and Clearly Identifiable delivery elements. This stage also applies any penalties or rewards based on the justification status of Over- or Under-Delivery.

### Calculation Components

6.1 The incentive calculation comprises the following key components:

- **Baseline Delivery:** The portion of delivery that aligns with the adjusted BNRO (NROBLAD)
- **Justified Over-/Under-Delivery:** Delivery outside the Deadband that Ofgem deems justified
- **Unjustified Over-/Under-Delivery:** Delivery outside the Deadband that is not justified
- **Clearly Identifiable Delivery:** Projects assessed separately from the automatic UCR mechanism
- **Associated Costs:** Efficient costs linked to each delivery element
- **Delivery Adjustment Factors (DAFs):** Set to 0% for RIIO-2, meaning UCRs remain fixed at Final Determinations levels

6.2 Calculations are undertaken using the reconciled and assessed outputs determined in the Delivery and Justification Assessment sections.

### Final Allowed Expenditure (NXPFAC)

6.3 The Final Allowed Expenditure is calculated using the following formula:

$$\text{NXPFAC} = \sum (\text{NROFAC} \times \text{UCRFAC}) + \text{CIXFAC}$$

- **NROFAC:** Final Network Risk Output for each delivery element

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- UCRFAC: Final Unit Cost of Risk Benefit (fixed at UCRBLAD for RIIO-2)
- CIXFAC: Efficient costs for Clearly Identifiable Over-/Under-Delivery elements

6.4 This formulation brings together the delivery elements described in this methodology to determine the final allowed position, applying a consistent approach across baseline delivery and any justified or unjustified over- or under-delivery. In practical terms, the calculation adjusts the baseline expectation to reflect observed delivery performance, taking into account validated Non-Intervention Risk Changes and the treatment of Clearly Identifiable delivery elements. Full detail on the construction of each component, including the underlying formulae and parameter definitions, is set out in the NARM Handbook.

6.5 Each delivery element (baseline, justified/unjustified over-/under-delivery) is assessed separately using formulas set out in Table 4 of the Handbook, ensuring consistency with the BNRO and justification evidence. This includes:

- Baseline delivery
- Justified Over-Delivery
- Justified Under-Delivery
- Unjustified Over-Delivery
- Unjustified Under-Delivery

### Penalty for Unjustified Under-Delivery

6.6 If a licensee has Unjustified Under-Delivery, a penalty is applied:

$$\text{Penalty} = 2.5\% \times (\text{Unjustified Under-Delivery Value})$$

6.7 This penalty is applied to the clawed-back portion of the allowance and is added to the revenue adjustment in RIIO-3.

### Treatment of Clearly Identifiable Delivery Elements

6.8 Where delivery elements are clearly identifiable and separable from risk-based outputs (e.g. specific asset replacements, safety-driven interventions), they are assessed under CIXFAC.

## 7. Conclusions and next steps

- 7.1 We welcome responses to this consultation, both generally and on the specific questions set out in this document. In particular, we welcome views on whether our proposed RIIO-2 NARM close-out methodology is clear, proportionate and provides an appropriate basis for assessing licensees' delivery against their Baseline Network Risk Outputs.
- 7.2 Licensees are required to submit NARM Close-out Reports in accordance with Part D of Special Condition 3.1.12 and the relevant requirements set out in the NARM Handbook. This consultation explains the proposed methodology we will use to assess those submissions, including delivery against baseline outputs, justification for over- or under-delivery, and the calculation of any funding adjustments or penalties.
- 7.3 We are also consulting, through separate statutory consultation notices, on proposed modifications to the NARM Regulatory Instructions and Guidance and associated reporting templates. These templates are intended to form the basis of licensees' NARM close-out submissions and should be read alongside this methodology.

### **Consultation Question**

- Q1. Do you agree with our proposed approach to implementing the RIIO-2 NARM close-out assessment, specifically as set out in Section 3 (Delivery Assessment) and Section 5 (Justification Assessment process and requirements)? In responding, please focus on any specific practical considerations needed to apply the approach consistently at close-out.

- 7.4 Please send your response to [AssetRiskResilience@ofgem.gov.uk](mailto:AssetRiskResilience@ofgem.gov.uk) by **24 June 2026**. We will consider all responses before finalising our position and publishing our decision.

## Send us your feedback

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

- Do you have any comments about the quality of this document?
- Do you have any comments about its tone and content?
- Was it easy to read and understand? Or could it have been better written?
- Are its conclusions balanced?
- Did it make reasoned recommendations?
- Do you have any further comments?

Please send your feedback to [stakeholders@ofgem.gov.uk](mailto:stakeholders@ofgem.gov.uk).

## Appendix 1. Requirement for Close-out report

### Standardised Structure of the NARM Close out Report

- A1.1 To support a consistent, transparent and auditable close out assessment, licensees must present their RIIO 2 NARM Close out Report using a standardised narrative structure.
- A1.2 This structure is intended to provide a clear and consistent framework for presenting close out information. Licensees should read this appendix alongside the relevant provisions of the NARM Handbook, in particular Section 8.2, which sets out the full requirements for the content and submission of the NARM Close out Report by 31 October 2026 in accordance with Part D of Special Condition 3.1.12.
- A1.3 Licensees must ensure that the Close out Report is internally consistent and fully traceable to the accompanying NARM close out workbook and supporting evidence.
- A1.4 As a minimum, the Close-out Report must present information in the following order:
1. A summary of delivery performance against the Baseline Network Risk Output;
  2. The BNRO to Final ONRO reconciliation, including adjustments for Non Intervention Risk Changes and the removal of Clearly Identifiable delivery elements;
  3. Identification and assessment of any proposed Clearly Identifiable Over Delivery or Under Delivery;
  4. A consolidated summary of Non Intervention Risk Changes and normalisation adjustments; and
  5. A scheme level evidence index cross referencing all supporting material relied upon.
- A1.5 This structure does not remove or override any requirements set out in the NARM Handbook or Part D of Special Condition 3.1.12. Licensees remain responsible for ensuring that all information required under the Handbook and the licence is provided as part of the close out submission.

## Appendix 2. Interaction with Other Mechanisms

- A2.1 The treatment of interactions between NARM delivery and other RIIO-2 funding mechanisms is set out in the NARM Handbook. Licensees should refer to Chapter 7, Section G, paragraphs 7.17 to 7.18, for the treatment of NARM Funding Category A2 projects funded under separate mechanisms, and Chapter 7, Section H, paragraph 7.19, for the treatment of NARM Funding Category A3 projects and NARM Excluded Price Control Deliverables.
- A2.2 This methodology does not amend or replace those requirements. Licensees should ensure that any relevant interactions with other mechanisms are appropriately reflected in their NARM Close-out Report and supporting evidence.

## Appendix 3. Summary of key parameters for cost-benefit analysis submissions

A3.1 Licensees should take reasonable steps to ensure that all CBA submissions adhere to the following parameters. Submissions should be made in Excel format using the Ofgem template, with all assumptions and sources clearly documented.

<b>Parameter</b>	<b>Requirement</b>
<b>Discount Rate</b>	Use Ofgem-approved rate (e.g. consistent with RIIO-2 WACC)
<b>Time Horizon</b>	Lifetime of asset or intervention, typically 45–60 years
<b>Valuation of Risk Benefit</b>	Use UCRBLAD values fixed for RIIO-2
<b>Sensitivity Analysis</b>	Required for key assumptions (e.g. cost, benefit timing, risk monetisation)
<b>Direct and Indirect Benefits</b>	Must be included and clearly distinguished
<b>Reference Data</b>	Must cite relevant RIGs tables and NARM reporting sources
<b>Consistency</b>	Inputs and assumptions must be internally consistent across the model

## Appendix 4. NARM General Definitions

A4.1 This appendix provides a summary of key terms relevant to the NARM Funding Adjustment and Penalty Mechanism, including terms used in the close-out assessment and incentive calculation. These terms are drawn from, and should be read alongside, the definitions and calculation terms set out in the NARM Handbook v4.0, including Appendix 1: NARM Glossary and Table 7: Chapter 7 Defined Calculation Terms. In the event of any inconsistency, the definitions in the relevant licence conditions and the NARM Handbook take precedence.

<b>Term</b>	<b>Definition</b>
The Authority	Has the meaning given in Standard Condition A1 (Definitions and interpretation).
Baseline Allowed NARM Expenditure	The allowed expenditure associated with the Baseline Network Risk Outputs as set out in Appendix 1 to Special Condition 3.1 (Baseline Network Risk Outputs).
Baseline Network Risk Output (BNRO)	The cumulative total, for a given Risk Sub-Category, of Network Risk Outputs for all items allocated to 'NARM Funding Category A1' in the licensee's Network Asset Risk Workbook.
Baseline Unit Cost of Risk Benefit (UCR <sub>BL</sub> )	The Unit Cost of Risk Benefit derived from Baseline Network Risk Output and associated Baseline Allowed NARM Expenditure values.
Business Plan (BP)	The plan that the licensee was invited to submit by paragraph 2.25 of the document titled 'RIIO-2 Sector Specific Methodology – Core document', published by the Authority on 24 May 2019.

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<b>Term</b>	<b>Definition</b>
Clearly Identifiable Over-Delivery	Projects/schemes/programmes of work that is individually driving Over-Delivery disproportionately more than other combined projects/schemes/programmes of work in the work plan, as determined by the criteria outlined in Section 10 of the NARM Handbook.
Clearly Identifiable Under-Delivery	Projects/schemes/programmes of work that is individually driving Under-Delivery disproportionately more than other combined projects/schemes/programmes of work in the work plan, as determined by the criteria outlined in Section 10 of the NARM Handbook.
Cost-Benefit Analysis	The process of assessing the costs, benefits and risks of alternative ways to meet objectives. The expected costs and benefits of an intervention are estimated and the trade-off between costs and benefits is considered
Deadband	Is the range around the Baseline Network Risk Output which the Authority will use to take a view on the proportion of Over-Delivery or Under-Delivery that has been justified. Delivery within the Deadband range is deemed to be justified whereas delivery outside of the Deadband range is not automatically deemed to be justified. The size of the Deadband for each sector is set out in Section E, Table 3.
Delivery Adjustment Factor (DAF)	<p>A proportion of the difference between Baseline Unit Cost of Risk Benefit and Outturn Unit Cost of Risk Benefit that is applied in determining the Final Unit Cost of Risk Benefit.</p> <p>DAF can have a value of between 0% and 100%. For RIIO-2, DAF has a value of 0%, which means that the Unit Cost of Risk Benefit is fixed at the Final Determinations level.</p>

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Term	Definition
Electricity Transmission (ET)	Electricity Transmission Owners (ETOs); <ul style="list-style-type: none"> <li>• National Grid Electricity Transmission Plc (NGET)</li> <li>• Scottish Hydro Electric Transmission Plc (SHET)</li> <li>• SP Transmission Ltd (SPT)</li> </ul>
Electricity Distribution (ED)	Distribution Network Operators (DNOs); <ul style="list-style-type: none"> <li>• Electricity North West Limited</li> <li>• Northern Powergrid: x2 DNOs</li> <li>• SP Energy Networks: x2 DNOs</li> <li>• SSE Power Distribution: x2 DNOs</li> <li>• UK Power Networks: x3 DNOs</li> <li>• Western Power Distribution: x4 DNOs</li> </ul>
Equally Challenging	Means presenting equal or higher challenge to the licensee compared to the Baseline Network Risk Outputs, where challenge relates to the scope for a licensee to over-deliver by carrying out the same volume of interventions but selecting different assets for intervention from those assumed in the setting of the Baseline Network Risk Outputs, and the proportionate levels of over-delivery and under-delivery of Baseline Network Risk Outputs resulting from higher or lower level of intervention volumes.
Final Allowed Expenditure ( $NXP_{FAC}$ )	Means the calculation term as defined in Table 7 of this document.
Final Unit Cost of Risk Benefit ( $UCR_{FAC}$ )	Means the calculation term as defined in Table 7 of this document.

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Term	Definition
Gas Distribution (GD)	Gas Distribution Networks (GDNs); <ul style="list-style-type: none"> <li>• Cadent Gas Ltd: x4 GDNs</li> <li>• Northern Gas Networks Ltd (NGN)</li> <li>• Scottish &amp; Southern Gas Networks Plc (SGN): x2 GDNs</li> <li>• Wales and West Utilities Ltd (WWU)</li> </ul>
Gas Transmission (GT)	Gas Transmission Owner; <ul style="list-style-type: none"> <li>• National Grid Gas plc (NGGT)</li> </ul>
Justified Over-Delivery	Where a licensee provides evidence to support the delivery of a higher level of Network Risk Output than a Baseline Network Risk Output or other benchmark measure.
Justified Under-Delivery	Where a licensee provides evidence to support the delivery of a lower level of Network Risk Output than a Baseline Network Risk Output or other benchmark measure.
Long-term Monetised Risk	The Monetised Risk measured over a defined period of time greater than one year from a given start date and equal to the cumulative Single-Year Monetised Risk values over the defined period.
Monetised Risk (MR)	An estimation of asset risk as derived in accordance with the NARM Methodology as well as the similarly derived estimated risks associated with aggregated asset groupings, and disaggregated sub-components, as relevant.
Monetised Risk Benefit	The risk benefit delivered or expected to be delivered by an asset intervention, which:

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Term	Definition
	<ul style="list-style-type: none"> <li>a) is the difference between without intervention and with intervention Monetised Risk;</li> <li>b) can be measured over one year or over a longer period of time; and</li> <li>c) includes both direct (i.e. on the asset itself) and indirect (i.e. on adjacent assets or on the wider system) risk benefit.</li> </ul>
NARM Asset	An asset specified within the NARM Methodology and where its associated Monetised Risk can be estimated by applying the NARM Methodology.
NARM Asset Category	A group of assets with similar function and design as specified in the NARM Methodology.
NARM Close-out Report	The report each licensee is required to submit at the end of the RIIO-2 period under Part D of Special Condition 3.1 (Baseline Network Risk Outputs).
NARM Funding Adjustment and Penalty Mechanism	The mechanism for adjusting a network company's funding to reflect the Network Risk Outputs delivered during RIIO-2, and for applying penalties in certain delivery scenarios. This mechanism takes account of, among other things, the outturn level of Network Risk Output delivered in RIIO-2 relative to a company's Baseline Network Risk Outputs.
NARM Funding Category	<p>Broad categorisation used to indicate scope of NARM Funding Adjustment and Penalty Mechanism and interaction with other mechanisms.</p> <ul style="list-style-type: none"> <li>A1 – NARM Funding Adjustment and Penalty Mechanism</li> <li>A2 - Funding Under a Separate Mechanism</li> <li>A3 - Ring-fenced Project/Activity</li> </ul>

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Term	Definition
	B - Non-NARM Assets
NARM Methodology/ NARM Methodologies	<p>The methodology established in accordance with Special Condition 9.2 (Network Asset Risk Metric methodology).</p> <p>The NOMs Methodology in effect on 31 March 2021 is deemed to be the NARM Methodology in effect from 1 April 2021 until superseded.</p>
NARM Objectives	The objectives set out in Part B of Special Condition 9.2 (Network Asset Risk Metric methodology).
Network Asset Risk Metric (NARM)	The Monetised Risk associated with a NARM Asset or the Monetised Risk Benefit associated with a NARM Asset intervention.
NARM Workbook NARW	The workbook containing the licensee's Baseline Network Risk Outputs issued by the Authority in accordance with Part F of Special Condition 3.1 (Baseline Network Risk Outputs).
Network Output Measures (NOMs)	RIIO-1 equivalent of Network Asset Risk Metric (NARM).
Network Risk Output	The risk benefit delivered or expected to be delivered by an Asset Intervention and is calculated as the difference between Monetised Risk values associated with the “without intervention scenario” and the “with intervention scenario”. This is measured over a period equal to the assumed intervention lifetime from the end of the Price Control Period, which can vary for asset category or specific assets

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Term	Definition
	and intervention types for Electricity Transmission and Gas Transmission. For Gas Distribution only the first year of risk benefit is measured following the intervention.
NOMs Incentive Methodology	The document entitled "Network Output Measures (NOMs) Incentive Methodology" published by the Authority on 6 December 2018, as amended in accordance with Part B of Special Condition 7.10 (Close-out of the RIIO-1 Network Outputs).
NOMs Methodology	<p>For ET, the methodology approved under Special Condition 2L (Methodology for Network Output Measures) of the ETOs' Electricity Transmission licences as in force on 31 March 2021.</p> <p>For GT, the methodology approved under Special Condition 7D (Methodology for Network Output Measures) of NGGT's licence as in force on 31 March 2021.</p> <p>For GD, the methodology approved under Special Condition 4G (Methodology for Network Output Measures) of the GDNs' Gas Transporter licences as in force on 31 March 2021.</p>
NOMs Target	The required outputs related to relevant asset management work for each network company in RIIO-1.
Non-Intervention Risk Changes	Changes to the assessed risk of an asset or group of assets as a result of factors other than the categories of interventions and/or projects intended to be directly funded through Baseline Allowed NARM Expenditure as set out in section 9 of the NARM Handbook.

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<b>Term</b>	<b>Definition</b>
Outturn Network Risk Output (ONRO)	The Monetised Risk Benefit delivered during the Price Control Period through the licensee’s Asset Interventions. Where an asset is excluded from the BNRO and a condition score and/or criticality has changed, the ONRO must be based on the updated condition score and/or criticality of the asset to reflect the latest information.
Outturn Unit Cost of Risk Benefit	A Unit Cost of Risk Benefit derived from a licensee’s Outturn Network Risk Output (ONRO) and outturn associated cost values.
Over-Delivery (OD)	Delivery of a higher level of Network Risk Output than a Baseline Network Risk Output or other benchmark measure.
Price Control Financial Model (PCFM)	The financial model which derives the incremental changes to base revenue during the RIIO price control period. It does this by recalculating base revenues based on a limited number of updated variables.
Rebased Baseline Network Risk Output	A Baseline Network Risk Output that has been revised to give effect to a modified NARM Methodology as approved under paragraph 9.2.9 of Special Condition 9.2 (Network Asset Risk Metric methodology) pending the Authority’s approval. If approved by the Authority, the Rebased Baseline Network Risk Output will supersede the Baseline Network Risk Output for the purposes of Special Condition 3.1 (Baseline Network Risk Output).
Rebasing	The process of modifying the Baseline Network Risk Output as set out in Part C of Special Condition 3.1 (Baseline Network Risk Outputs).

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Term	Definition
RIIO-2 Business Plan Data Template (BPDT)	The document of that name submitted by the licensee to the Authority on 9 <sup>th</sup> December 2019.
RIIO-2 Final Determinations	The documents published by the Authority on 8 December 2020 setting out the Authority’s decisions in relation to the Price Control Period.
RIIO-3	The price control period that will commence on 1 April 2026 for Electricity Transmission, Gas Transmission and Gas Distribution licensees and on 1 April 2028 for Electricity Distribution licensees.
Risk Sub-Category	<p>A subdivision of Baseline Network Risk Output.</p> <ul style="list-style-type: none"> <li>• Electricity Transmission – 7 Risk Sub-Categories equivalent to the seven lead asset categories (Circuit Breaker, Overhead Line Conductor, Overhead Line Fittings, Overhead Line Tower, Reactor, Transformer, Underground Cable). An ETO project allocated to a Risk Sub-Category according to the asset category delivering the highest risk benefit.</li> <li>• Gas Transmission – 3 Risk Sub-Categories (Low, Medium, and High). Interventions are allocated to Risk Sub-Category according to the average Unit Cost of Risk Benefit they deliver.</li> <li>• Gas Distribution – no subdivision of BNRO.</li> </ul> <p>The NARM Funding Adjustment and Penalty Mechanism operates independently for each Risk Sub-Category.</p>
Risk Pound (R£)	The unit used to denote Monetised Risk values. R£ is used to differentiate from financial monetary values.
Single-Year Monetised Risk	The Monetised Risk measured over a given one-year time period.

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<b>Term</b>	<b>Definition</b>
Under-Delivery	Delivery of a lower level of Network Risk Output than a Baseline Network Risk Output or other benchmark measure.
Unit Cost of Risk Benefit (UCR)	The average cost of delivering a single unit (one Risk Pound, R£1) of Monetised Risk Benefit for a given intervention in an asset or group of assets.
Unjustified Over-Delivery	Where a licensee is unable to provide reasonable evidence to support the delivery of a higher level of Network Risk Output than a Baseline Network Risk Output or other benchmark measure.
Unjustified Under-Delivery	Where a licensee is unable to provide reasonable evidence to support the delivery of a lower level of Network Risk Output than a Baseline Network Risk Output or other benchmark measure.

## Appendix 5. Privacy policy

### **Personal data**

The following explains your rights and gives you the information you are entitled to under the General Data Protection Regulation (GDPR).

Note that this section only refers to your personal data (your name address and anything that could be used to identify you personally) not the content of your response to the consultation.

#### **1. The identity of the controller and contact details of our Data Protection Officer**

The Gas and Electricity Markets Authority is the controller, (for ease of reference, “Ofgem”). The Data Protection Officer can be contacted at [dpo@ofgem.gov.uk](mailto:dpo@ofgem.gov.uk)

#### **2. Why we are collecting your personal data**

Your personal data is being collected as an essential part of the consultation process, so that we can contact you regarding your response and for statistical purposes. We may also use it to contact you about related matters.

#### **3. Our legal basis for processing your personal data**

As a public authority, the GDPR makes provision for Ofgem to process personal data as necessary for the effective performance of a task carried out in the public interest. i.e. a consultation.

#### **4. With whom we will be sharing your personal data**

Information: Include here all organisations outside Ofgem who will be given all or some of the data. There is no need to include organisations that will only receive anonymised data. If different organisations see different set of data then make this clear. Be as specific as possible.

#### **5. For how long we will keep your personal data, or criteria used to determine the retention period.**

Your personal data will be held for (be as clear as possible but allow room for changes to programmes or policy. It is acceptable to give a relative time e.g. ‘six months after the project is closed’)

#### **6. Your rights**

The data we are collecting is your personal data, and you have considerable say over what happens to it. You have the right to:

- know how we use your personal data

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- access your personal data
- have personal data corrected if it is inaccurate or incomplete
- ask us to delete personal data when we no longer need it
- ask us to restrict how we process your data
- get your data from us and re-use it across other services
- object to certain ways we use your data
- be safeguarded against risks where decisions based on your data are taken entirely automatically
- tell us if we can share your information with 3<sup>rd</sup> parties
- tell us your preferred frequency, content and format of our communications with you
- to lodge a complaint with the independent Information Commissioner (ICO) if you think we are not handling your data fairly or in accordance with the law. You can contact the ICO at <https://ico.org.uk/>, or telephone 0303 123 1113.

**7. Your personal data will not be sent overseas** (Note that this cannot be claimed if using Survey Monkey for the consultation as their servers are in the US. In that case use “the Data you provide directly will be stored by Survey Monkey on their servers in the United States. We have taken all necessary precautions to ensure that your rights in term of data protection will not be compromised by this”.

**8. Your personal data will not be used for any automated decision making.**

**9. Your personal data will be stored in a secure government IT system.** (If using a third party system such as Survey Monkey to gather the data, you will need to state clearly at which point the data will be moved from there to our internal systems.)

**10. More information** For more information on how Ofgem processes your data, click on the link to our “[ofgem privacy promise](#)”.