

Transmission Price Control Review: Draft licence modifications

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Overview:

The Transmission Price Control Review (TPCR) will set out proposals for the revised electricity and gas transmission price controls to apply from 1 April 2007. To give effect to these proposals we will need to modify the licences of each transmission company.

This document outlines the licence changes we think are needed, and sets out the process for completing this work. We believe that it is important to engage stakeholders at an early stage in the process. Where possible we have included working drafts of the relevant proposed licence conditions to help inform debate. In other cases we provide a narrative description of the changes we envisage.

Contact name and details: Robert Hull, Director Transmission

Tel: 020 7901 7050

Email: robert.hull@ofgem.gov.uk

Team: Transmission Directorate

Context

The Transmission Price Control Review (TPCR) has been taken forward through a series of five consultation documents starting in July 2005. We will publish Final Proposals in December 2006. Implementation of our Final Proposals will require formal modifications of the licences of each of the electricity transmission companies and National Grid Gas National Transmission System's (NGG NTS) gas transporters licence.

We published an open letter last month setting our views on how the licence might need to be amended in relation to our proposals for gas offtake. This document sets out our current thinking on the changes we're proposing to NGG NTS's licence and the three electricity transmission licences. This reflects the position we set out in our September Updated Proposals document but is subject to change in light of consideration of responses to that document and further consultations.

Associated Documents

- Transmission Price Control Review: Draft Licence Modifications, November 2006 (Ref No. xx)
- TPCR 2007-2012 Updated Proposals, September 2006 (Ref No. 170/06)
- TPCR 2007-2012 Updated Proposals, Appendices, September 2006 (Ref No. 170/06a)
- TPCR 2007-2012 Initial Proposals, June 2006 (Ref No. 104/06)
- TPCR 2007-2012 Initial Proposals, Main Appendices, June 2006 (Ref No. 104b/06)
- TPCR 2007-2012: Third Consultation, March 2006 (Ref No. 51/06)
- TPCR 2007-2012: Third Consultation, Supplementary Appendices, March 2006 (Ref No. 51/06b)
- TPCR Second Consultation, December 2005 (Ref No. 277/05)
- TPCR Initial Consultation, July 2005 (Ref No. 172/05)

Table of Contents

Appendix 5 – NGG NTS Gas Entry - Mapping of existing licence conditions to proposed new structure	1
Appendix 6 – NGG NTS Gas Entry: Draft legal text - Capacity reallocation obligations	6
Capacity substitution obligation	6
Capacity transfer facilitation obligation.....	6
Capacity trade facilitation obligation	7
Appendix 7 - Proposed text - new NGET licence conditions	9
Amended Transmission Network Reliability Incentive - proposed transmission licence drafting: Special Condition AA5F	9
SF6 Incentives - Special condition []: adjustment to restriction of transmission charges due to SF ₆ incentive	14
Innovation Funding Incentive - Special condition [] – Calculation of charge restriction adjustments arising from the innovation funding incentive scheme ..	15
Appendix 8 – Draft legal text - NGET SO conditions.....	18
Appendix 9 – Proposed new Scottish licence conditions.....	28
Amended Transmission Network Reliability Incentive: Special Condition Q - Adjustment to Restriction of Transmission Charges due to Transmission Network Reliability Incentive	28
SF6 Incentives: Special condition [] - adjustment to restriction of transmission charges due to SF ₆ incentive	34
Innovation Funding Incentive - Special condition [] – Calculation of charge restriction adjustments arising from the innovation funding incentive scheme ..	35
Appendix 10 – Draft legal text - Amended Standard Conditions B ...	38

Appendix 5 – NGG NTS Gas Entry - Mapping of existing licence conditions to proposed new structure

1.1. This appendix shows how the proposed new Special Condition C8D "NTS gas entry incentives, costs and revenues" and other new conditions would relate to the existing provisions of the licence covering gas entry and other arrangements. The tables below give an initial indication of the nature of changes to the current licence drafting that will be made.

1.2. The first table breaks down current Special Conditions C8A and C8B, which contain most of the licence drafting relevant for gas entry incentives. It shows the likely impact of the new licence drafting on the existing text in those special conditions, in terms of where equivalent text is likely to feature in the new NTS licence. The key licence conditions for gas entry are highlighted in bold.

Current licence condition	Impact of new proposals (SC = Special Condition)
Special Condition C8A – Revenue restriction definitions in respect of the NTS transportation owner activity and NTS system operation activity	This condition will be retained as SC C8A .
Para 1 - definitions	Some new definitions will be required for gas entry, for example for the new "capacity reallocation obligation" provisions and for the two separate buyback incentives.
Special Condition C8B – Revenue restriction of revenue in respect of the NTS transportation owner activity and NTS system operation activity	This condition will be separated into two. - SC C8B "The NTS transportation owner activity revenue restriction" will cover the TO revenue restriction. Changes to this section are not considered in this document but will be consulted on separately. - SC C8C "The NTS system operation activity revenue restriction" will cover the SO revenue restriction.
<i>Part 1 a - NTS TO revenue restriction</i>	-
Para 1 - TO principal restriction	Covered in SC C8B.
Para 2 - TO revenue	Covered in SC C8B.
Para 3 - maximum TO revenue	Covered in SC C8B.
Para 4 - TO reporting obligations	Covered in SC C8B.
Para 5 - TO disapplication	Covered in SC C8B.

<i>Part 2 - NTS SO revenue restriction</i>	-
Para 12 - SO principal restriction	Covered in SC C8C.
Para 13 - SO revenue	Covered in SC C8C.
- 13 (1) principal formula (SOR)	Covered in SC C8C.
- 13 (2) SO revenue from entry capacity sales	Covered in SC C8C. [There are unlikely to be entirely new sources of SO revenue from entry capacity sales so new text is probably not required.]
- 13 (3) associated SO charges	Covered in SC C8C.
Para 14 - maximum SO revenue	Covered in SC C8C.
- 14(1) principal formula (SOMR)	Covered in SC C8C.
- 14(2) SO incentive revenue	Covered in SC C8C. This needs to incorporate the revised buyback incentive revenues from the two separate buyback incentives (for operational and incremental buybacks). The default incentive revenue for the incremental buyback incentive will be zero.
- 14(3) SO costs	Covered in SC C8C. This needs to incorporate any costs incurred under the two separate buyback incentives (for operational and incremental buybacks).
- 14(4) SO revenue adjustment factor	Covered in SC C8C.
- 14(5) entry capacity investment incentive revenue	Covered in SC C8D. New text needs to incorporate details of the "capacity reallocation obligations" and various other new aspects of the proposals. The current text in 14(5) is likely to be substantially simplified and redrafted.
- 14(6) exit capacity investment incentive revenue	Covered in SC C8E.
- 14(7) entry capacity buyback incentive revenue	Covered in SC C8D. New text on buyback needs to incorporate details on the two separate buyback incentives.
- 14(8) system balancing incentive revenue	Covered in SC C8F.
- 14(9) residual gas balancing incentive revenue	Covered in SC C8F.
- 14(10) internal cost incentive revenue	Covered in SC C8G.
- 14(11) adjustment factor to principal formula (SOMR)	Covered in SC C8C.

- 14(12) exit capacity buyback and interruption incentive revenue	Covered in SC C8E.
- 14 (13) quality of information incentive	Covered in SC C8F.
Para 15 - SO reporting obligations	Covered in SC C8C.
Para 16 - SO disapplication	Covered in SC C8C.

1.3. The tables break down paragraphs 14(5) and 14(7) of Special Condition C8B, respectively. These two paragraphs currently contain most of the detailed provisions relating to two main gas entry SO incentives, namely the entry capacity investment incentive and the entry capacity buyback incentive, and equivalent material (although substantially redrafted and simplified in the case of paragraph 14(5)) is likely to make up most of the new text under Special Condition C8D.

1.4. The tables provide a mapping of the current text in paragraphs 14(5) and 14(7) of Special Condition C8B to the proposed six sections of the new Special Condition C8D:

- Section 1: Obligations for NGG NTS to release capacity;
- Section 2: Capacity transfer and trade facilitation obligations;
- Section 3: Changes to obligations for NGG NTS to release capacity;
- Section 4: Revenue drivers for changes to NGG NTS's obligations to release capacity;
- Section 5: The incentive on NGG NTS regarding operational buybacks, and
- Section 6: The incentive on NGG NTS regarding incremental buybacks.

1.5. Breakdown of current paragraph 14 (5) of Part 2 of Special Condition C8B:

Current licence condition	Impact of new proposals
Para 14(5) entry capacity investment incentive revenue	Covered in SC C8D.
14(5)(a) principal formula	Covered in SC C8D. A new principal formula is likely to be set out at the start of SC C8D, while some details contained in the current principal formula (eg in relation to incentive revenues from sales of obligated incremental entry capacity, including the revenue driver functions) are likely to be reflected in Section 4 of SC C8D.
14(5)(b) determination of obligated incremental entry capacity	Covered in SC C8D. Equivalent text is likely to be included in Section 3 of SC C8D.
14(5)(c) allocation of firm entry capacity	Covered in SC C8D. Interactions with the capacity allocation regime (the auction regime) are likely to be

	covered in Section 1 of SC C8D.
14(5)(d) SO incentive revenue in respect of obligated incremental entry capacity	Covered in SC C8D. Equivalent text is likely to be included in Section 4 of SC C8D. It is likely that this text can be simplified as we are not proposing to retain the concepts of "minimum" and "maximum" entry capacity investment incentive revenue.
14(5)(e) maximum entry capacity investment incentive revenue	Covered in SC C8D. However this paragraph is likely to become largely superfluous as we are not proposing to retain the concept of "maximum" entry capacity investment incentive revenue.
14(5)(f) obligated entry capacity for which the licensee still has an obligation to offer for sale	Covered in SC C8D. Equivalent but revised text defining "capacity release obligations" net of capacity previously sold is likely to feature in Section 1 of SC C8D. Text on the new "capacity substitution obligation" is likely to feature either in Section 1 or Section 4 of SC C8D. Text on the new "capacity transfer facilitation obligation" and "capacity trade facilitation obligation" will feature in Section 2 of SC C8D.
14(5)(g) calculation of obligated entry capacity	Covered in SC C8D. Equivalent but revised text defining obligated "baseline" entry capacity and "obligated incremental entry capacity" is likely to feature in Section 1 of SC C8D. Some details on the calculation of "obligated incremental entry capacity" may also feature in Section 3 of SC C8D.
14(5)(h) minimum entry capacity investment incentive revenue	Covered in SC C8D. However this paragraph is likely to become largely superfluous as we are not proposing to retain the concept of "minimum" entry capacity investment incentive revenue.
14(5)(i) calculation of entry capacity incentive revenue	Covered in SC C8D. However this paragraph is likely to become largely superfluous as we are not proposing to retain the concept of SO incentive revenue for obligated incremental entry capacity being a function of the revenues NGG NTS earns from sales of entry capacity in the auctions.
14(5)(j) non-obligated incremental entry capacity revenue	Covered in SC C8C and SC C8D. The concept of non-obligated incremental entry capacity revenue will continue to feed into the definition of SO revenues (currently in paragraph 13, but to be covered in SC C8C in the new licence) and into the definition of the buyback performance measure for the operational buyback incentive (currently in paragraph 14(7)(b), but to be covered in Section 5 of SC C8D in the new licence).
14(5)(k) annual revenues from entry capacity sales	Most likely to be covered in SC C8C. Equivalent formulae for revenues derived from sales of obligated, non-obligated and permanent obligated incremental entry capacity are likely to continue to feed into the definition of SO revenues (currently in paragraph 13, but to be covered in SC C8C in the

	new licence).
14(5)(l) revenues from on the day sales of entry capacity	Covered in SC C8C and SC C8D. Revenues from on the day sales of entry capacity are likely to continue to feed into the definition of SO revenues (currently in paragraph 13, but to be covered in SC C8C in the new licence) and into the definition of the buyback performance measure for the operational buyback incentive (currently in paragraph 14(7)(b), but to be covered in Section 5 of SC C8D in the new licence).

1.6. Breakdown of current paragraph 14 (7) of Part 2 of Special Condition C8B:

Current licence condition	Impact of new proposals
14(7) entry capacity buyback incentive revenue	Covered in SC C8D. This paragraph corresponds to new section 5 of SC C8D (on the operational buyback incentive). Similar text on the operational buyback incentive will feature in section 5. Equivalent text for the incremental buyback incentive will feature in section 6 of SC C8D.
14(7)(a) principal formula	Covered in SC C8D. There is likely to be a principal formula for the operational buyback incentive in Section 5 of SC C8D and a principal formula for the incremental buyback incentive in Section 6 of SC C8D.
14(7)(b) entry capacity buyback performance measure	Covered in SC C8D. Separate buyback performance measures will be defined in Section 5 of SC C8D for the operational buyback incentive and in Section 6 of SC C8D for the incremental buyback incentive.

Appendix 6 – NGG NTS Gas Entry: Draft legal text - Capacity reallocation obligations

This is preliminary draft legal text. This text will therefore be subject to further changes pursuant to Ofgem internal review and in the light of comments received in respect of all prior relevant consultation processes.

Capacity substitution obligation

1.1. In relation to any release of entry capacity above the baselines the licensee shall provide to Ofgem in writing a calculation of all [[reasonable]] substitution of unsold capacity from existing entry points that could be used to provide the incremental obligated entry capacity.

1.2. The information provided shall take the form of a statement for each entry point documenting the amount of capacity transferred to that entry point. Unless the Authority otherwise directs the licensee in writing within [[X]] days of receiving this statement the term SOENAC it shall, for each entry point *i*, take the value from this statement for the corresponding entry point.

Capacity transfer facilitation obligation

1.3. Before any auction or other mechanism for the release of entry capacity, the licensee shall respond to any request from a shipper for a capacity transfer rate for use in that auction. A capacity transfer rate shall be a rate by which entry capacity bought at a specified entry point (the “**giving point**”) can be utilised at a different specified entry point (the “**receiving point**”).

1.4. Where a shipper has been provided with a capacity transfer rate by the licensee any entry capacity purchased by that shipper at the giving point can be transferred, within [a specified period relating the date of the relevant auction], at the shippers discretion, from the giving point to the receiving point at the specified capacity transfer rate.

1.5. In providing the capacity transfer rate specified the licensee shall act in accordance with the methodology established.

1.6. By [[date]] the licensee shall establish a methodology by which it will determine the method of calculation for capacity transfer rates. The methodology shall be designed in a manner best calculated to meet the following objectives:

- Compliance with the methodology will reflect the physical possibilities of transferring capacity across the network;
- The methodology will facilitate effective competition between gas shippers, gas suppliers and other parties associated with the gas industry, and
- The methodology will be designed in such a way as to allow any reasonable gas shipper to make an estimate of how the methodology will be applied.

1.7. The licensee shall, if so directed by the Authority and in any event at least once a year, review the statement in consultation with gas shippers and other interested parties likely to be affected by it and allow each of them a period of not less than 28 days in which to make representations.

1.8. The licensee shall from time to time make revisions to its established methodology to ensure that it meets the relevant objectives. However the licensee shall not, without written consent from the Authority, make any revisions to the methodology unless it has:

- Sent a copy of the proposed revisions to the Authority, gas shippers who are signatories to the licensee's network code, and any other party who requests one;
- Consult interested parties and allow them a period of not less than 28 days in which to make representations;
- Within 7 days of the close of the consultation submit to the Authority a report setting out: the revisions originally proposed; the representations (if any) made to the licensee; and any change to the revisions, and
- Not receive a direction from the Authority that it should not proceed with the revisions.

1.9. The licensee shall, by [] each year, provide the Authority with a statement indicating the licensee's views on the application and implementation of the methodology setting out its views on the extent to which the objectives have been met.

1.10. The licensee may make a charge for providing a transfer capacity rate and such a charge shall not to exceed the reasonable costs incurred by the licensee in making such calculations and carrying out such modelling as is necessary.

1.11. The licensee may make a charge for any copy of a statement, report or revision sent pursuant to this condition of an amount reflecting the licensee's reasonable costs of providing such a copy which shall not exceed the maximum amount specified in directions issued by the Authority for the purposes of this condition.

Capacity trade facilitation obligation

1.12. The licensee shall respond to any request from any two shippers for a capacity transfer rate to allow the entry capacity at one entry point held by one of the shippers to be transferred to the other shipper at a different entry point at a particular date or period. A capacity transfer rate shall be a rate by which entry

capacity bought at a specified entry point (the "**giving point**") can be utilised at a different specified entry point (the "**receiving point**").

1.13. The capacity transfer rate may be subject to a time limited period during which it is valid. Said time limited period shall be as long as reasonably practicable.

1.14. Where a pair of shippers have been provided with a capacity transfer rate and the shippers both indicate to the licensee, in writing and within the time limited period (if any) specified, that they wish to transfer an amount of capacity at that rate, the licensee shall effect the transfer of entry capacity.

In providing the capacity transfer rate specified the licensee shall act in accordance with the methodology established.

Appendix 7 - Proposed text - new NGET licence conditions

1.1. The following section sets out our current views on the amendments and additions to NGET's special licence conditions that would be necessary to implement a number of the proposals (particularly on new policy areas) put forward in the September updated proposals document. The licence drafting we have provided relates to amendments to the existing reliability incentive scheme, and additions necessary to introduce an SF6 incentive and the Innovation Funding Incentive. Throughout the drafting, square brackets denote numbers or references that are yet to be finalised, and are included in order for the overall structure of the licence provisions to be visible. The details of the reliability incentive scheme and Innovation Funding Initiative make reference to regulated revenues at various points. It will be necessary to amend this term in light of the revised duration and form of the price control to apply from April 2007.

1.2. The drafting relating to the reliability incentive scheme contains only one major change from what exists today. This reflects our proposal to introduce a penalties only scheme. In the licence of NGET we also propose removing some redundant provisions in paragraph 1.

1.3. With regard to the drafting on the SF6 incentive, we use terms for actual and target leakage. Our discussions with the transmission licensees have made it apparent that there needs to be a clear methodology associated with these terms. We are in the process of establishing appropriate provisions for leakage and monitoring arrangements. We will consult on our findings as part of the December final proposals document.

1.4. The innovation funding incentive, which is anticipated to apply in an almost identical format across the three electricity licensees and the gas transmission licensee, may need to have additional terms and definitions added, to reflect the development of the RIGs and the Good Practice Guide. We are currently in the process of developing the RIGs, and are liaising with the industry to develop the Good Practice Guide.

Amended Transmission Network Reliability Incentive - proposed transmission licence drafting: Special Condition AA5F

1. For the purpose of paragraph 1 of Special Condition AA5A Part 1, the term RI_t shall be derived from the following formula:

$$RI_t = P_{t-1} \cdot RAF_y$$

where:

RAF_y is the adjustment factor based on the licensee's performance against the transmission network reliability incentive during incentive period y , and is derived from the following formulae:

If $RIP_y < RILT_y$:

$$RAF_y = 0$$

If $RIP_y > RIUT_y$:

$$RAF_y = \max \left(RIDPA_y, RIDPA_y \left[\frac{RIP_y - RIUT_y}{RICOL_y - RIUT_y} \right] \right)$$

Otherwise:

$$RAF_y = 0$$

where:

$RILT_y$ is the lower incentivised loss of supply volume target in respect of incentive period y , which has the value as specified in the following table:

Incentive Period y	2007/08	2008/09	2009/10	2010/11	2011/12
$RILT_y$	[]	[]	[]	[]	[]

$RIUT_y$ is the upper incentivised loss of supply volume target in respect of incentive period y , which has the value as specified in the following table:

Incentive Period y	2007/08	2008/09	2009/10	2010/11	2011/12
RIUT_y	[]	[]	[]	[]	[]

$RIDPA_y$ is the maximum downside percentage adjustment in respect of incentive period y, which has the value as specified in the following table:

Incentive Period y	2007/08	2008/09	2009/10	2010/11	2011/12
RIDPA_y	[]	[]	[]	[]	[]

$RICOL_y$ is the incentivised loss of supply collar in respect of incentive period y which has the value as specified in the following table:

Incentive Period y	2007/08	2008/09	2009/10	2010/11	2011/12
RICOL_y	[]	[]	[]	[]	[]

RIP_y is the sum of the volumes of unsupplied energy in all incentivised loss of supply events in incentive period y.

$\max(A,B)$ means the value equal to the greater of A and B.

- For the purposes of this Special Condition "incentivised loss of supply event" shall mean any event on the licensee's transmission system that causes electricity not to be supplied to a customer subject to the following exclusions:

- (a) any such event that causes electricity to not be supplied to 3 or less directly connected parties;
 - (b) any unsupplied energy resulting from a shortage of available generation;
 - (c) any unsupplied energy resulting from a de-energisation or disconnection of a user's equipment under an event of default as defined in the CUSC;
 - (d) any unsupplied energy resulting from a user's request for disconnection in accordance with in the Grid Code; and
 - (e) any unsupplied energy resulting from emergency de-energisation by a user as defined in the CUSC; and
3. For the purpose of paragraph 2 a "directly connected party" is any party with a direct connection to the licensee's transmission system with the exception of any connection to a distribution system.
4. Where:
- (a) the licensee considers that any event on the licensee's transmission system that causes electricity not to be supplied to a customer has been wholly or partially caused by an exceptional event;
 - (b) the licensee has notified the Authority of such event within 14 days of its occurrence;
 - (c) the licensee has provided details of the volume of unsupplied energy that the licensee considers resulted from the exceptional event and such further information, if any, as the Authority may require in relation to such an exceptional event; and

- (d) the Authority is satisfied that the event notified to it under sub-paragraph (b) is an exceptional event

the Authority may, by notice to the licensee, direct that, for the purpose of calculating the volume of unsupplied energy for the relevant incentivised loss of supply event the constituent data relevant to that event shall be adjusted as specified in that direction.

5. For the purpose of paragraph ,4 the adjustment directed by the Authority shall be based on the extent to which the Authority is satisfied that the licensee had taken reasonable steps to prevent the event having the effect of interrupting supply and to mitigate its effect (both in anticipation and subsequently).
6. A direction under paragraph 8 shall not have effect unless, before it is made, the Authority has given notice to the licensee:
- a) setting out the terms of the proposed direction;
 - b) stating the reasons why it proposes to issue the direction; and
 - c) specifying the period (not being less than 14 days from the date of the notice) within which the licensee may make representations or objections

and the Authority has considered such representations or objections and given reasons for its decision.

7. For the purpose of paragraph 4, an "exceptional event" means an event or circumstance that is beyond the reasonable control of the licensee and which results in or causes electricity not to be supplied to a customer and includes an act of the public enemy, war declared or undeclared, threat of war, terrorist act, revolution, riot, insurrection, civil commotion, public demonstration, sabotage, act of vandalism, fire (not related to weather), any severe weather event resulting in more than [] faults being recorded by the

licensee on the licensee's transmission system in any 24 hour period, governmental restraint, Act of Parliament, other legislation, bye law or directive (not being any order, regulation or direction under section 32, 33, 34 and 35 of the Electricity Act 1989) provided that lack of funds shall not be interpreted as a cause beyond the reasonable control of the licensee.

SF₆ Incentives - Special condition []: adjustment to restriction of transmission charges due to SF₆ incentive

1. This condition defines the value of SF_t, which is a term that forms part of the licensee's revenue restriction.
2. The purpose of this condition is to provide for adjustments to allowed revenue to reflect performance of the licensee in relation to its Sulphur Hexafluoride (SF₆) incentive scheme.
3. For the purposes of paragraph [] of special condition [], SF_t is derived for the relevant year t from the formula:

Where:

If $ALK_t < TLK_t$:

$$SF_t = [£]$$

If $ALK_t \geq TLK_t$:

$$SF_t = [£]$$

Where:

ALK_t is the actual leakage rate of SF₆ gas as a percentage of inventory of SF₆ gas as reported by the licensee pursuant to [standard condition B16]

TLK_t is the target leakage rate of SF₆ gas as a percentage of inventory of SF₆ and shall take the values in the table below:

	2007/08	2008/09	2009/10	2010/11	2011/12
TLK_t	[]	[]	[]	[]	[]

Innovation Funding Incentive - Special condition [] – Calculation of charge restriction adjustments arising from the innovation funding incentive scheme

1. The purpose of this condition is to provide for adjustments to allowed revenue to reflect performance of the licensee in relation to its investment in innovation under the Innovation Funding Incentive (IFI) scheme
2. For the purposes of paragraph [xx] of special condition [xx], IFI_t is derived for the relevant year t from the formula:

$$IFI_t = ptri_t * (\min(IFIE_t, (([] * PR_t) + KIFI_t)))$$

Where:

$IFIE_t$ means the eligible expenditure for the relevant year t as reported in the IFI annual report for that year

PR_t means the regulated transmission revenue in year t as defined in special condition AA5A

ptr_t is the pass-through factor applicable for the relevant year t as specified below

$KIFI_t$ is the carry forward in relation to the incentive scheme as set out in the IFI annual report for relevant year t-1, and is calculated from the following formula:

$$KIFI_t = \begin{cases} [] * [] * PR_{t-1}, & \text{if } IFIE_{t-1} \leq ([] * [] * PR_{t-1}), \\ ([] * PR_{t-1}) - IFIE_{t-1}, & \text{if } IFIE_{t-1} > ([] * [] * PR_{t-1}) \text{ and } IFIE_{t-1} \leq ([] * PR_{t-1}), \\ 0, & \text{if } IFIE_{t-1} > ([] * PR_{t-1}); \end{cases}$$

Where, for the year commencing 1 April 2007, $KIFI_t$, shall be zero

- For the purposes of the incentive scheme, the eligible IFI internal expenditure that qualifies as eligible IFI expenditure in the relevant year t ($IFIIE_t$) shall be the amount determined in the following formula:

$$IFIIE_t \leq z * IFIE_t$$

Where:

$IFIIE_t$ is the eligible IFI internal expenditure that qualifies as eligible IFI expenditure for the relevant year t

z shall take the value, except insofar as the Authority consents otherwise, and subject to any conditions the Authority may at its discretion attach to such consent, of [].

- For the purposes of this condition:

“eligible IFI internal expenditure”	means the amount of eligible IFI expenditure spent or accrued on the internal resources of the licensee; and
“eligible IFI expenditure”	means the amount of expenditure spent or accrued by the licensee in respect of eligible IFI projects.

Appendix 8 – Draft legal text - NGET SO conditions

Part 2 (ii): Balancing services activity revenue restriction on internal costs

13. The licensee shall use its best endeavours to ensure that in the relevant year t the revenue derived by the licensee from the balancing services activity associated with internal costs (being all balancing services activity revenue in relevant year t with the exception of any revenue in relevant year t accounted for under special condition AA5A Part 2(i) paragraph 5) shall not exceed an amount calculated in accordance with the following formula:

$$BXint_t = (SOint_t [NPI])$$

where:

$BXint_t$ means the balancing services activity revenue associated with internal costs in the relevant year other than any revenue in relevant year t accounted for under paragraph 5 of Part 2(i) special condition AA5A and is derived from the following components:

$SOint_t$ which is the aggregate of all internal costs associated with the balancing services activity in respect of relevant year t , calculated in accordance with paragraph 14 of this special condition;

NPI means the NETA Profiling Index in respect of relevant year t calculated in accordance with paragraph B10 of Part B of Schedule A; and

14. For the purpose of paragraph 13, the term $SOint_t$ shall be derived from the following formula:

$$SOint_t = CSOC_t + IncPayInt_t + NSOC_t + IAT_t + T_t + P_t + ON_t + IONT_t$$

where:

$CSOC_t$ means the aggregate of the incentivised internal costs associated with the balancing services activity in respect of relevant year t calculated in accordance with paragraph 15 of this condition.

$IncPayInt_t$ means the incentive payment associated with the internal costs of undertaking the balancing services activity in respect of relevant year t, calculated in accordance with paragraph 16 of this special condition.

$NSOC_t$ has the value set against relevant year t in the table in paragraph B8 in Part B of Schedule A and represents the allowed revenue in respect of the non-incentivised internal costs of the licensee in operating the licensee's transmission system during relevant year t, including costs in preparing for the introduction of the New Electricity Trading Arrangements but excluding non-domestic rates incurred by the licensee in operating the licensee's transmission supply during relevant year t.

IAT_t means, in respect of each relevant year t, the amount of any allowed income adjustment given by paragraph 19(b) below.

T_t means the tax allowance in respect of relevant year t as set out in the following table;

	<u>Relevant year</u>				
<u>Variable</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>
T_t (£,million)					

P_t means the pension cost allowance in respect of relevant year t as set out in the following table;

	<u>Relevant year</u>				
<u>Variable</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>
P_t (£,million)					

ON_t has the value £1,000,000 for the relevant year t and represents an allowance for payments by the licensee in respect of outage changes.

$IONT_t$ means, in respect of each relevant year t, the amount of any allowed income adjustments given by paragraph 25(b).

15. Determination of incentivised internal costs

For the purposes of paragraph 14, the term $CSOC_t$ shall be derived from the following formula:

$$CSOC_t = CSOOC_t + CSOCEC_t$$

where:

CSOOC_t means the aggregate of the incentivised internal operating costs associated with the balancing services activity in respect of relevant year t.

CSOCEC_t means the aggregate of the incentivised internal capital expenditure associated with the balancing services activity in respect of relevant year t and calculated in accordance with part (a) of this paragraph.

- a. For the purposes of this paragraph 15 the term CSOCEC_t shall be derived from the following formula

$$CSOCEC_t = CSOD_t + CSOR_t$$

where::

CSOD_t means the depreciation on the SO regulatory asset base in respect of relevant year t and is

calculated as $\frac{\text{the regulatory asset base at 1 April in relevant year t}}{7}$; and

CSOR_t means the return on the [average] SO regulatory asset base in respect of relevant year t and is calculated as []% of the [SO]regulatory asset base [in respect of year_t][at rate of []%]; and

16. Determination of incentive payments on internal costs

For the purposes of paragraph 14, the term IncPayInt_t shall be derived from the following formula:

$$\text{IncPayInt}_t = \left(\left[(\text{ISF}_t(\text{IMOT}_t - \text{CSOOC}_t)) + (\text{ISF}_t(\text{IMCET}_t - \text{CSOCEC}_t)) \right] + \frac{1}{\text{NPI}_M} \left[\sum (1 - \text{CSF}_{Mt})(\text{CP}_{Mt} - \text{OS}_{Mt}) \right] \right)$$

where:

ISF_t which is a balancing services activity sharing factor in respect of relevant year t, and is calculated in accordance with part (a) of this paragraph; and

$IMOT_t$	which is a target for the incentivised internal operating costs associated with the balancing services activity in respect of relevant year t and has the value specified for relevant year t in the table in paragraph B5 in Part B of Schedule A.
$IMCET_t$	which is a target for the incentivised internal capital expenditure associated with the balancing services activity in respect of relevant year t and has the value specified for relevant year t in the table in paragraph B6 in Part B of Schedule A.
$CSOOC_t$	has the meaning given in paragraph 15
$CSOCEC_t$	has the meaning given in paragraph 15
CSF_{Mt}	is the Contingency Provisions (as defined in the BSC from time to time) sharing factor in respect of each month M of relevant period t and has the value determined in accordance with paragraph B11 in Part B of Schedule A.
CP_{Mt}	is the sum of the Ad-Hoc Trading Charges (as defined in the BSC from time to time) payable by the licensee in respect of the Contingency Provisions (as defined in the BSC from time to time) in month M of the relevant period t.
OS_{Mt}	which is the Contingency Provisions (as defined in the BSC from time to time) offset in respect of each month M of relevant period t, has the value determined in accordance with paragraph B12 in Part B of Schedule A .
\sum_M	means the summation over all months M in relevant period t.
NPI	shall have the meaning given in paragraph 13 of Part 2(ii) of this special condition.

(a) for the purposes of this paragraph 16 ISF_t shall be determined as follows in respect of relevant year t_t

if $IMOT_t > CSOOC_t$ then $ISF_t = IUSF_t$ otherwise $ISF_t = IDSF_t$; and

if $IMCET_t > CSCEC_t$ then $ISF_t = IUSF_t$ otherwise $ISF_t = IDSF_t$;

where:

$IUSF_t$ which is a balancing services activity upside sharing factor in respect of relevant year t and has the value specified in paragraph B7 in Part B of Schedule A.

$IDSF_t$ which is a balancing services activity downside sharing factor in respect of relevant year t and has the value specified in paragraph B7 in Part B of Schedule A.

$IMOT_t$ has the meaning given in this paragraph 16.

$IMCET_t$ has the meaning given in this paragraph 16.

$CSOOC_t$ has the meaning given in paragraph 15.

$CSOCEC_t$ has the meaning given in paragraph 15.

17. Income adjusting events under the balancing services activity revenue restriction on internal costs

(a) An income adjusting event in relevant year t may arise from any of the following:

- i) an event or circumstance constituting force majeure under the STC;
- ii) an event or circumstance resulting from an amendment to the STC not allowed for in setting the allowed revenues of the licensee for the relevant year t ; and

iii) an event or circumstance other than listed above which is, in the opinion of the Authority, an income adjusting event and approved by it as such in accordance with paragraph 18 of this licence condition

where the event or circumstance has, for relevant year t , increased or decreased the value of $CSOC_t$ by more than £1,000,000 (the "STC threshold amount").

(b) For the purpose of relevant year t commencing on 1 April 2007 and ending on 31 March 2012 events or circumstances arising directly from the implementation or otherwise of the following proposed amendments (both the original and any alternative) listed in table 1 below shall not qualify as an income adjusting event for the purpose of paragraph 17(a) above:

Table 1:

Amendment No.	Amendment Title

18. Notice of proposed income adjusting event

- (a) Where the licensee considers, and can provide supporting evidence that, in respect of relevant year t , there have been costs and/or expenses that have been incurred or saved by an income adjusting event, then the licensee shall give notice of this event to the Authority.
- (b) A notice provided to the Authority under paragraph 18(a) shall give particulars of:
- (i) the event to which the notice relates and the reason(s) why the licensee considers this event to be an income adjusting event;

- (ii) the amount of any change in costs and/or expenses that can be demonstrated by the licensee to have been caused or saved by the event and how the amount of these costs and/or expenses has been calculated;
 - (iii) the amount of any allowed income adjustment proposed as a consequence of that event and how this allowed income adjustment has been calculated; and
 - (iv) any other analysis or information which the licensee considers to be sufficient to enable the Authority and the relevant parties referred to in subparagraph 19(a) to fully assess the event to which the notice relates.
- (c) If the Authority considers that the analysis or information provided in sub-paragraphs 18(b)(i) to 18(b)(iv) above is insufficient to enable both the Authority and the relevant parties referred to in subparagraph 19(a) to assess whether an income adjusting event has occurred and/or the amount of any allowed income adjustment that should be approved, the Authority can request that the supporting evidence be supplemented with additional information that it considers appropriate.
- (d) A notice of an income adjusting event shall be given as soon as is reasonably practicable after the occurrence of the income adjusting event, and, in any event, not later than three months after the end of the relevant year in which it occurs.
- (e) The Authority will make public, excluding any confidential information, any notice of an income adjusting event following its receipt.
- (f) Any notice submitted to the Authority under paragraph 17(a) above should clearly identify whether any of the information contained in the notice is of a confidential nature. The Authority shall make the final determination as to confidentiality having regard to:

- (i) the need to exclude from disclosure, so far as is reasonably practicable, information whose disclosure the Authority considers would or might seriously prejudicially affect the interests of a person to which it relates; and
- (ii) the extent to which the disclosure of the information mentioned in sub-paragraph 18(f)(i) is necessary for the purposes of enabling the relevant parties to fully assess the event to which the notice relates.

19. The Authority's determination

- (a) The Authority shall determine (after consultation with the licensee and such other persons as it considers desirable):
 - (i) whether any or all of the costs and/or expenses given in a notice pursuant to paragraph 18(a) were caused or saved by an income adjusting event;
 - (ii) whether the event or circumstance has increased or decreased the value of $CSOC_t$ by more than the STC threshold amount;
 - (iii) if so, whether the amount of the proposed income adjustment ensures that the financial position and performance of the licensee are, insofar as is reasonably practicable, the same as if that income adjusting event had not taken place, and if not, what allowed income adjustment would secure that effect; and
 - (iv) the periods, if any, over which the amounts should apply.
- (b) In relation to the relevant year t , the allowed income adjustment (IAT_t) shall be:
 - (i) the value determined by the Authority under paragraph 19(a) above; or

- (ii) if the Authority has not made a determination under paragraph 19(a) above within three months of the date on which notice of an income adjusting event was provided to the Authority, the amount of the allowed income adjustment proposed as a consequence of the event in the notice given to the Authority under sub-paragraph 18(b)(iii); or
 - (iii) in all other cases zero, including situations where the Authority has not made a determination under paragraph 19(a) above within three months of the date on which notice of an income adjusting event was provided to the Authority and the Authority has, before the end of that three month period, informed the licensee that the Authority considers that the analysis or information provided in accordance with paragraphs 18(b) and/or 18(c) is insufficient to enable the Authority to assess whether an income adjusting event has occurred and/or the amount of any allowed income adjustment.
- (c) The Authority's decision in relation to any notice given under paragraph 18(a) shall be in writing, shall be copied to the licensee and shall be in the public domain.
- (d) The Authority may revoke an approval of an income adjusting event and allowed income adjustment with the consent of the licensee, following consultation with the licensee and relevant parties. Revocation of any income adjusting event and allowed income adjustment shall be in writing, shall be copied to the licensee and shall be in the public domain.

20. [Not used]

Appendix 9 – Proposed new Scottish licence conditions

1.1. The following sets out our current views on a number of the amendments and additions to SHETL and SPTL’s special licence conditions which we consider necessary to reflect the position set out in the September updated proposals document. The licence drafting we have provided relates to amendments to the existing reliability incentive scheme, and additions necessary to introduce an SF6 incentive and the Innovation Funding Incentive. Throughout the drafting, square brackets denote numbers or references that are yet to be finalised, and are included in order for the overall structure of the licence provisions to be visible. These figures, for both SHETL and SPTL, will be consulted on further in our December document.

1.2. Our proposals on network reliability incentives reflect our proposal to introduce a penalties only scheme. With regard to the drafting on the SF6 incentive, we use terms for actual and target leakage. Our discussions with the transmission licensees have made it apparent that there needs to be a clear methodology associated with these terms. We are in the process of establishing appropriate provisions for leakage and monitoring arrangements. We will consult on our findings as part of the December final proposals document.

1.3. The innovation funding incentive, which is anticipated to apply in an almost identical format across the three electricity licensees and the gas transmission licensee, may need to have additional terms and definitions added, to reflect the development of the RIGs and the Good Practice Guide. We are currently in the process of developing the RIGs, and are liaising with the industry to develop the Good Practice Guide.

Amended Transmission Network Reliability Incentive: Special Condition Q - Adjustment to Restriction of Transmission Charges due to Transmission Network Reliability Incentive

1. For the purpose of paragraph 1 of Special Condition J, the term RI_t shall be derived from the following formula:

$$RI_t = R_t.RAF_y$$

where:

R_t shall be calculated in accordance with the formula specified in paragraph 1 of Special Condition J.

RAF_y is the revenue adjustment factor based on the licensee’s performance against the transmission network reliability incentive during incentive period y , and is derived from the following formula:

If $RIP_y < RILT_y$:

$$RAF_y = 0$$

If $RIP_y > RIUT_y$:

$$RAF_y = \max \left(RIDPA_y, RIDPA_y \left[\frac{RIP_y - RIUT_y}{RICOL_y - RIUT_y} \right] \right)$$

Otherwise:

$$RAF_y = 0$$

where:

$RILT_y$ is the lower incentivised loss of supply event target in respect of incentive period y , which is the number of events specified in the following table:

Incentive Period y	2007/08	2008/09	2009/10	2010/11	2011/12
RILT_y	[]	[]	[]	[]	[]

$RIUT_y$ is the upper incentivised loss of supply event target in respect of incentive period y , which is the number of events specified in the following table:

Incentive Period y	2007/08	2008/09	2009/10	2010/11	2011/12
RIUT_y	[]	[]	[]	[]	[]

$RIDPA_y$ is the maximum downside percentage adjustment in respect of incentive period y , which has the value as specified in the following table:

Incentive Period y	2007/08	2008/09	2009/10	2010/11	2011/12
RIDPA_y	[]	[]	[]	[]	[]

$RICOL_y$ is the incentivised loss of supply collar in respect of incentive period y which is the number of events specified in the following table:

Incentive Period y	2007/08	2008/09	2009/10	2010/11	2011/12
RICOL_y	[]	[]	[]	[]	[]

RIP_y is the number of incentivised loss of supply events in incentive period y .

$\max(A,B)$ means the value equal to the greater of A and B.

2. For the purposes of this Special Condition, "incentivised loss of supply event" shall mean any event on the licensee's transmission system that causes electricity not to be supplied to a customer subject to the following exclusions:
 - (a) any such event that causes electricity to not be supplied to 3 or less directly connected parties;
 - (b) any unsupplied energy resulting from a shortage of available generation;
 - (c) any unsupplied energy resulting from a user's request for disconnection in accordance with the Grid Code;
 - (d) any unsupplied energy resulting from emergency de-energisation of part of the licensee's transmission system, either as a consequence of a user's request for emergency de-energisation of its equipment or the user carrying out an emergency de-energisation of its equipment;
 - (e) any unsupplied energy resulting from a planned outage as defined in the Grid Code;
 - (f) any unsupplied energy resulting from a de-energisation or disconnection of a user's equipment necessary to ensure

compliance with an instruction by the system operator to the licensee pursuant to the STC; and

- (g) any unsupplied energy resulting from an emergency de-energisation or disconnection of a user's equipment necessary to ensure compliance with the Electricity Safety, Quality and Continuity Regulations 2002, as amended from time to time, or to otherwise ensure public safety.
3. For the purpose of paragraph 2, a "directly connected party" is any party with a direct connection to the licensee's transmission system with the exception of any connection to a distribution system.
4. Where:
- (a) the licensee considers that any event on the licensee's transmission system that causes electricity not to be supplied to a customer has been wholly or partially caused by an exceptional event;
 - (b) the licensee has notified the Authority of such event within 14 days of its occurrence;
 - (c) the licensee has provided details of the exceptional event and such further information, if any, as the Authority may require in relation to such an exceptional event; and
 - (d) the Authority is satisfied that the event notified to it under subparagraph (b) is an exceptional event,

the Authority may, by notice to the licensee, direct that the number of incentivised loss of supply events in incentive period y shall be adjusted as specified in that direction.

5. For the purpose of paragraph 4, the adjustment directed by the Authority shall be based on the extent to which the Authority is satisfied

that the licensee had taken reasonable steps to prevent the event having the effect of interrupting supply and to mitigate its effect (both in anticipation and subsequently).

6. A direction under paragraph 4 shall not have effect unless, before it is made, the Authority has given notice to the licensee:
 - (a) setting out the terms of the proposed direction;
 - (b) stating the reasons why it proposes to issue the direction; and
 - (c) specifying the period (not being less than 14 days from the date of the notice) within which the licensee may make representations or objections

and the Authority has considered such representations or objections and given reasons for its decision.

7. For the purpose of paragraph 4, an "exceptional event" means an event or circumstance that is beyond the reasonable control of the licensee and which results in or causes electricity not to be supplied to a customer and includes an act of the public enemy, war declared or undeclared, threat of war, terrorist act, revolution, riot, insurrection, civil commotion, public demonstration, sabotage, act of vandalism, fire (not related to weather), any severe weather event resulting in more than [] faults being recorded by the licensee on the licensee's transmission system in any 24 hour period, governmental restraint, Act of Parliament, other legislation, bye law or directive (not being any order, regulation or direction under section 32, 33, 34 and 35 of the Electricity Act 1989) provided that lack of funds shall not be interpreted as a cause beyond the reasonable control of the licensee.

SF₆ Incentives: Special condition [] - adjustment to restriction of transmission charges due to SF₆ incentive

1. This condition defines the value of SF_t, which is a term that forms part of the licensee's revenue restriction.
2. The purpose of this condition is to provide for adjustments to allowed revenue to reflect performance of the licensee in relation to its Sulphur Hexafluoride (SF₆) incentive scheme.
3. For the purposes of paragraph [] of special condition [], SF_t is derived for the relevant year t from the formula:

Where:

If $ALK_t < TLK_t$:

$$SF_t = [£]$$

If $ALK_t \geq TLK_t$:

$$SF_t = [£]$$

Where:

ALK_t is the actual leakage rate of SF₆ gas as a percentage of inventory of SF₆ gas as reported by the licensee pursuant to [standard condition B16]

TLK_t is the target leakage rate of SF₆ gas as a percentage of inventory of SF₆ and shall take the values in the table below:

	2007/08	2008/09	2009/10	2010/11	2011/12
TLK_t	[]	[]	[]	[]	[]

Innovation Funding Incentive - Special condition [] – Calculation of charge restriction adjustments arising from the innovation funding incentive scheme

1. The purpose of this condition is to provide for adjustments to allowed revenue to reflect performance of the licensee in relation to its investment in innovation under the Innovation Funding Incentive (IFI) scheme
2. For the purposes of paragraph [] of special condition [], IFI_t is derived for the relevant year t from the formula:

$$IFI_t = ptri_t * (\min(IFIE_t, (([] * PR_t) + KIFI_t)))$$

Where:

$IFIE_t$ means the eligible expenditure for the relevant year t as reported in the IFI annual report for that year

PR_t means the regulated transmission revenue in year t as defined in special condition AA5A

$ptri_t$ is the pass-through factor applicable for the relevant year t as specified below

$KIFI_t$ is the carry forward in relation to the incentive scheme as set out in the IFI annual report for relevant year t-1, and is calculated from the following formula:

$$KIFI_t = \begin{cases} []*[]*PR_{t-1}, & \text{if } IFIE_{t-1} \leq ([]*[]*PR_{t-1}), \\ ([]*PR_{t-1}) - IFIE_{t-1}, & \text{if } IFIE_{t-1} > ([]*[]*PR_{t-1}) \text{ and } IFIE_{t-1} \leq ([]*PR_{t-1}), \\ 0, & \text{if } IFIE_{t-1} > ([]*PR_{t-1}); \end{cases}$$

Where, for the year commencing 1 April 2007, $KIFI_t$, shall be zero

- For the purposes of the incentive scheme, the eligible IFI internal expenditure that qualifies as eligible IFI expenditure in the relevant year t ($IFIIE_t$) shall be the amount determined in the following formula:

$$IFIIE_t \leq z * IFIE_t$$

Where:

$IFIIE_t$ is the eligible IFI internal expenditure that qualifies as eligible IFI expenditure for the relevant year t

z shall take the value, except insofar as the Authority consents otherwise, and subject to any conditions the Authority may at its discretion attach to such consent, of [].

- For the purposes of this condition:

“eligible IFI internal expenditure”	means the amount of eligible IFI expenditure spent or accrued on the internal resources of the licensee; and
“eligible IFI expenditure”	means the amount of expenditure spent or accrued by the licensee in respect of eligible IFI projects.

Appendix 10 – Draft legal text - Amended Standard Conditions B

1.1. Appendix 10 provides details of our proposed amendments to several of the existing standard conditions with section B of the transmission licences. The table below shows the conditions we currently propose to change.

No	Licence Condition	Description
1	B1	Regulatory Accounts
2	B2	Change of Financial Year
3	B6	Restriction on activity and financial ring fencing
4	B7	Availability of Resources
5	B9	Indebtedness
6	B10	Credit Rating
7	B15	Price Review Information
8	B16	Revenue Reporting

1.2. Due to the size of the licence conditions, we have placed versions on the Ofgem website. These can be accessed via the TPCR area of work section or by clicking on the + symbol next to this document.