



*Promoting choice and  
value for all customers*

National Grid Electricity  
Transmission plc,  
Scottish Hydro-Electric  
Transmission Limited, SP  
Transmission Limited, users of  
the electricity transmission  
system, consumer groups and  
other interested parties

Your Ref:  
Our Ref: 248/07  
Direct Dial: 020 7901 7050  
Email: [robert.hull@ofgem.gov.uk](mailto:robert.hull@ofgem.gov.uk)

19<sup>th</sup> October 2007

Dear Colleague,

## **Recovering the costs of compensation for temporary physical disconnection (CAP048) - proposed modification of transmission licences**

### **Purpose of this consultation**

Following the Authority's decision to approve Connection and Use of System Code (CUSC) Amendment Proposal 048 (CAP048) "Firm Access and Temporary Physical Disconnection"<sup>1</sup>, changes are required to the transmission licences held by National Grid Electricity Transmission plc (NGET), Scottish Hydro Electric Transmission Ltd (SHETL) and Scottish Power Transmission Ltd (SPTL). These changes would provide a mechanism for recovering payments made to generators in accordance with the criteria set out in the CAP048 arrangements. This consultation seeks views on how to create such a mechanism in the transmission licences.

### **Background**

CAP048 was approved on 19 March 2004 and came into effect in England and Wales on 1 April 2004, and subsequently came into force in Scotland following implementation of British Electricity Trading and Transmission Arrangements (BETTA) on 1 April 2005. It established a compensation mechanism within the CUSC that required the Great Britain System Operator (GBSO) to compensate generators in the event that they are disconnected from the transmission network because of a planned or unplanned event. Whilst both types of event are potentially eligible for compensation provided the relevant criteria are met, the level of compensation payable under CAP048 is different depending on whether the event is planned or unplanned. Compensation for a planned outage is calculated based on the greater of system average Transmission Network Use of System (TNUoS) charges or site TNUoS charges. For unplanned events, an eligible generator is compensated using the Market Index Price (MIP)<sup>2</sup> for the first 24 hours of an event, with compensation being paid based on TNUoS charges for periods in excess of 24 hours.

<sup>1</sup> Please see the following link for background information and the Authority's decision letter:  
[http://www.nationalgrid.com/uk/Electricity/Codes/systemcode/amendments/amendment\\_archive/](http://www.nationalgrid.com/uk/Electricity/Codes/systemcode/amendments/amendment_archive/).

<sup>2</sup> As published on the Balancing Mechanism Report Service (BMRS) website at [www.bmreports.com](http://www.bmreports.com).

In the approval letter, the Authority indicated that there would be separate consultations on the funding arrangements for costs incurred by the licensees due to the implementation of CAP048. So far, given the outstanding consultation, the GBSO has not yet been able to recoup payments made under the CAP048 mechanism to parties interrupted.

#### *April 2005 and March 2007 consultation documents*

On 7 April 2005, we published a consultation document<sup>3</sup> setting out our thoughts on mechanisms for recovering the costs of compensation under the CAP048 regime. This letter set out two main options for cost recovery, firstly via Balancing Services Use of System (BSUoS) charges and secondly via the Transmission Network Use of System (TNUoS) charges route. The BSUoS route would have seen costs for compensation incorporated within National Grid's System Operator (SO) incentive scheme, or adding a new term to the balancing services activity revenue restriction. The TNUoS route would have added a new term to the transmission asset owners' (TOs') allowed revenue restriction, allowing the costs to be passed through via TNUoS charges, or setting an incentive scheme comprising of targets, caps and collars. During the consultation process for this letter it became apparent that there was limited information available on historic levels of compensation costs in England and Wales, and only information on forecast planned outages in Scotland. It was therefore difficult to set an incentive scheme given the information available at the time.

It also became apparent that following the introduction of BETTA the cost forecasts provided to Ofgem in the course of the April 2005 consultation were not accurate. These forecasts were inaccurate as they included plant which subsequently entered into agreements with NGET which limit or prevent them from being eligible for compensation. Therefore our position following our April 2005 consultation was that an incentive mechanism could not be set with any degree of accuracy and was not appropriate at the time.

On 22 March 2007, Ofgem published an open letter consultation and minded to statement<sup>4</sup>. In this letter we acknowledged that setting an incentive would be difficult due to the lack of relevant data, but continue to consider that in the long term an incentive scheme would be beneficial in minimising the frequency and duration of disconnections from the GB transmission system. However, at this stage, Ofgem acknowledged the risks of setting a target too high, resulting in unnecessarily high costs to users and consumers, or too low, potentially resulting in the need to re-open any cost target.

A difficult issue that materialised in the April 2005 consultation was whether and how to allocate responsibility for compensation costs between the GBSO and the TOs. This issue was returned to in the March 2007 consultation where we state that attributing responsibility between the GBSO and the TOs is problematic, and agree with those respondents who consider the funding mechanism should not be overly complex. Therefore we stated that costs should be recovered solely via TNUoS charges on the basis that the charge represents a payment which allows users to export power to the

---

<sup>3</sup> This letter can be found at: <http://www.ofgem.gov.uk/Networks/Policy/Documents1/10466-11505.pdf>.

<sup>4</sup> This letter can be found at: <http://www.ofgem.gov.uk/Networks/Trans/ElecTransPolicy/Charging/Documents1/Recovering%20the%20cost%20of%20compensation%20for%20temporary%20physical%20disconnection%20-%20CAP048.pdf.pdf>.

transmission system, and therefore would be an appropriate mechanism for rebating costs associated with the unavailability of that system.

Our minded to position, as stated in the March 2007 letter, was that it may be appropriate to insert an additional term into the revenue restrictions of the three transmission licensees which allows them to pass-through compensation costs for the first two years of the price control period starting on 1 April 2007. We also made clear that beyond this period (from 1 April 2009), it may be appropriate to revisit the issue and consider the development of appropriate incentives for the licensees to optimise relevant costs. This timing would be useful given interactions with the reliability incentives and network performance output measures work as described in our Transmission Price Control Review 2007/12 final proposals document<sup>5</sup>.

### **Ofgem's views**

Following our consultations in April 2005 and March 2007, and having carefully considered the associated responses, Ofgem is proposing to introduce licence changes consistent with the approach we set out in the open letter of March 2007.

Our preferred approach is that costs are recovered via TNUoS from all users of the network, by introducing an additional term into the three transmission licensees' revenue restrictions. Our rationale for this position has not changed. We continue to believe, as we set out in our original decision letter on CAP048, that by approving alternative amendment C, the mechanism would essentially be compensating the user for the capacity it is unable to use. Given this view, we continue to believe that the most appropriate mechanism from which to recover the costs of not being able to use the system is that which deals with payments to use the system, namely TNUoS, and more specifically the residual element of TNUoS that does not vary with location. We consider that this licence approach is most consistent with the intent of CAP048.

As set out in appendices 1 to 6, we are proposing to amend NGET's special licence condition D4 (Pass Through Items) and D1 (Transmission Network Revenue Restriction: Definitions), and equivalent provisions in SPTL's and SHETL's special licence condition J4 (Pass Through Items) and J1 (Restriction of Transmission Charges: Definitions), to introduce an additional term and associated definitions to provide an appropriate funding mechanism for the recovery of costs for temporary physical disconnection. The licence drafting makes provisions for cost recovery in an ongoing manner. However, it may be appropriate to consider developing an enduring incentive regime in the future when more data on costs are available, which we envisage would be implemented in April 2009.

In the interim, we propose to introduce the licence modifications appended to this consultation document. The licence drafting takes into account expenditure already incurred by the three transmission licensees<sup>6</sup>, retrospectively from 1 April 2004 (1 April 2005 for SPTL and SHETL) until 31 March 2008, plus subsequent years starting on 1 April. NGET's licence provisions differ from SPTL and SHETL's as essentially it is the GBSO that makes the payments to users under the CAP048 mechanism. For events in England and Wales, NGET would recoup its funding from TNUoS. Similarly, payments made to generators by the GBSO for events on the Scottish transmission systems would

---

<sup>5</sup> This document can be found at the following link:

[http://www.ofgem.gov.uk/Networks/Trans/PriceControls/TPCR4/ConsultationDecisionsResponses/Documents1/16342-20061201\\_TPCR%20Final%20Proposals\\_in\\_v71%206%20Final.pdf](http://www.ofgem.gov.uk/Networks/Trans/PriceControls/TPCR4/ConsultationDecisionsResponses/Documents1/16342-20061201_TPCR%20Final%20Proposals_in_v71%206%20Final.pdf)

<sup>6</sup> Although at present only NGET has incurred any costs relating to interruption events.

be recouped via TNUoS from SPTL and SHETL in respect of their licensed areas, who in turn are allowed to pass through what they have been charged.

### **Consultation questions**

We are keen to obtain industry and consumer views on the proposed modification to NGET, SHETL and SPTL's transmission licences to give effect in the licence to the funding provisions associated with CAP048. The proposed draft licence modifications are provided in appendices 1 to 6 for information, and indicated in red text.

It is open for respondents to comment on any of the issues raised in this letter.

### **Next steps**

We would like to hear the views of any interested parties regarding the issues raised in this letter. Responses should be made by **16<sup>th</sup> November 2007** to:

Karron Baker  
Analyst  
Office of Gas and Electricity Markets  
9 Millbank  
London  
SW1P 3GE

Or by email to [karron.baker@ofgem.gov.uk](mailto:karron.baker@ofgem.gov.uk).

Following closure of this open letter consultation, and careful consideration of respondents' views, we intend to consult formally on this issue in November or December 2007.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Robert Hull', with a horizontal line underneath.

Robert Hull  
Director, Transmission

## Appendix 1 - Proposed drafting of National Grid Electricity Transmission plc's special condition D4

### Special Condition D4. Pass Through Items

1. For the purposes of paragraph 2 of special condition D2 (Restriction on Transmission Network Revenue), in each relevant year  $t$ ,  $PT_t$  shall be derived in accordance with the following formula:

$$PT_t = TSP_t + TSH_t + LF_t + RB_t - TSR_t + ITC_t + Term_t + TPD_t$$

where:

$TSP_t$  means the amount specified to the licensee by SP Transmission Ltd or any successor company in relation to relevant year  $t$  pursuant to its transmission licence;

$TSH_t$  means the amount specified to the licensee by Scottish Hydro-Electric Transmission Ltd or any successor company in relation to relevant year  $t$  pursuant to its transmission licence;

$LF_t$  means the revenue adjustment term, whether of a positive or of a negative value, calculated in the relevant year  $t$  in respect of licence fee payments as derived from the formula set out in paragraph 2;

$RB_t$  means the revenue adjustment term, whether of a positive or of a negative value, calculated in the relevant year  $t$  in respect of non-domestic rates as derived from the formula set out in paragraph 3;

$TSR_t$  means the revenue adjustment term, whether of a positive or of a negative value, calculated in the relevant year  $t$  in respect of revenue earned by the licensee for tower space rental as derived from the formula set out in paragraph 6;

$ITC_t$  shall take the value zero unless otherwise determined by the Authority in the event of the participation by Great Britain in a European Union inter-

TSO compensation scheme, and following consultation with other interested parties;

$Term_t$  means an amount equal to the income received by the licensee in the relevant year  $t$  in respect of users who terminate relevant bilateral agreements for connection and /or access rights to the GB transmission system prior to commencing use of the GB transmission system (for the avoidance of doubt, net of any amounts that are treated as capital contributions); and

**$TPD_t$  means the temporary physical disconnection term and shall be determined in accordance with paragraphs 7 to 8.**

**Formula for the Licence Fee Revenue Adjustment**

2. For the purposes of paragraph 1,  $LF_t$  shall be calculated in accordance with the following formula:

$$LF_t = (LP_t - LA_t) + \left( L_t \times \left( 1 + \frac{I_t}{100} \right) \right)$$

where:

$LP_t$  means an amount equal to the payments made by the licensee, in respect of relevant year  $t$ , in accordance with its obligations set out in standard licence condition A4 (Payments to the Authority) (being for the avoidance of doubt, in pounds sterling in money of the day);

$LA_t$  is derived from the following formula:

$$LA_t = PF_t \times PIT_t$$

where:

$PF_t$  is the amount of the licence fee payments allowance for the relevant year t (in 2004/05 prices) as set out:

Relevant year t commencing on 1 April	2007	2008	2009	2010	2011
$PF_t$	£8,600,000	£8,400,000	£8,200,000	£8,000,000	£8,100,000

$PIT_t$  shall take the same meaning as given in paragraph 2 of special condition D2 (Restriction on Transmission Network Revenue);

$L_t$  shall, in respect of the relevant year commencing 1 April 2007, be calculated as the difference between the actual licence fee payable by the licensee in the relevant year commencing 1 April 2006 pursuant to standard condition A4 (Payments to the Authority) (being, for the avoidance of doubt, in pounds sterling in money of the day) and the estimate made in respect of that relevant year of £13,200,000. In the relevant year commencing 1 April 2008 and each subsequent relevant year  $L_t$  shall take the value zero; and

$I_t$  means the average specified rate as defined in special condition D1 (Definitions).

**Formula for the Non-domestic rates Revenue Adjustment**

3. For the purposes of paragraph 1, subject to paragraph 4 below,  $RB_t$  is an amount calculated in accordance with the following formula:

$$RB_t = (RP_t - RA_t) + \left( Rate_t \times \left( 1 + \frac{I_t}{100} \right) \right)$$

where:

$RP_t$  is the amount payable by the licensee, in respect of the relevant year t, in respect of non-domestic rates;

$RA_t$  is the non-domestic rates allowance, and is derived from the following formula:

$$RA_t = RV_t \times PIT_t$$

where:

$RV_t$  is the non-domestic rates allowance in 2004/05 prices, and shall take the value set out in the table below:

Relevant year t commencing on 1 April	2007	2008	2009	2010	2011
$RV_t$	£93,000,000	£93,000,000	£93,000,000	£93,000,000	£93,000,000

$PIT_t$  shall take the same meaning as given in paragraph 2 of special condition D2 (Restriction on Transmission Network Revenue);

$Rate_t$  shall, in respect of the relevant year commencing 1 April 2007, be calculated as the difference between the non-domestic rates payable by the licensee in respect of the relevant year commencing 1 April 2006 (being for the avoidance of doubt, in pounds sterling in money of the day) and the estimate made in respect of that relevant year of £94,900,000. In the relevant year commencing 1 April 2008 and each subsequent relevant year  $Rate_t$  shall take the value zero; and

$I_t$  means the average specified rate as defined in special condition D1 (Definitions).

4. From the relevant year commencing 1 April 2010,  $RB_t$  shall take the value zero, unless otherwise directed by the Authority on or before 31 March 2010.

5. For the purposes of paragraph 4 of this condition, the Authority may direct that, in respect of the relevant year commencing 1 April 2010 and each subsequent relevant year,  $RB_t$  be calculated in accordance with the formula set out in paragraph 3 of this condition where the Authority is satisfied that the licensee has used reasonable endeavours to minimise the amount payable for those years in respect of non-domestic rates.

**Formula for the tower space rental revenue adjustment**

6. For the purposes of paragraph 1,  $TSR_t$  is an amount calculated in accordance with the following formula:

$$TSR_t = 0.5 \times TSRR_{t-2}$$

where:

$TSRR_{t-2}$  means the revenue received in relevant year t-2 by the licensee from any company in respect of fees for permitting mobile telephony equipment to be installed on the licensee's electricity transmission towers.

**Formula for the Temporary Physical Disconnection Term**

- 7. For the purposes of paragraph 1,  $TPD_t$ , for the relevant year commencing 1 April 2007, is an amount equal to the interruption payments made by the licensee in respect of the period commencing on 1 April 2004 and ending on 31 March 2008 where any payments made by the licensee prior to 1 April 2007 shall be adjusted for 'financing costs' and shall be derived from the following formula:**

$$TPD_t = \left[ \sum_m TPD_m \times TPDMult_m \right] \times PIT_t$$

**where:**

**m** means the relevant year m such that the first relevant year shall be the year commencing on 1 April 2004 and the fourth relevant year shall be the year commencing 1 April 2007;

**TPD<sub>m</sub>** means the interruption payments in 2004/05 prices in the relevant year m;

**PIT<sub>t</sub>** shall, for the relevant year t, take the same meaning as given in paragraph 2 of special condition D2 (Restriction on Transmission Network Revenue);

**TPDMult<sub>m</sub>** is the adjustment factor for financing costs and is calculated using the formula below:

$$TPDMult_m = (1.0625)^p$$

**Where**

**p** is the number of years between the relevant year t and the relevant year m, and

**TPDMult<sub>m</sub>** shall take the number set out in the table below:

<b>Relevant year m in which interruption payment is made</b>	<b>2004/05</b>	<b>2005/06</b>	<b>2006/07</b>	<b>2007/08</b>
<b>TPDMult<sub>m</sub></b>	<b>1.199463</b>	<b>1.12891</b>	<b>1.06250</b>	<b>1.00000</b>

8. For the relevant year t commencing 1 April 2008, and each subsequent relevant year t, TPD<sub>t</sub> shall be an amount equal to the interruption payments made by the licensee within each respective relevant year t.

**Appendix 2 - Proposed drafting of National Grid Electricity Transmission plc's special condition D1**

**Special Condition D1. Transmission Network Revenue Restriction: Definitions**

1. In this special condition, and in special conditions D2 to D10 inclusive:

“average specified rate”	means the average of the daily base rates of Barclays Bank PLC current from time to time during the period in respect of which any calculation falls to be made.
“base transmission revenue”	means the revenue allowances calculated in accordance with paragraph 2 of special condition D2 (Restriction on Transmission Network Revenue).
“excluded services”	means those services provided by the licensee as part of its transmission business which in accordance with the principles set out in Special Condition D10 (Excluded Services) fall to be treated as excluded services.
<b>“interruption payment”</b>	<b>shall, for the purposes of paragraphs 7 and 8 of special condition D4 (Pass Through Items), have the same meaning as set out in section 11 of the Connection and Use of System</b>

**Code provided for in paragraph 2 of standard condition C10 (Connection and Use of System Code (CUSC)).**

“logged up costs”

means:

- (a) for the purposes of paragraphs 2 and 3 of special condition D2 (Restriction on Transmission Network Revenue), the capital expenditure and operating expenditure costs incurred by the licensee in respect of those items referred to in those paragraphs; and
- (b) for the purposes of paragraphs 3 and 11 of special condition D9 (Capital Expenditure Incentive and Safety Net), the capital expenditure incurred by the licensee in respect of those items referred to in those paragraphs.

“maximum revenue”

means the revenue calculated in accordance with the formula in paragraph 2 of special condition D2 (Restriction on Transmission Network Revenue).

“non-domestic rates”

means non-domestic rates payable by the licensee in respect of

hereditaments (other than excepted hereditaments being a hereditament consisting of or comprising premises used wholly or mainly: (a) as a shop or other place for the sale, display or demonstration of apparatus or accessories for use by consumers of electricity (any use for receipts of payments for the use of electricity being disregarded); (b) as office premises of the licensee where those premises are not situated on operational land of the licensee; or (c) for both of the foregoing purposes (for the avoidance of doubt, office premises and operational land shall have the meaning ascribed to those terms in SI 2000/525 Central Ratings List (England) Regulations)) wholly or mainly used for the purposes of the transformation or transmission of electrical power, or for ancillary purposes.

“relevant year”

means a financial year commencing on or after 1 April 1990.

“relevant year t”

means that relevant year for the purposes of which any calculation falls to be made;

“relevant year t-1”	means the relevant year preceding relevant year t, and similar expressions shall be construed accordingly.
“remote transmission asset rentals”	means any rent or other periodic payment receivable by the licensee from an authorised electricity operator under an agreement relating to remote transmission assets.
“TIRG relevant year”	means, in relation to each transmission investment project i specified in Annex A of special condition D3 (Adjustment to the Transmission Network Revenue Restriction due to Transmission Investment for Renewable Generation), the relevant year in which a revenue allowance falls to be made under special condition D3 (Adjustment to the Transmission Network Revenue Restriction due to Transmission Investment for Renewable Generation) with respect to that transmission investment project i, where: <p style="margin-left: 40px;">(a) <math>t=p</math> means the relevant year commencing 1 April 2005;</p>

- (b)  $t=p$  to  $t=-1$  means the preconstruction period (where  $p \leq -1$ );
- (c)  $t=0$  means the relevant year in which construction of that transmission investment project  $i$  commences;
- (d)  $t=0$  to  $t=n$  means the construction period;
- (e)  $t=n$  means the relevant year in which that transmission investment project  $i$  is commissioned;
- (f)  $t=n+1$  means the relevant year in year 1 post commissioning period for that transmission investment project  $i$  and similar expressions shall be construed accordingly.

“transmission network revenue”

means the aggregate of revenue in the relevant year derived by the licensee from the provision of transmission network services and from remote transmission asset rentals.

“transmission network revenue restriction”

means special condition D2 (Restriction on Transmission Network Revenue), and such parts of special conditions D3 to D10 inclusive as are ancillary thereto, all as from time to time modified or replaced in accordance therewith or

pursuant to sections 11, 14 or 15 of the Act.

“transmission network services”

shall have the same meaning as set out in standard condition C1 (Interpretation of Section C) (and for the avoidance of doubt shall not include excluded services or balancing services activity).

“user maintenance”

means maintenance by a user of connections in operation before the grant of this licence.

2. In this special condition and in special conditions D2 to D10 inclusive, all revenue shall be measured on an accruals basis, after deduction of value added tax (if any) and any other taxes based directly on the amounts so derived.
3. Any term used in the formulae appearing in special conditions D2 to D10 inclusive, and defined for the purposes of those formulae shall have the same meaning if used in any other formulae in those other special conditions.
4. In this special condition and in special conditions D2 to D10, any cost, charge, payment or amount may either be positive or negative.

**Appendix 3 – Proposed drafting of Scottish Hydro Electric Transmission Ltd special condition J4**

**Special Condition J4 – Restriction of transmission charges: Allowed pass-through items**

1. The purpose of this condition is to provide for revenue adjustments to reflect certain costs that can be passed through to consumers as part of allowed transmission owner revenue.
2. For the purposes of paragraph 3 of special condition J2 (Restriction of transmission charges: revenue from transmission owner services)  $PT_t$  is derived from the following formula:

$$PT_t = LF_t + RB_t + IAT_t + TPD_t$$

Where

$LF_t$  means the licence fee revenue adjustment term, whether of a positive or of a negative value, as derived from the formula set out in paragraph 3.

$RB_t$  means the network rates revenue adjustment term, whether of a positive or of a negative value, as derived from the formula set out in paragraphs 4 to 6.

$IAT_t$  means the income adjusting event revenue adjustment term, whether of a positive or of a negative value, and shall be determined in accordance with paragraphs 7 to 9

**$TPD_t$  means the temporary physical disconnection term and shall be determined in accordance with paragraphs 10 to 11.**

**Formula for the Licence Fee Revenue Adjustment ( $LF_t$ )**

3. For the purposes of paragraph 2,  $LF_t$  is an amount calculated in accordance with the following formula:

$$LF_t = LP_t - LA_t$$

Where:

$LP_t$  is an amount in respect of licence fee payments and means the amount equal to the payments made by the licensee, in the relevant year t, in accordance with its obligations set out in standard licence condition A4 (Payments to the Authority); and

$LA_t$  is the amount of the licence fee payments allowance and has the value zero.

**Formula for the Network Rates Revenue Adjustment ( $RB_t$ )**

4. For the purposes of paragraph 2, subject to paragraph 5 below,  $RB_t$  is an amount calculated in accordance with the following formula:

$$RB_t = RP_t - RA_t$$

where:

$RP_t$  is the amount payable by the licensee, in respect of the relevant year t, in respect of network rates.

$RA_t$  is the network rates allowance, and is derived from the following formula:

$$RA_t = RV_t \times PIT_t$$

where:

$RV_t$  is the network rates allowance in 2004/05 prices, and shall take the value set out in the table below:

Relevant year t	2007	2008	2009	2010	2011
-----------------	------	------	------	------	------

commencing on 1 April					
RV <sub>t</sub>	£3,500,000	£3,500,000	£3,500,000	£3,500,000	£3,500,000

PIT<sub>t</sub> shall take the same meaning as given in paragraph 3 of special condition J2 (Restriction of transmission charges: revenue from transmission owner services)

5. From the relevant year commencing 1 April 2010 RB<sub>t</sub> shall take the value zero, unless otherwise directed by the Authority on or before 31 March 2010.
6. For the purposes of paragraph 5 of this condition, the Authority may direct that, in respect of the relevant year commencing 1 April 2010 and each subsequent relevant year, RB<sub>t</sub> be calculated in accordance with the formula set out in paragraph 4 of this condition where the Authority is satisfied that the licensee has used reasonable endeavours to minimise the amount payable for those years in respect of network rates.

***Formula for a revenue adjustment in respect of an Income Adjusting Event (IAT<sub>t</sub>)***

7. (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 is approved by it as such in accordance with paragraph 9 of this licence condition

where the event or circumstance has, for relevant year t, increased or decreased costs and/ or expenses by more than £1,000,000 (the “STC threshold amount”).

- (b) For the purpose of the relevant year t commencing on 1 April 2007 and ending on 31 March 2008 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 7(a) above:

**Table 1:**

<b>Amendment No.</b>	<b>Amendment Title</b>

8. (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 8(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 8(a) to fully assess the event to which the notice relates.
  - (c) If the Authority considers that the analysis or information provided in subparagraphs 8(b)(i) to 8(b)(iv) above is insufficient to enable both the Authority and the relevant parties referred to in subparagraph 8(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 8(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 8(f)(i) is necessary for the purposes of enabling the relevant parties to fully assess the event to which the notice relates.
9. (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 8(a) were caused or saved by an income adjusting event;
  - (ii) whether the event or circumstance has increased or decreased the relevant costs and/or expenses 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 9(a) above; or
  - (ii) if the Authority has not made a determination under paragraph 9(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 8(b)(iii); or
  - (iii) in all other cases zero, including situations where the Authority has not made a determination under paragraph 9(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 8(b) and/or 8(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 8(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.

**Formula for the Temporary Physical Disconnection Term (TPDt)**

- 10. For the purposes of paragraph 2, for the relevant year  $t$  commencing 1 April 2007,  $TPD_t$  shall be an amount equal to the interruption payments charged by the system operator to the transmission licensee in accordance with the STC in respect of the period commencing 1 April 2005 and ending 31 March 2008.**
- 11. For the relevant year  $t$  commencing 1 April 2008 and each subsequent relevant year  $t$ ,  $TPD_t$  shall be an amount equal to the interruption payments charged by the system operator to the transmission licensee in accordance with the STC within each respective relevant year  $t$ .**

**Appendix 4 - Proposed drafting of Scottish Hydro Electricity Transmission  
Ltd special condition J1**

**Special Condition J1 - Restriction of Transmission Charges (Definitions)**

1. In this condition and in special conditions J2 to J11 inclusive and in schedule A to C:

“allowed pass-through items”	means the items referred to in special condition J4 (Restriction of transmission charges: Allowed pass-through items).
“allowed transmission owner revenue”	means: (a) in the relevant year commencing 1 April 2007 and every subsequent relevant year the revenue calculated in accordance with the formula set out in paragraph 3 of special condition J2 (Restriction of transmission charges: revenue from transmission owner services); and (b) in the relevant year preceding 1 April 2007, the revenue calculated in accordance with the formula set out in paragraph 1 of special condition J (Restriction of transmission charges) of this licence in the form in which it was in force at 31 March 2007.
"average specified rate"	means the average of the daily base rates of Barclays Bank plc current from time to time during the period in respect of which the calculation falls to be made.
“base transmission revenue”	means the revenue calculated in accordance with the formula set out in paragraph 3 of special condition J2 (Restriction of transmission charges: revenue from transmission owner services).

“BETTA”	means the British electricity trading and transmission arrangements which are provided for in Chapter 1 of Part 3 of the Energy Act 2004
" charge restriction conditions"	means Special Conditions J1 to J11 inclusive together with Schedules A to C to this licence, as from time to time modified or replaced in accordance with the provisions of the Act.
"excluded services"	means those services provided by the licensee as part of its transmission business which in accordance with the principles set out in Part A of Schedule A (Supplementary provisions of the charge restriction conditions), fall to be treated as excluded services.
<b>“interruption payment”</b>	<b>means, for the purposes of paragraph 10 and 11 of special condition J4 (Restriction on Transmission Charges: Allowed Pass-through Items), have the same meaning as set out in section 11 of the Connection and Use of System Code provided for in paragraph 2 of standard condition C10.</b>
“logged up costs”	means: <ul style="list-style-type: none"> <li>(c) for the purposes of paragraphs 3 and 4 of special condition J2 (Restriction of transmission charges: revenue from transmission owner services), those capital expenditure and operating expenditure costs incurred by the licensee in respect of those items referred to in those paragraphs; and</li> <li>(d) for the purposes of paragraphs 3 and 7 of special condition J7 (Capital Expenditure</li> </ul>

	Incentive and Safety Net), the capital expenditure incurred by the licensee in respect of those items referred to in those paragraphs.
"metered"	means in relation to any quantity of units of electricity transmitted, as measured by a meter installed for such purpose or (where no such meter is installed) as otherwise reasonably calculated.
"network rates"	means: <ul style="list-style-type: none"> <li>(a) in England and Wales, the rates payable by the licensee in respect of hereditaments on the Central Rating Lists (England and Wales) compiled under section 52 of the Local Government Finance Act 1988; and</li> <li>(b) in Scotland, the rates payable by the licensee in respect of any land and heritages on the Valuation Rolls compiled under the Local Government Scotland Act 1975, the Local Government etc (Scotland) Act 1994, or any legislation amending or replacing those enactments</li> </ul>
"notified value"	means, in relation to any term, such value as the Secretary of State shall ascribe to that term in a written notice given to the licensee as soon as practicable after the date of grant of this licence.
"outage change"	has the meaning given in Schedule A.
"regulated transmission revenue"	means the revenue (measured on an accruals basis) derived from the provision of transmission owner services (including to any separate business, other than the transmission business) in the relevant year, after deduction

	of value added tax (if any) and any other taxes based directly on the amounts so derived.
"relevant year"	means a financial year commencing on or after 1 April 1990.
"relevant year t"	means that relevant year for the purposes of which any calculation falls to be made.
"relevant year t-1"	means the relevant year immediately preceding relevant year t or, in respect of the period prior to 1 April 1990, the period of 12 calendar months commencing on 1 April 1989; and similar expressions shall be construed accordingly.
TIRG relevant year $t$	means, in relation to each transmission investment project $i$ specified in Schedule C, the relevant year in which a revenue allowance falls to be made under Special Condition J3 (Restriction of transmission charges: Transmission Investment for Renewable Generation) with respect to that transmission investment project $i$ : <ul style="list-style-type: none"> <li>(a) <math>t=p</math> means the relevant year commencing on 1 April 2005;</li> <li>(b) <math>t=p</math> to <math>t=-1</math> means the preconstruction period (where <math>p \leq -1</math>);</li> <li>(c) <math>t=0</math> means the relevant year in which construction of that transmission project <math>i</math> commences;</li> <li>(d) <math>t=0</math> to <math>t=n</math> means the construction period;</li> <li>(e) <math>t=n</math> means the relevant year in which that transmission investment project <math>i</math> is commissioned;</li> <li>(f) <math>t=n+1</math> means the relevant year in year 1 post commissioning period for that transmission investment project <math>i</math> and similar expressions shall be construed</li> </ul>

accordingly.

"transmission owner services"

means all services provided as part of the transmission business other than excluded services.

"unit"

means a kilowatt hour.

**Appendix 5 - Proposed drafting of Scottish Power Transmission Ltd special condition J4**

**Special Condition J4 – Restriction of transmission charges: Allowed pass-through items**

1. The purpose of this condition is to provide for revenue adjustments to reflect certain costs that can be passed through to consumers as part of allowed transmission owner revenue.
2. For the purposes of paragraph 3 of special condition J2 (Restriction of transmission charges: revenue from transmission owner services)  $PT_t$  is derived from the following formula:

$$PT_t = LF_t + RB_t + IAT_t + TPD_t$$

Where

$LF_t$  means the licence fee revenue adjustment term, whether of a positive or of a negative value, as derived from the formula set out in paragraph 3.

$RB_t$  means the network rates revenue adjustment term, whether of a positive or of a negative value, as derived from the formula set out in paragraphs 4 to 6.

$IAT_t$  means the income adjusting event revenue adjustment term, whether of a positive or of a negative value, and shall be determined in accordance with paragraphs 7 to 9.

**$TPD_t$  means the temporary physical disconnection term and shall be determined in accordance with paragraphs 10 to 11.**

**Formula for the Licence Fee Revenue Adjustment ( $LF_t$ )**

3. For the purposes of paragraph 2,  $LF_t$  is an amount calculated in accordance with the following formula:

$$LF_t = LP_t - LA_t$$

Where:

$LP_t$  is an amount in respect of licence fee payments and means the amount equal to the payments made by the licensee, in the relevant year t, in accordance with its obligations set out in standard licence condition A4 (Payments to the Authority); and

$LA_t$  is the amount of the licence fee payments allowance and has the value zero.

**Formula for the Network Rates Revenue Adjustment ( $RB_t$ )**

4. For the purposes of paragraph 2, subject to paragraph 5 below,  $RB_t$  is an amount calculated in accordance with the following formula:

$$RB_t = RP_t - RA_t$$

where:

$RP_t$  is the amount payable by the licensee, in respect of the relevant year t, in respect of network rates.

$RA_t$  is the network rates allowance, and is derived from the following formula:

$$RA_t = RV_t \times PIT_t$$

where:

$RV_t$  is the network rates allowance in 2004/05 prices, and shall take the value set out in the table below:

Relevant year t commencing on 1 April	2007	2008	2009	2010	2011
$RV_t$	£12,500,000	£12,500,000	£12,500,000	£12,500,000	£12,500,000

$PIT_t$  shall take the same meaning as given in paragraph 3 of special condition J2 (Restriction of transmission charges: revenue from transmission owner services)

5. From the relevant year commencing 1 April 2010  $RB_t$  shall take the value zero, unless otherwise directed by the Authority on or before 31 March 2010.
6. For the purposes of paragraph 5 of this condition, the Authority may direct that, in respect of the relevant year commencing 1 April 2010 and each subsequent relevant year,  $RB_t$  be calculated in accordance with the formula set out in paragraph 4 of this condition where the Authority is satisfied that the licensee has used reasonable endeavours to minimise the amount payable for those years in respect of network rates.

***Formula for a revenue adjustment in respect of an Income Adjusting Event ( $IAT_t$ )***

7. (a) An income adjusting event in relevant year t may arise from any of the following:
  - iv) an event or circumstance constituting force majeure under the STC;
  - v) 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

- vi) an event or circumstance other than listed above which is, in the opinion of the Authority, an income adjusting event and is approved by it as such in accordance with paragraph 9 of this licence condition

where the event or circumstance has, for relevant year t, increased or decreased costs and/ or expenses by more than £1,000,000 (the “STC threshold amount”).

- (b) For the purpose of the relevant year t commencing on 1 April 2007 and ending on 31 March 2008 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 7(a) above:

**Table 1:**

Amendment No.	Amendment Title

- 8. (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 8(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 8(a) to fully assess the event to which the notice relates.

(c) If the Authority considers that the analysis or information provided in subparagraphs 8(b)(i) to 8(b)(iv) above is insufficient to enable both the Authority and the relevant parties referred to in subparagraph 8(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 8(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 8(f)(i) is necessary for the purposes of enabling the relevant parties to fully assess the event to which the notice relates.
  
- 9. (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 8(a) were caused or saved by an income adjusting event;
  - (ii) whether the event or circumstance has increased or decreased the relevant costs and/or expenses 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 9(a) above; or
  - (ii) if the Authority has not made a determination under paragraph 9(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 8(b)(iii); or

- (iii) in all other cases zero, including situations where the Authority has not made a determination under paragraph 9(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 8(b) and/or 8(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 8(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.

**Formula for the Temporary Physical Disconnection Term (TPD<sub>t</sub>)**

- 10. For the purposes of paragraph 2, for the relevant year  $t$  commencing 1 April 2007,  $TPD_t$  shall be an amount equal to the interruption payments charged by the system operator to the transmission licensee in accordance with the STC in respect of the period commencing 1 April 2005 and ending 31 March 2008.**
- 11. For the relevant year  $t$  commencing 1 April 2008 and each subsequent relevant year  $t$ ,  $TPD_t$  shall be an amount equal to the interruption payments charged by the system operator to the transmission licensee in accordance with the STC within each respective relevant year  $t$ .**

**Appendix 6 - Proposed drafting of Scottish Power Transmission Limited  
special condition J1**

**Special Condition J1 - Restriction of Transmission Charges (Definitions)**

1. In this condition and in special conditions J2 to J11 inclusive and in schedule A to C:

“allowed pass-through items”	means the items referred to in special condition J4 (Restriction of transmission charges: Allowed pass-through items).
“allowed transmission owner revenue”	means: (c) in the relevant year commencing 1 April 2007 and every subsequent relevant year the revenue calculated in accordance with the formula set out in paragraph 3 of special condition J2 (Restriction of transmission charges: revenue from transmission owner services); and (d) in the relevant year preceding 1 April 2007, the revenue calculated in accordance with the formula set out in paragraph 1 of special condition J (Restriction of transmission charges) of this licence in the form in which it was in force at 31 March 2007.
"average specified rate"	means the average of the daily base rates of Barclays Bank plc current from time to time during the period in respect of which the calculation falls to be made.
“base transmission revenue”	means the revenue calculated in accordance with the formula set out in paragraph 3 of special condition J2 (Restriction of transmission charges: revenue from transmission owner services).

“BETTA”	means the British electricity trading and transmission arrangements which are provided for in Chapter 1 of Part 3 of the Energy Act 2004
" charge restriction conditions"	means Special Conditions J1 to J11 inclusive together with Schedules A to C to this licence, as from time to time modified or replaced in accordance with the provisions of the Act.
"excluded services"	means those services provided by the licensee as part of its transmission business which in accordance with the principles set out in Part A of Schedule A (Supplementary provisions of the charge restriction conditions), fall to be treated as excluded services.
<b>“interruption payment”</b>	<b>means, for the purposes of paragraph 10 and 11 of special condition J4 (Restriction on Transmission Charges: Allowed Pass-through Items), have the same meaning as set out in section 11 of the Connection and Use of System Code provided for in paragraph 2 of standard condition C10.</b>
“logged up costs”	means: <ul style="list-style-type: none"> <li>(e) for the purposes of paragraphs 3 and 4 of special condition J2 (Restriction of transmission charges: revenue from transmission owner services), those capital expenditure and operating expenditure costs incurred by the licensee in respect of those items referred to in those paragraphs; and</li> <li>(f) for the purposes of paragraphs 3 and 7 of special condition J7 (Capital Expenditure</li> </ul>

	Incentive and Safety Net), the capital expenditure incurred by the licensee in respect of those items referred to in those paragraphs.
"metered"	means in relation to any quantity of units of electricity transmitted, as measured by a meter installed for such purpose or (where no such meter is installed) as otherwise reasonably calculated.
"network rates"	means: <ul style="list-style-type: none"> <li>(c) in England and Wales, the rates payable by the licensee in respect of hereditaments on the Central Rating Lists (England and Wales) compiled under section 52 of the Local Government Finance Act 1988; and</li> <li>(d) in Scotland, the rates payable by the licensee in respect of any land and heritages on the Valuation Rolls compiled under the Local Government Scotland Act 1975, the Local Government etc (Scotland) Act 1994, or any legislation amending or replacing those enactments</li> </ul>
"notified value"	means, in relation to any term, such value as the Secretary of State shall ascribe to that term in a written notice given to the licensee as soon as practicable after the date of grant of this licence.
"outage change"	has the meaning given in Schedule A.
"regulated transmission revenue"	means the revenue (measured on an accruals basis) derived from the provision of transmission owner services (including to any separate business, other than the transmission business) in the relevant year, after deduction

	of value added tax (if any) and any other taxes based directly on the amounts so derived.
"relevant year"	means a financial year commencing on or after 1 April 1990.
"relevant year t"	means that relevant year for the purposes of which any calculation falls to be made.
"relevant year t-1"	means the relevant year immediately preceding relevant year t or, in respect of the period prior to 1 April 1990, the period of 12 calendar months commencing on 1 April 1989; and similar expressions shall be construed accordingly.
TIRG relevant year $t$	means, in relation to each transmission investment project $i$ specified in Schedule C, the relevant year in which a revenue allowance falls to be made under Special Condition J3 (Restriction of transmission charges: Transmission Investment for Renewable Generation) with respect to that transmission investment project $i$ : <ul style="list-style-type: none"> <li>(g) <math>t=p</math> means the relevant year commencing on 1 April 2005;</li> <li>(h) <math>t=p</math> to <math>t=-1</math> means the preconstruction period (where <math>p \leq -1</math>);</li> <li>(i) <math>t=0</math> means the relevant year in which construction of that transmission project <math>i</math> commences;</li> <li>(j) <math>t=0</math> to <math>t=n</math> means the construction period;</li> <li>(k) <math>t=n</math> means the relevant year in which that transmission investment project <math>i</math> is commissioned;</li> <li>(l) <math>t=n+1</math> means the relevant year in year 1 post commissioning period for that transmission investment project <math>i</math> and similar expressions shall be construed</li> </ul>

accordingly.

"transmission owner services"

means all services provided as part of the transmission business other than excluded services.

"unit"

means a kilowatt hour.