

## Transmission price control review: Draft licence conditions (electricity) - second informal consultation

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**Target audience:** This document will be of interest to network owners and operators, generators, shippers, suppliers, customers and other interested parties.

### Overview:

In December 2006 we published our final proposals following our review of the price controls of the four transmission companies in electricity and gas. Our proposals have now been accepted in principle by the companies and will take effect on 1 April 2007. To give effect to our proposals we need to amend the licences of the four companies. Throughout the process we have engaged the licensees to develop licence drafting that accurately reflects our final proposals, and serves to enhance the clarity and robustness of the existing licence provisions. We expect to continue to utilise bilateral discussions from now until the publication of our formal notices to further develop the licence drafting. Please note that the drafting will be subject to further review following our bilateral meetings with the licensees, and is therefore subject to change. Such changes are anticipated to include further housekeeping amendments. Shortly following publication of this document, we will be publishing a similar document regarding proposed changes to National Grid Gas' NTS licence.

This document is our second informal consultation on the detailed changes we propose to make to the licences of the three electricity transmission companies. Following this consultation we intend to publish our formal section 11 and section 11A notices to propose the necessary licence changes in February.

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## Context

Over the past two years we have been in the process of reviewing the price controls of the four transmission companies we regulate. The price controls determine how much revenue each of the companies is permitted to recover, generally over a five year period. This is an important process to ensure we continue to regulate network monopolies effectively by implementing provisions so that the companies can finance their activities and by providing the companies with the right set of financial incentives to act in the interests of consumers.

This process has now concluded with the publication of our final proposals in December 2006. In order to give effect to our proposals, however, we must modify the transmission licences held by each of the companies. The licences are the means by which the companies are bound to the terms of our new price controls. It is important therefore that the licences reflect our policy as set out in the final proposals document in an accurate and unambiguous manner. The process of consultation on the draft licence conditions is designed to ensure that these aims are met.

## Associated Documents

- TPCR 2007-2012 Draft licence conditions - NGET Transmission Licence Special Conditions - second informal consultation - Appendix 6, January 2007 (Ref No. 10a/07)
- TPCR 2007-2012 Draft licence conditions (electricity) - second informal consultation - Appendix 7, January 2007 (Ref No. 10b/07)
- TPCR 2007-2012 Draft licence conditions (electricity) - second informal consultation - Appendix 8, January 2007 (Ref No. 10c/07)
- TPCR 2007-2012 Draft licence conditions (electricity) - second informal consultation - Appendix 9, January 2007 (Ref No. 10d/07)
- National Grid Electricity Transmission and National Grid Gas System Operator Incentives from 1 April 2007, Initial Proposals, December 2006 (Ref No. 208/06)
- TPCR 2007-2012 Final Proposals, Decision Document, December 2006 (Ref No. 206/06)
- TPCR 2007-2012 Final Proposals - Appendices, December 2006 (Ref No. 206/06b)
- TPCR 2007-2012 Draft Licence Modifications, November 2006 (Ref No. 197/06)
- TPCR 2007-2012 Draft Licence Modifications - Appendices, November 2006 (Ref No. 197/06a)
- 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)
- Access Reform in Electricity Transmission: Working group report and next steps, May 2006 (Ref No. 83/06a)

- A framework for considering reforms to how generators gain access to the GB electricity transmission system: A report by the Access Reform Options Development Group April 2006, May 2006 (Ref No. 83/06b)
- 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 Capital Expenditure Projections 2007-2012 (open letter), 1 February 2006 (Ref No. 21/06)
- TPCR Second Consultation, December 2005 (Ref No. 277/05)
- TPCR Initial Consultation, July 2005 (Ref No. 172/05)

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## Summary

This document sets out the changes we are proposing to the licences of the electricity transmission companies to give effect to the findings of our transmission price control review. It is necessary to amend some existing conditions, delete others and introduce new conditions. In addition, we will also take the opportunity to rationalise the licences, including making various housekeeping changes and amendments to enhance the clarity of the provisions of the licensees' obligations. The three electricity transmission companies are:

- National Grid Electricity Transmission Plc (NGET)
- Scottish Power Transmission Limited (SPTL)
- Scottish Hydro-Electric Transmission Limited (SHETL)

We published our final proposals for the transmission price control review in December 2006. All three companies have now announced their acceptance, in principle, of our proposals.

The licences are legal documents and, among other things, the vehicle through which the companies are bound to the terms of our proposed new price controls. It is important that the detail of our proposals is implemented clearly, accurately and unambiguously. To meet this objective we have chosen to consult on the changes we are proposing before we formally propose their implementation. This document is the second and final such informal consultation prior to the formal statutory consultation in February 2007, which, if accepted, will give effect in the licences to our final proposals. As mentioned earlier, our formal proposals will be issued in accordance with the processes detailed in sections 11 and 11A of the Electricity Act 1989.

This document sets out the proposed changes for each of the companies in turn. The main document summarises the changes, highlights any particular points to note and provides references to the relevant appendices where the draft legal text is set out. It also sets out our proposed amendments and additions to the standard licence conditions.

Please note that the drafting will be subject to further review following our bilateral meetings with the licensees, and is therefore subject to change.

We will shortly be publishing a consultation in relation to proposed changes to National Grid Gas' NTS licence.



## 1. NGET

### Chapter Summary

This chapter describes the changes we are proposing to make to the licence of NGET to give effect to our final proposals following our review of NGET's price control. It also describes the process we are adopting to align these changes with the process of implementing analogous changes to the NGET's System Operator (SO) revenue restriction.

### Questions

**Question 1.1:** Do you have any comments on the proposed licence drafting?

## Introduction

1.1. NGET's licence obligations are derived from a combination of standard conditions for transmission licensees and special conditions specific to NGET. The bulk of the price control arrangements are contained within the special conditions of NGET's licence. The amendments to give effect to our TPCR proposals will affect the special conditions of NGET's licence.

1.2. There are two broad classes of change we are proposing to NGET's licence, namely changes required to:

- Re-set the base (non-contingent) revenue allowances and main price control formula; and
- Set the rules for calculating a number of potential adjustments to revenues associated with logging up, revenue drivers and incentive mechanisms.

1.3. These two areas are discussed in turn with cross-references to the relevant appendices setting out the associated draft legal text.

1.4. We are also proposing to transfer some obligations in respect of regulatory reporting from current special conditions to new standard conditions, which will consolidate periodic regulatory reporting obligations in a single place in the licence - supported by a set of Regulatory Instructions and Guidance (RIGs). This is discussed in more detail in chapter 4.

1.5. We have proposed the introduction of network output measures via a new standard condition B17. This is the first time that the provisions of this condition will have been consulted on, as they have been developed following our final proposals for the transmission network reliability incentive. As we have previously set out in our consultation documents, we believe it is important for the industry and ourselves

to improve the measurement of overall network condition, underlying network risks and the impact on system performance, given the substantial upturn in costs to replace and refurbish assets. We consider that our proposed licence drafting will help deliver such improvements.

1.6. We are also continuing to work on strengthening the regulatory reporting requirements, particularly in relation to monitoring compliance against licence requirements. At present, we envisage that more work will need to be carried out in conjunction with the licensees prior to February's statutory consultation.

1.7. The current transmission licence conditions include detailed provisions in relation to NGET's System Operator (SO) role. During the course of this consultation process, we have formed the view that it would be beneficial to separate out the Transmission Owner (TO) provisions from the SO provisions in the transmission licence. Our rationale for this view is that there continues to be ongoing developments to the SO incentive scheme, and the licence provisions that implement any proposals in this area.

1.8. As such, we consider it is appropriate to remove the linkage between the two areas of the transmission licence in certain areas. The aim of adopting this approach is that it will enable both sets of proposals for the TOs' price control and the SO's external incentive scheme to be implemented independently of each other, both now and in the future, removing any interdependency between the two mechanisms, and preventing conflict with the implementation of either scheme. Our final proposals for NGET's SO external incentive scheme will be published in February and both sets of changes will be scheduled for implementation on 1 April 2007.

1.9. We have also taken the opportunity to make a few minor housekeeping changes such as removing obsolete provisions that no longer apply from 1 April 2007, and relocating various provisions into more intuitive locations.

## **Baseline revenue and main formula**

1.10. The main formula that sets the maximum revenue that NGET is permitted to recover in respect of its Transmission Owner activities will be set out in an amended Special Condition D2. Definitions of terms used in section D will be contained in a new Special Condition D1.

1.11. The structure of D2 will be as follows:

- Context - the condition obliges NGET to use its best endeavours to avoid recovering more from TO activities than the revenue total calculated in accordance with the main formula.
- Main formula: comprises a core element of price control based revenue allowance (PR) together with excluded service income, plus a number of terms (linked to incentive and adjustment mechanisms - TIRG, PT, IP and CxIncRA)

which can potentially alter the core element of revenue. Absent these adjustments, the core revenue allowance increases in line with inflation, accounting for an "X" term, each year. The main formula also provides for differences between actual revenues and allowed revenues in any given year to be carried forward to the next year (K).

- The derivations of each of the incentive and adjustment mechanisms are set out in other special conditions (discussed below). The main formula consolidates these individual adjustments and nets them off (or adds them to) the core revenues that would otherwise be recoverable.

1.12. We are also proposing to amend the existing provisions in NGET's Special Condition AA5E, in order to separate out the drafting that relates to disapplication requests in the transmission network revenue restriction and the balancing services activity revenue restriction. This will enable the provisions to be activated independently by the TO or the SO. The draft TO provisions have been moved to Special Condition D8. The provisions of AA5E will need to be similarly modified such that they are only activated by the SO.

1.13. We have also included proposed drafting to give effect in the revenue restriction to estimated costs that may arise from the issuance of new equity.

## **Revenue adjustments and incentive mechanisms**

1.14. The main price control formula in Special Condition D2 contains four different mechanisms for adjusting the core revenue allowance. These are discussed in turn below:

### **Transmission Investment for Renewable Generation (TIRG)**

1.15. In 2004 we amended NGET's price control to provide for additional revenue allowances commensurate with undertaking works on its networks specifically required to facilitate the connection of renewable generation. This, in effect, created a separate 'price control' running in parallel with the main price control. The TIRG term in the main formula picks up the allowed revenues through this mechanism. The TPCR process did not review the TIRG adjustment mechanisms. Therefore the provisions that previously existed in Special Condition AA5 have been moved into new Special Condition D3 as a result of our proposals.

### **Pass Through items**

1.16. In our final proposals we set out a number of cost areas where we proposed to base the revenue allowance on the actual costs incurred (or income received) by NGET, whatever they might be. This is done through terms in the main formula reconciling actual and expected costs/income. The items we set out in our final proposals document were:

- The revenues that SPTL and SHETL recover from NGET
- Licence fees
- Non-domestic rates
- Income from Gridcom
- EU inter-TSO compensation scheme
- Price control extension reconciliation revenue adjustment

1.17. Special Condition D4 calculates each of these items, and summates them. This total (PT) is included in the main formula in Special Condition D2.

### **Incentive mechanisms**

1.18. Our final proposals also included a number of other incentive and adjustment mechanisms, related to particular activities and outputs. These are:

- Reliability incentive
- SF6 incentive
- Innovation Funding Incentive (IFI)

1.19. Each of these can result in adjustments being made to the total revenue that NGET should be entitled to recover. The rules for deriving these adjustments are set out in Special Condition D5. The structure of the condition is a primary formula which adds together each of the component parts in any given year (to calculate the term IP), with a number of sub-sections which set out the derivation of each component part.

1.20. As mentioned in our final proposals document, we have recently consulted on the provisions of the DNO IFI scheme. Having considered the responses to the consultation, we have removed the cap on eligible IFI internal expenditure, and therefore the "z" that previously existed in the proposed drafting has been removed.

### **Capex incentive and 'safety net'**

1.21. Our final proposals set out the policy position that NGET should be exposed to 25% of any difference between its capex allowance and its actual capital expenditure. We proposed to give effect to this policy by adjusting revenues in the first year of the next price control, 2012/13.

1.22. Special Condition D9 sets out how this one-off revenue adjustment is calculated. The adjustment is based on the difference between:

- Actual efficiently incurred expenditure (subject to a small number of excluded cost items); and
- Capex allowances (subject to a small number of excluded cost allowances) adjusted for differences between actual volumes of generation and demand and

the volumes of generation and demand assumed in setting the base capex allowance.

1.23. The rules for making the adjustments in the capex allowances for generation and demand volume differences (the 'revenue drivers') are also set out in Special Condition D9 (in term 'LV'), and reflect our policy position, as set out in the final proposals document.

1.24. Our final proposals also set out a policy to consider proposing adjustments to the capex allowances (and the associated revenue allowances) if a licensee was spending significantly below its allowance for capital expenditure. This 'safety net' policy is given effect through Special Condition D9 of NGET's licence.

### **Our related proposals on System Operator (SO) incentives**

1.25. The current set of price controls and incentives in place for NGET is organised under two broad headings: Transmission Owner (TO) and System Operator (SO). The TPCR has proposed changes to the TO elements of the current arrangements. The SO incentives have been subject to a separate (and ongoing) consultation process, resulting in final proposals in February 2007, which, should the proposals be approved, will be implemented on 1 April 2007<sup>1</sup>. As such, we have sought to rationalise the split between the two areas of responsibility, and give effect to it in the proposed licence drafting.

1.26. We propose to issue two separate notices of proposed licence modifications for TO and SO provisions. It is intended that the TO statutory notices that is required to give effect to the price control final proposals will be published in advance of the notice required to implement the SO Incentive scheme. The TO notices will strip out from the existing revenue restriction provisions in Special Condition AA5 and AA5A(which encompasses both SO and TO revenue restrictions) all TO elements, and move these to a number of new licence conditions. The SO notice will then modify the parts of the current revenue restriction that remain. This process will ensure that our TO and SO proposals can both take effect by 1 April 2007.

1.27. The aim of adopting this approach is that it will enable both sets of proposals for the TOs' price control and the SO's external incentive scheme to be implemented independently of each other both now and in the future, removing any interdependency between the two mechanisms.

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<sup>1</sup> For more information on this consultation process, please see Ofgem's initial proposals document for NGET's SO incentive scheme from 1 April 2007, which can be found at the following link:

[http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/17936\\_208\\_06.pdf](http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/17936_208_06.pdf)

## 2. SPTL

### Chapter Summary

This chapter describes the changes we are proposing to make to the licence of SPTL to give effect to our final proposals following our review of SPTL's price control.

### Questions

**Question 2.1:** Do you have any comments on the proposed licence drafting?

## Introduction

2.1. SPTL's licence obligations are derived from a combination of standard conditions for transmission licensees and special conditions specific to SPTL. The bulk of the price control arrangements are contained within the special conditions of SPTL's licence. The amendments to give effect to our TPCR proposals will affect the special conditions of SPTL's licence.

2.2. There are two broad classes of change we are proposing to the special conditions of SPTL's licence to:

- Re-set the base (non-contingent) revenue allowances and main price control formula; and
- Set the rules for calculating a number of potential adjustments to revenues associated with logging up, revenue drivers and incentive mechanisms.

2.3. These two areas are discussed in turn with cross-references to the relevant appendices setting out the associated draft legal text.

2.4. We are also proposing to transfer some obligations in respect of regulatory reporting from current special conditions to new standard conditions, which will consolidate periodic regulatory reporting obligations in a single place in the licence - supporting by a set of RIGs. This is discussed in more detail in chapter 4.

2.5. We have proposed the introduction of output measures via a new standard condition B17. This is the first time that the provisions of this condition will have been consulted on, as they have been developed following our final proposals for the transmission network reliability incentives. As we have previously set out in our consultation documents, we believe it is important for the industry and ourselves to improve the measurement of overall network condition, underlying network risks and the impact on system performance, given the substantial upturn in costs to replace and refurbish assets. We consider that our proposed licence drafting will help deliver such improvements.

2.6. We are also continuing to work on strengthening the regulatory reporting requirements, particularly in relation to monitoring compliance against licence requirements. At present, we envisage that more work will need to be carried out in conjunction with the licensees prior to February's statutory consultation.

2.7. We have also taken the opportunity to make a few minor housekeeping changes such as removing obsolete provisions that no longer apply from 1 April 2007, and relocating various provisions into more intuitive locations.

2.8. We have also included proposed drafting to give effect in the revenue restriction to estimated costs that may arise from the issuance of new equity.

### **Baseline revenue and main formula**

2.9. The main formula that sets the maximum revenue that SPTL is permitted to recover will be set out in Special Condition J2. Definitions of terms used in J2 will be contained in Special Condition J1.

2.10. The structure of Special Condition J2 will be as follows:

- Context: the condition obliges SPTL to use its best endeavours to avoid recovering more from TO activities than the total revenue calculated in accordance with the main formula.
- Main formula: comprises a core element of price control based revenue allowance (PR) together with excluded service income, plus a number of terms (linked to incentive and adjustment mechanisms - TIRG, PT, IP and CxIncRA) which can potentially alter the core element of revenue. Absent these adjustments, the core revenue allowance increases in line with inflation each year. The main formula also provides for differences between actual revenues and allowed revenues in any given year to be carried forward to the next year (K).
- The derivations of each of the incentive and adjustment mechanisms are set out in other special conditions (discussed below). The main formula consolidates these individual adjustments and nets them off (or adds them to) the core revenues that would otherwise be recoverable.

### **Revenue adjustments and incentive mechanisms**

2.11. The main price control formula in Special Condition J2 contains four different mechanisms for adjusting the core revenue allowance. These are discussed in turn below:

### **Transmission Investment for Renewable Generation (TIRG)**

2.12. In 2004 we amended SPTL's price control to provide for additional revenue allowances commensurate with undertaking works on its networks specifically required to facilitate the connection of renewable generation. This, in effect, created a separate 'price control' running in parallel with the main price control. The TIRG term in the main formula picks up the allowed revenues through this mechanism. The TPCR process did not review the TIRG adjustment mechanisms. Therefore the provisions that previously existed in Special Condition O have been moved into new Special Condition J3 as a result of our proposals.

### **Pass Through items**

2.13. In our final proposals we set out a number of cost areas where we proposed to base the revenue allowance on the actual costs incurred (or income received) by SPTL, whatever they might be. This is done through terms in the main formula reconciling between actual and expected costs/income. The items were:

- Licence fees
- Non-domestic rates
- Any income adjusting events

2.14. Special Condition J4 calculates each of these items, and adds them up. This total (PT) is included in the main formula in Special Condition J2.

### **Incentive mechanisms**

2.15. Our final proposals also included a number of other incentive and adjustment mechanisms, related to particular activities and outputs. These are:

- Reliability incentive
- Revenue drivers (please see below for more details)
- SF6 incentive
- Innovation Funding Incentive

2.16. Each of these can result in adjustments being made to the total revenues that SPTL should be entitled to recover. The rules for deriving these adjustments are set out in Special Condition J5. The structure of the condition is a primary formula which adds together each of the component parts in any given year (to calculate the term IP), with a number of sub-sections which set out the derivation of each component part.

2.17. As mentioned in our final proposals document, we have recently consulted on the provisions of the DNO IFI scheme. Having considered the responses to the consultation, we have removed the cap on eligible IFI internal expenditure, and therefore the "z" that previously existed in the proposed drafting has been removed.

**Capex incentive and 'safety net'**

2.18. Our final proposals set out the policy position that SPTL should be exposed to 25% of the difference between its capex allowance and its actual capital expenditure. We proposed to give effect to this policy by adjusting revenues in the first year of the next price control, 2012/13.

2.19. Special Condition J7 sets out how this one-off revenue adjustment is calculated. The adjustment is based on the difference between:

- Actual efficiently incurred expenditure (subject to a small number of excluded cost items); and
- Capex allowances (subject to a small number of excluded cost allowances) adjusted for differences between actual volumes of generation connections and assumed in setting the base capex allowance.

2.20. The rules for making the adjustments in the capex allowances for generation volume differences are set out in Special Condition J7 also (in term 'LV').

2.21. The adjustment to revenue allowances made in 2012/13 pursuant to Special Condition J7 will also take account of any revenue that might already have been advanced to SPTL pursuant to Special Condition J5 ('revenue drivers'), as discussed below.

2.22. Our final proposals also set out a policy to consider proposing adjustments to the capex allowances (and the associated revenue allowances) if a licensee was spending significantly below its allowance for capital expenditure without good reason. This 'safety net' policy is given effect through Special Condition J7 of SPTL's licence.

**Revenue drivers**

2.23. We are also proposing to introduce a mechanism for SPTL to adjust revenues within the price control period if the pace at which new generation connections are required is significantly more rapid than we have assumed in setting our base revenue allowances. Special condition J5 sets out how this mechanism will operate.

## 3. SHETL

### Chapter Summary

This chapter describes the changes we are proposing to make to the licence of SHETL to give effect to our final proposals following our review of SHETL's price control.

### Question box

**Question 3.1:** Do you have any comments on the proposed licence drafting?

## Introduction

3.1. SHETL's licence obligations are derived from a combination of standard conditions for transmission licensees and special conditions specific to SHETL. The price control arrangements are contained within the special conditions of SHETL's licence. The amendments to give effect to our TPCR proposals will affect the special conditions of SHETL's licence.

3.2. There are two broad classes of change we are proposing to the special conditions of SHETL's licence to:

- Re-set the base (non-contingent) revenue allowances and main price control formula; and
- Set the rules for calculating a number of potential adjustments to revenues associated with logging up, revenue drivers and incentive mechanisms.

3.3. These two areas are discussed in turn with cross-references to the relevant appendices setting out the associated draft legal text.

3.4. We are also proposing to transfer some obligations in respect of regulatory reporting from current special conditions to new standard conditions, which will consolidate periodic regulatory reporting obligations in a single place in the licence - supporting by a set of RIGs. This is discussed in more detail in chapter 4.

3.5. We have proposed the introduction of output measures via a new standard condition B17. This is the first time that the provisions of this condition will have been consulted on, as they have been developed following our final proposals for the transmission network reliability incentives. As we have previously set out in our consultation documents, we believe it is important for the industry and ourselves to improve the measurement of overall network condition, underlying network risks and the impact on system performance, given the substantial upturn in costs to replace and refurbish assets. We consider that our proposed licence drafting will help deliver such improvements.

3.6. We are also continuing to work on strengthening the regulatory reporting requirements, particularly in relation to monitoring compliance against licence requirements. At present, we envisage that more work will need to be carried out in conjunction with the licensees prior to February's statutory consultation.

3.7. We have also taken the opportunity to make a few minor housekeeping changes such as removing obsolete provisions that no longer apply from 1 April 2007, and relocating various provisions into more intuitive locations.

3.8. We have also included proposed drafting to give effect in the revenue restriction to estimated costs that may arise from the issuance of new equity.

### **Baseline revenue and main formula**

3.9. The main formula that sets the maximum revenue that SHETL is permitted to recover will be set out in Special Condition J2. Definitions of terms used in J2 will be contained in Special Condition J1.

3.10. The structure of Special Condition J1 will be as follows:

- Context: the condition obliges SHETL to use its best endeavours to avoid recovering more from TO activities than the total revenue calculated in accordance with the main formula.
- Main formula: comprises a core element of revenue allowance (PR) plus a number of terms (linked to incentive and adjustment mechanisms - TIRG, PT, IP and CxIncRA) which can potentially alter the core element of revenue. Absent these adjustments, the core revenue allowance increases in line with inflation each year. The main formula also provides for differences between actual revenues and allowed revenues in any given year to be carried forward to the next year (K).
- The derivations of each of the incentive and adjustment mechanisms are set out in other special conditions (discussed below). The main formula consolidates these individual adjustments and nets them off (or adds them to) the core revenues that would otherwise be recoverable.

### **Revenue adjustments and incentive mechanisms**

3.11. The main price control formula in J2 contains four different mechanisms for adjusting the core revenue allowance. These are discussed in turn below:

#### **Transmission Investment for Renewable Generation (TIRG)**

3.12. In 2004 we amended SHETL's price control to provide for additional revenue allowances commensurate with undertaking works on its networks specifically

required to facilitate the connection of renewable generation. This, in effect, created a separate 'price control' running in parallel with the main price control. The TIRG term in the main formula picks up the allowed revenues through this mechanism. The TPCR process did not review the TIRG adjustment mechanisms, and therefore the provisions that previously existed in Special Condition O have been moved into new Special Condition J3 as a result of our proposals.

### **Pass Through items**

3.13. In our final proposals we set out a number of cost areas where we proposed to base the revenue allowance on the actual costs incurred (or income received) by SHETL, whatever they might be. This is done through terms in the main formula reconciling between actual and expected costs/income. The items were:

- Licence fees
- Non-domestic rates
- Any income adjusting events

3.14. Special Condition J4 calculates each of these items, and adds them up. This total (PT) is included in the main formula in Special Condition J2.

### **Incentive mechanisms**

3.15. Our final proposals also included a number of other incentive and adjustment mechanisms, related to particular activities and outputs. These are:

- Reliability incentive
- Revenue drivers (please see below for more details)
- SF6 incentive
- Innovation Funding Incentive

3.16. Each of these can result in adjustments being made to the total revenues that SHETL should be entitled to recover. The rules for deriving these adjustments are set out in Special Condition J5. The structure of the condition is a primary formula which adds together each of the component parts in any given year (to calculate the term IP), with a number of sub-sections which set out the derivation of each component part.

3.17. As mentioned in our final proposals document, we have recently consulted on the provisions of the DNO IFI scheme. Having considered the responses to the consultation, we have removed the cap on eligible IFI internal expenditure, and therefore the "z" that previously existed in the proposed drafting has been removed.

**Capex incentive and 'safety net'**

3.18. Our final proposals set out the policy position that SHETL should be exposed to 25% of the difference between its capex allowance and its actual capital expenditure. We proposed to give effect to this policy by adjusting revenues commensurately in the first year of the next price control, 2012/13.

3.19. Special Condition J7 sets out how this one-off revenue adjustment is calculated. The adjustment is based on the difference between:

- Actual efficiently incurred expenditure (subject to a small number of excluded cost items); and
- Capex allowances (subject to a small number of excluded cost allowances) adjusted for differences between actual volumes of generation connections and assumed in setting the base capex allowance.

3.20. The rules for making the adjustments in the capex allowances for generation volume differences are set out in Special Condition J7 also (in term 'LV').

3.21. The adjustment to revenue allowances made in 2012/13 pursuant to Special Condition J7 will also take account of any revenue that might already have been advanced to SHETL pursuant to Special Condition J5, Part 2 ('revenue drivers'), as discussed below.

3.22. Our final proposals also set out a policy to consider proposing adjustments to the capex allowances (and the associated revenue allowances) if a licensee was spending significantly below its allowance for capital expenditure without good reason. This 'safety net' policy is given effect through Special Condition J7 of NGET's licence.

**Revenue drivers**

3.23. We are also proposing to introduce a mechanism for SHETL to adjust revenues within the price control period if the pace at which new generation connections are required is significantly more rapid than we have assumed in setting our base revenue allowances. Special condition J5 sets out how this mechanism will operate.

## 4. Regulatory reporting and associated policy issues

### Chapter Summary

This chapter describes the changes we are proposing to make to the standard conditions of the transmission licence to consolidate and strengthen the requirements on licensees to report periodically on costs, revenues and performance metrics. It also describes the new obligation we are proposing to develop in respect of network output measures.

### Questions

**Question 4.1:** Do you agree with our proposed approach to acquire information on the performance of the licensees?

**Question 4.2:** Do you have any comments on the proposed licence drafting?

### Introduction

4.1. The current transmission licences oblige the companies to report periodically on a wide range of issues relating to the costs they incur, the revenues they recover and the physical characteristics and performance of their networks. These obligations have developed in a piecemeal fashion over time and are spread out across a number of different licence conditions.

4.2. We are proposing to consolidate these periodic reporting obligations within two new standard conditions, B15 and B16, which will deal with cost and output reporting and revenue reporting, respectively. We are also proposing minor changes to some of the existing standard conditions. These changes cover a few minor general housekeeping, including extending to transmission some general changes in regulatory reporting that have previously been consulted and concluded on in Electricity and Gas Distribution.

4.3. The obligations under B15 and B16 will be complemented by a set of RIGs. The detail and format of the reporting requirements will be contained within the RIGs rather than in the licence itself. A draft Regulatory Reporting Pack, exclusive of revenue reporting, has already been discussed with each licensee. An updated pack with illustrative figures for 2004/05 has also been sent to the transmission licensees for comment. A blank copy is available on the Ofgem website.

4.4. As part of the TPCR from 2007/08 to 2011/12, we formed a view that future TPCRs (and the regulation of transmission in general) would benefit from having a wider range of metrics in relation to the outputs of the transmission system. This will hopefully provide a fuller picture of how the companies are performing, and what consumers are getting in return for the funding we provide. We also concluded that the licensees themselves were best placed to develop such network output measures. Our final proposal to continue to apply the transmission network

reliability incentive was informed by our belief that until such time as network output measures could be developed and implemented, incentives for enhanced system performance should remain in place. We are therefore proposing a new standard licence condition to oblige the transmission companies to develop such output measures in a timely manner. The draft provisions of Standard Condition B17, provided in appendix 9, set out how we currently anticipate the legal text regarding network output measures might look. We are also considering whether it would be beneficial to include a provision to set out in detail a process by which information and notices can be served on the Authority. As mentioned earlier, we will continue to engage the transmission licences in the time remaining until our statutory licence consultation document is published in February 2007.

## Existing Standard Conditions

4.5. We are proposing, pursuant to a general process of housekeeping and updating the licences, to amend the following existing standard conditions:

- B1 - Regulatory Accounts
- B2 - Change of financial year
- B6 - Restriction on activity and financial ring fencing
- B7 - Availability of resources
- B10 - Credit rating
- B13 - BETTA implementation

4.6. The changes we are proposing to these conditions were set out in our previous (November) consultation, and are set out for completeness in mark-up form in Appendix 9. We will make further changes to these conditions following publication of this document, to be included in the statutory licence consultation in February. In addition to minor changes to the standard conditions detailed in the list above, we are also proposing to amend or introduce the following provisions set out below.

## B9 - Indebtedness

4.7. To improve clarity we have indicated the interpretation that Ofgem will use for "arms length" transactions "on normal commercial terms" when assessing liabilities for payment in the event of ring fencing. This is necessary in order to preclude customers bearing the potentially excessive cost of hybrid securities from related parties

## B15 - Cost and output reporting

4.8. In the November consultation Ofgem has proposed a new standard condition for price control review information. The condition establishes a framework for the provision of information relating to price controls thereby allowing the periodic collection of more accurate information.

4.9. Following the November consultation we are proposing to make the deadline for submission of information to 31st July of each relevant year. Licensees have made representations to Ofgem about the practical implementation of this and the corresponding effect it would have given other statutory and regulatory reporting deadlines. We have given consideration to these implications but we are proposing the 31st July as a standard deadline for consistency of reporting with other regulated network entities.

4.10. A further change to B15 is a new clause relating to comparative operational and cost metrics. As price controls progress we would envisage greater changes and developments within regulatory practice. Developments within transmission networks could potentially produce greater data thereby allowing greater comparability. It is therefore important that, where applicable, such systems are developed and maintained to allow relevant data to be captured.

4.11. Another amendment following the November consultation is the introduction of a new clause requiring the licensee to maintain systems of control and appropriate governance arrangements over information reported under this condition. It is important that information submitted for the purpose of setting and monitoring the price controls is complete and accurate, and this clause clarifies the licensees' obligations in this area. Consequently the introduction of this clause provides additional assurance that the data is "fit for purpose."

4.12. We are planning to publish the cost reporting RIGs established under this condition in late February as part of this consultation.

4.13. New Standard Condition B15 is contained with appendix 9.

## **B16 - Revenue reporting**

4.14. We are also aiming to introduce Standard Licence Condition B16 in relation to Revenue Reporting. This condition aims to establish an effective framework and process for monitoring the revenue restrictions and incentive payments.

4.15. As with B15, we have modified this condition since the November consultation and introduced a clause requiring the licensee to maintain system of control and appropriate governance arrangements over information reported to us. The reasons for this are those described in paragraph 4.10 above. Additionally, we have also placed a requirement on the licensee to inform us of any errors in the revenue calculations.

4.16. B16 also establishes a RIGs process for the reporting of revenue, including revenue derived from the various incentive mechanisms. We are in the process of drafting the RIGs, and aim to publish them in February as part of the statutory licence consultation.

4.17. Amended Standard Licence Condition B16 is contained with Appendix 9.

## **B17 - Development of network output measures**

4.18. The final proposals document indicated Ofgem's intention to develop reporting frameworks for network output measures. Following on from this we are therefore proposing to introduce Standard Condition B17 that aims to acquire good quality information in relation to the following areas:

- "Asset Condition" - the current condition of the population of assets which collectively form the licensee's transmission system, including asset component condition, reliability, and the predicted rate of deterioration in the condition of such assets relevant for their current and forecast ability to perform their required function;
- "Network Risk" - the overall level of risk to the reliable provision of network capability of the transmission system as a result of the Asset Condition and the interdependence between assets;
- "Network Performance" - those aspects of the technical performance of the licensee's transmission system having a direct impact on the reliability and cost of services provided by the licensee in its capacity as transmission owner to its users, and
- "Network Capability" - the level of the capability and the utilisation of the licensee's transmission system at entry and exit points and other network capability and utilisation factors.

4.19. The aim of requesting information in these specified areas is to:

- monitor the licensee's performance in development, maintenance and operation of an efficient, co-ordinated and economical system of electricity transmission;
- permit the assessment of historical and forecast network expenditure on the licensee's transmission system;
- facilitate comparative analysis over time between geographic areas and asset groups within the licensee's transmission system, licensed transmission networks within Great Britain, transmission networks in Great Britain and in other countries, and transmission and distribution networks in Great Britain;
- facilitate the communication in a transparent manner of relevant information regarding the capability and performance of the licensee's transmission system, and
- facilitate the assessment of customer satisfaction derived from the services provided by the licensee in its capacity as transmission owner to its users.

4.20. The new Standard Condition B17 is contained within Appendix 9.

## Appendices

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### Index - Supplementary Appendices

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7	SPTL Transmission Licence Special Conditions
8	SHETL Transmission Licence Special Conditions
9	Transmission Licence Standard Conditions

Note that the Supplementary Appendices are found in a separate appendices document.

## Appendix 1 - Consultation Response and Questions

1.1. Ofgem would like to hear the views of interested parties in relation to any of the issues set out in this document.

1.2. We would especially welcome responses to the specific questions which we have set out at the beginning of each chapter heading and which are replicated below.

1.3. Responses should be received by 16 February 2007 and should be sent to:

Robert Hull  
Director - Transmission  
Office of Gas & Electricity Markets  
9 Millbank  
London  
SW1P 3GE

Tel: 020 7901 7050  
Email: [tpcr.responses@ofgem.gov.uk](mailto:tpcr.responses@ofgem.gov.uk)

1.4. Unless marked confidential, all responses will be published by placing them in Ofgem's library and on its website [www.ofgem.gov.uk](http://www.ofgem.gov.uk). Respondents may request that their response is kept confidential. Ofgem shall respect this request, subject to any obligations to disclose information, for example, under the Freedom of Information Act 2000 or the Environmental Information Regulations 2004.

1.5. Respondents who wish to have their responses remain confidential should clearly mark the document/s to that effect and include the reasons for confidentiality. It would be helpful if responses could be submitted both electronically and in writing. Respondents are asked to put any confidential material in the appendices to their responses.

1.6. Next steps: Having considered the responses to this consultation, Ofgem intends to continue to engage the transmission licensees in developing the drafting. The conclusion of the process will be the publication of our statutory licence consultation in February 2007. Should the licensees accept the provisions in the February consultation, we will be issuing directions to modify the transmission licences in March 2007. Any questions on this document should, in the first instance, be directed to:

Colin Green  
Senior Manager - Transmission Price Control Review  
Office of Gas & Electricity Markets  
9 Millbank  
London

Proposed TPCR licence modification

19 January 2007

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SW1P 3GE

Tel: 020 7901 7143

Email: colin.green@ofgem.gov.uk

**CHAPTER: 1**

**Question1:** Do you have any comments on the proposed licence drafting?

**CHAPTER: 2**

**Question1:** Do you have any comments on the proposed licence drafting?

**CHAPTER: 3**

**Question 3.1:** Do you have any comments on the proposed licence drafting?

**CHAPTER: 4**

**Question 4.1:** Do you agree with our proposed approach to acquire information on the performance of the licensees?

**Question 4.2:** Do you have any comments on the proposed licence drafting?

## Appendix 2 – Summary of Respondents' Views

1.1. This appendix summarises the responses to the November licence drafting consultation document, and sets out our view of the issues raised. The following text summarises the key themes, separated into licensees' views, and other respondents' views. Please note that due to the relatively low number of responses, the following sections break with the normal structure of setting out responses by chapter.

### **Regulatory Reporting**

1.2. NGET is supportive of Ofgem's approach to collate all regulatory reporting obligations into one location in each licence, and considers that they should improve the transparency of available information. However, NGET considers that there should be a clear regulatory purpose in requiring the information, and the cost of providing that information should be proportionate to the regulatory benefit.

1.3. SPTL suggested that there are governance issues related to regulatory reporting which need some further work. SPTL considers that there is an important distinction between reporting requirements set out in the licence, which requires a formal changes process, and information provided for in the RIGs. SPTL is concerned that the change process supporting the RIGs allows Ofgem to introduce changes with limited consultation, and without formal consent.

1.4. SHETL was broadly supportive of our proposals to capture all reporting requirements into a single new Standard Condition B16. SHETL did suggest that the increase in information required by the Authority under the umbrella of regulatory reporting should result in a lesser demand for information at the time of the next price control.

#### *Ofgem's response*

1.5. We welcome the broad support for our proposed changes to the regulatory reporting regime. In addition to improving the quality of information to the Authority, we expect this will reduce the workload the licensees face when the next price control needs to be set. By having this detailed information, we can also be aware of any issues as they become known to us, and can be dealt with in the appropriate manner.

### **Regulatory Accounts**

1.6. NGET recognises our attempts to bring this part of the licence up to date and the associated additional elements of the regulatory accounts. NGET would prefer that references to the consolidated transmission business are retained for consistency, and applied throughout the licence in the appropriate locations.

*Ofgem's response*

1.7. We have acknowledged this point.

**Reliability Incentives**

1.8. NGET identified that there was a difference in the metric used for calculating unsupplied energy compared to Ofgem's proposals for the scheme for SHETL and SPTL. NGET suggested that there should continue to be drafting in the licence that sets out the requirements for a methodology for calculating unsupplied energy to be in place. NGET also suggested that there was the potential for confusion regarding the application of the various tables in the proposed drafting. To address this, NGET suggested that each table should have an additional row added, to include relevant year t.

1.9. SPTL believes that there needs to be the introduction of a relevant year t concept in the proposed drafting.

1.10. SHETL expressed concern that it had not yet seen a version of the reliability incentive to be proposed from 1 April 2007.

*Ofgem's response*

1.11. Ofgem is now providing full drafting for the reliability incentive in this consultation document. As set out in our final proposals document, the structure of the scheme has not changed, merely the parameter values. However, these have been calculated on the same basis as the previous schemes. We also note NGET's point on adding further clarification to the tables in the drafting, and have made the necessary amendments.

**Innovation Funding**

1.12. NGET considers that two additional terms, IFI annual report and eligible IFI projects needs to be included in the IFI drafting provisions. It also considers that there should be supporting RIGs and a reference to a Good Practice Guide, in the same way as in the existing electricity distribution licence drafting.

1.13. SPTL considers that there should be some minor amendments to the algebra in the IFI scheme. It also considers that there is an unnecessary redefinition of the term "z" which dictates the limitation on the amount of funding that can be used for internal purposes.

1.14. SHETL made the point that the previous set of licence drafting regarding the Innovation Funding Incentive did not include a de minimis amount. SHETL believes this should be addressed.

*Ofgem's response*

1.15. Our final proposals document set out our position that there would be a de minimis amount of £500,000 written into the licence drafting. For the Scots, this is in addition to being able to include TIRG assets in the calculation of regulated revenue. As set out elsewhere, the "z" term has now been removed.

**SF6 Incentive**

1.16. NGET suggested some minor changes to the proposed SF6 incentive drafting, including binding the reporting of information to the relevant RIGs.

1.17. SPTL considers that the SF6 incentive drafting as previously proposed implies the licensee would be subject to a penalty as the algebra derives a value figure from the variance between two percentages.

*Ofgem's response*

1.18. The RIGs are still in development, but we envisage the reporting of information in relation to the SF6 scheme to be provided in conjunction with standard condition B16 and the RIGs. We do not feel that there is any provision for a penalty in the drafting of the SF6 incentive algebra. As set out in our final proposals document, there is a target profile for leakage as a proportion of inventory, and out-performance in this area is rewarded with a payment. There is no provision in the drafting for a penalty if the licensee underperforms.

**SO Internal Costs**

1.19. NGET considers that the draft licence modifications for NGET's SO internal costs contain some but not all of the changes required to represent Ofgem's proposals in licence form. NGET welcomes inclusion of new terms for tax and pensions, as well as the removal of redundant algebraic terms. NGET considers that the non-incentivised element of the NGET SO RAV includes investment prior to 2001 in assets with a 40 year life, and that this element will therefore not be fully depreciated by 2010/11 as Ofgem states. NGET also considers that it is not correct to state that there are no rateable assets as NGET SO property rates are considered in the calculation of NGET business rates.

1.20. NGET also considers that the depreciation calculation specified for NGET SO assets is inconsistent with the depreciation calculations used across NGET and NGG NTS. It therefore recommends this is amended to a 'straight-line' depreciation calculation.

*Ofgem's response*

1.21. We consider that the licence drafting in this document represents our final proposals position on SO internal costs. However, as mentioned elsewhere, the provisions may be subject to change depending on the outcome of the bilateral meetings we will have with the licensees in the run up to our statutory licence consultation in February.

**Other comments**

1.22. NGET welcomed Ofgem's intention to initiate industry-wide consultation on recovering costs of temporary physical disconnection, with a view to implementing the changes from April 2007. NGET considers that it would be beneficial to include a separate term in the revenue restriction formula in order to make the correct adjustment.

1.23. NGET considers that because the generic final sums arrangements do not make a direct linkage between costs incurred and final sums revenue received, then both will need to be addressed within the price control. NGET anticipates that final sums revenue would not be an excluded service, but would count against the revenue restriction. Given this treatment, any partially completed investments or other costs arising as part of a substantially terminated user agreement would need to be addressed in the capex incentive mechanism.

1.24. NGET considers that there are several conditions that are now obsolete and could be removed, including Special Condition C, I, J and paragraph 5 of Special Condition L.

1.25. SHETL considers that whilst there have been no changes to the TIRG funding mechanism, we have proposed changes to the duration over which depreciation is calculated. SHETL believes that as a result, the TIRG DEPt term in the schedules would need to be doubled.

1.26. All the respondents to the consultation welcomed our approach to simplify and consolidate the transmission licences. However, one respondent to the consultation expressed concerns that the regulatory regime is being relaxed in several areas. Without going into specifics, this consultation respondent stated that it prefers a more rigorous regime given the information imbalance between the TSOs and the market.

*Ofgem's response*

1.27. We have taken onboard the comments made by NGET and will be giving further consideration to the best way in which to deal with the issues and will address them in our February 2007 statutory licence consultation.

1.28. We can confirm that our proposed drafting includes depreciation over twenty years for TIRG assets.

1.29. We acknowledge respondents' broad support for our intent to simplify the licences, and will continue to make changes and housekeeping amendments for the February 2007 statutory licence consultation.

## Appendix 3 – The Authority's Powers and Duties

1.1. Ofgem is the Office of Gas and Electricity Markets which supports the Gas and Electricity Markets Authority ("the Authority"), the regulator of the gas and electricity industries in Great Britain. This Appendix summarises the primary powers and duties of the Authority. It is not comprehensive and is not a substitute to reference to the relevant legal instruments (including, but not limited to, those referred to below).

1.2. The Authority's powers and duties are largely provided for in statute, principally the Gas Act 1986, the Electricity Act 1989, the Utilities Act 2000, the Competition Act 1998, the Enterprise Act 2002 and the Energy Act 2004, as well as arising from directly effective European Community legislation. References to the Gas Act and the Electricity Act in this Appendix are to Part 1 of each of those Acts.<sup>2</sup>

1.3. Duties and functions relating to gas are set out in the Gas Act and those relating to electricity are set out in the Electricity Act. This Appendix must be read accordingly<sup>3</sup>.

1.4. The Authority's principal objective when carrying out certain of its functions under each of the Gas Act and the Electricity Act is to protect the interests of consumers, present and future, wherever appropriate by promoting effective competition between persons engaged in, or in commercial activities connected with, the shipping, transportation or supply of gas conveyed through pipes, and the generation, transmission, distribution or supply of electricity or the provision or use of electricity interconnectors.

1.5. The Authority must when carrying out those functions have regard to:

- The need to secure that, so far as it is economical to meet them, all reasonable demands in Great Britain for gas conveyed through pipes are met;
- The need to secure that all reasonable demands for electricity are met;
- The need to secure that licence holders are able to finance the activities which are the subject of obligations on them<sup>4</sup>; and
- The interests of individuals who are disabled or chronically sick, of pensionable age, with low incomes, or residing in rural areas.<sup>5</sup>

1.6. Subject to the above, the Authority is required to carry out the functions referred to in the manner which it considers is best calculated to:

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<sup>2</sup> entitled "Gas Supply" and "Electricity Supply" respectively.

<sup>3</sup> However, in exercising a function under the Electricity Act the Authority may have regard to the interests of consumers in relation to gas conveyed through pipes and vice versa in the case of it exercising a function under the Gas Act.

<sup>4</sup> under the Gas Act and the Utilities Act, in the case of Gas Act functions, or the Electricity Act, the Utilities Act and certain parts of the Energy Act in the case of Electricity Act functions.

<sup>5</sup> The Authority may have regard to other descriptions of consumers.

- 
- Promote efficiency and economy on the part of those licensed<sup>6</sup> under the relevant Act and the efficient use of gas conveyed through pipes and electricity conveyed by distribution systems or transmission systems;
  - Protect the public from dangers arising from the conveyance of gas through pipes or the use of gas conveyed through pipes and from the generation, transmission, distribution or supply of electricity;
  - Contribute to the achievement of sustainable development; and
  - Secure a diverse and viable long-term energy supply.

1.7. In carrying out the functions referred to, the Authority must also have regard, to:

- The effect on the environment of activities connected with the conveyance of gas through pipes or with the generation, transmission, distribution or supply of electricity;
- The principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed and any other principles that appear to it to represent the best regulatory practice; and
- Certain statutory guidance on social and environmental matters issued by the Secretary of State.

1.8. The Authority has powers under the Competition Act to investigate suspected anti-competitive activity and take action for breaches of the prohibitions in the legislation in respect of the gas and electricity sectors in Great Britain and is a designated National Competition Authority under the EC Modernisation Regulation<sup>7</sup> and therefore part of the European Competition Network. The Authority also has concurrent powers with the Office of Fair Trading in respect of market investigation references to the Competition Commission.

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<sup>6</sup> or persons authorised by exemptions to carry on any activity.

<sup>7</sup> Council Regulation (EC) 1/2003

## Appendix 4 - Glossary

### A

None

### B

#### Baseline

Baselines define the reference levels of capacity that the transmission licensee is to release. Baselines also determine the levels above (or below) which incremental capacity is defined.

#### Baseline Capital Expenditure

Baseline capital expenditure is the total amount of capex required in association with the baseline. It includes both load related capex and non-related capex.

#### British Electricity Trading and Transmission Arrangements (BETTA)

BETTA introduced a single GB-wide set of arrangements for trading energy and for access to and use of the transmission system which came fully into effect at BETTA go-live (1 April 2005).

### C

#### Capital Expenditure (Capex)

Expenditure on investment in long-lived transmission assets, such as gas pipelines or electricity overhead lines.

#### Capex Incentive

A mechanism that limits the extent to which our allowed revenue and actual revenues differ. Our final proposals limit the difference to 25%.

### D

#### Distribution Price Control Review (DPCR)

The price control review for the electricity distribution network operators conducted in 2003 & 2004. The resulting price control covers the years 2005 to 2010.

#### Distribution Network Operators (DNOs)

Holders of electricity distribution licences. Licences are granted for specified geographical areas. Currently in Great Britain there are seven companies who own the fourteen licensed distribution areas.

**E**

[None](#)

**F**

[Final Sums Liability \(FSL\)](#)

The level of financial security a generator seeking connection to the network is required to post to cover the costs of works completed to connect them.

[Forecast Business Plan Questionnaire \(FBPQ\)](#)

Expenditure information requested by Ofgem from the licensees relating to the period from 2005/06 to 2011/12.

**G**

[Great Britain System Operator \(GBSO\)](#)

See SO.

**H**

[Historical Business Plan Questionnaire \(HBPQ\)](#)

Expenditure information requested by Ofgem from the licensees relating to the period from the year before their most recent five-year full price control until 2004/05.

**I**

[Information Quality Incentive Mechanism](#)

A form of incentive design adopted by Ofgem as part of the DPCR which provided companies with the potential for greater rewards if they chose more challenging cost targets.

[Innovation Funding Initiative \(IFI\)](#)

A mechanism to remunerate research & development expenditure by DNOs.

**L****Load Related Capex**

The installation of new assets to accommodate changes in the level or pattern of electricity or gas supply and demand.

**M**

None

**N****National Grid Electricity Transmission (NGET)**

The electricity transmission licensee in England & Wales.

**Non-Load Related Capex**

The replacement or refurbishment of assets which are either at the end of their useful life due to their age or condition, or need to be replaced on safety or environmental grounds.

**O****Operating Expenditure (Opex)**

The costs of the day to day operation of the network such as staff costs, repairs and maintenance expenditures, and overhead.

**P****Public Electricity Suppliers (PESs)**

The fourteen successor companies to which were transferred the electricity distribution and supply undertakings of the former area boards at privatisation. Each PES was required to provide distribution services and connections, and to provide a supply to consumers, in the geographical area (the 'authorised area') formerly served by the area board to which it was the successor. The duty to supply was progressively removed as competition was introduced, and was eliminated entirely by the Utilities Act 2000 which converted each PES licence into separate distribution and supply licences. The duty to provide distribution services and connections within its authorised area remains an obligation of the EDNO which, in each of the fourteen areas, is the present successor to the relevant PES.

### Plugs Model

A method used by NGET to classify network assets (for the purposes of charging) as either general infrastructure assets or connection assets. The plugs model identifies connection assets as excluding any assets which are shared or sharable by another user. The cost of connection assets are used to derive connection charges, while the cost of infrastructure assets is used to derive use of system charges. See Transmission Network Use of System charges.

## R

### Regulatory Asset Value (RAV)

The value ascribed by Ofgem to the capital employed in the licensee's regulated transmission or (as the case may be) distribution business (the 'regulated asset base'). The RAV is calculated by summing an estimate of the initial market value of each licensee's regulated asset base at privatisation and all subsequent allowed additions to it at historical cost, and deducting annual depreciation amounts calculated in accordance with established regulatory methods. These vary between classes of licensee. A deduction is also made in certain cases to reflect the value realised from the disposal of assets comprised in the regulatory asset base. The RAV is indexed to RPI in order to allow for the effects of inflation on the licensee's capital stock. The revenues licensees are allowed to earn under their price controls include allowances for the regulatory depreciation and also for the return investors are estimated to require to provide the capital.

### Re-openers

A process undertaken by Ofgem to re-set the revenue allowances (or the parameters that give rise to revenue allowances) under a price control before the scheduled next formal review date for the relevant price control.

### Repex

In this consultation this term describes the use of an operating allowance to fund each year's expected non load related capital expenditure.

### RPI-X

The form of price control currently applied to network monopolies. Each company is given a revenue allowance in the first year of each control period. The price control then specifies that in each subsequent year the allowance will move by 'X' per cent in real terms.

### Revenue Driver

A means of linking revenue allowances under a price control to specific measurable events which are considered to influence costs. An example might be to allow a specified additional revenue allowance for each MW of new generation connecting to

the network. Revenue drivers are used by Ofgem to increase the accuracy of the revenue allowances.

#### Rolling Incentives

A measure which ensures licensees are able to retain the rewards of efficiency savings for a period of five years (consistent with the duration of the price control) irrespective of when the efficiency saving is made.

### S

#### Security and Quality of Supply Standard (SQSS)

As referred to in the electricity Transmission Licence Standard Conditions C17 and D3, this is the standard in accordance with which the electricity transmission licensees shall plan, develop and operate the transmission system.

#### Scottish Hydro-Electric Transmission Limited (SHETL)

The electricity transmission licensee in northern Scotland.

#### Scottish Power Transmission Limited (SPTL)

The electricity transmission licensee in southern Scotland.

#### Sliding scale

This term is used generically to describe incentive schemes which involve profit (and loss) sharing around a fixed target costs, such as the current form of SO incentives in gas and electricity.

#### System Operator (SO)

The system operator has responsibility to construct, maintain and operate the NTS and associated equipment in an economic, efficient and co-ordinated manner. In its role as SO, NGG NTS is responsible for ensuring the day-to-day operation of the transmission system.

### T

#### Transmission Entry Capacity (TEC)

Defines a generator's maximum allowed export capacity onto the transmission system. The holder of the TEC has the right to export the specified number of megawatts onto the transmission system at any one time, and is eligible for compensation if NGET cannot accommodate this export on the network.

#### Transmission Investment for Renewable Generation (TIRG)

In the context of this document, this means the regulatory mechanisms developed before the start of the next main price control in 2007, to fund a number of specific network enhancement projects required to provide transmission capacity for new renewable generation plants.

#### Transmission Owners (TO)

Companies which hold transmission owner licenses. Currently there are three electricity TOs; NGET, SPTL and SHETL. NGG NTS is the gas TO.

#### Transmission Price Control Review (TPCR)

The TPCR will establish the price controls for the transmission licensees which will take effect in April 2007 for a 5-year period. The review applies to the three electricity transmission licensees, NGET, SPTL, SHETL and to the licensed gas transporter responsible for the gas transmission system, NGG NTS

#### Transmission Use of System Charges (TNUoS)

Charges levied by NGET on users of the GB electricity transmission network to recover the costs of providing and maintaining the general network infrastructure assets. TNUoS charges vary by location, and are different for generators and for suppliers.

## U

None

## V

#### Vesting Assets

Assets included in the RAV at the vesting date.

#### Vesting

The date at which the regulated gas and electricity transmission and distribution companies were privatised.

## Appendix 5 - Feedback Questionnaire

1.1. Ofgem considers that consultation is at the heart of good policy development. We are keen to consider any comments or complaints about the manner in which this consultation has been conducted. In any case we would be keen to get your answers to the following questions:

1. Do you have any comments about the overall process, which was adopted for this consultation?
2. Do you have any comments about the overall tone and content of the report?
3. Was the report easy to read and understand, could it have been better written?
4. To what extent did the report's conclusions provide a balanced view?
5. To what extent did the report make reasoned recommendations for improvement?
6. Please add any further comments?

1.2. Please send your comments to:

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