

To: Scottish Hydro Electric Transmission plc

NOTICE UNDER SECTION 11A(2) OF THE ELECTRICITY ACT 1989

The Gas and Electricity Markets Authority (the Authority) hereby gives notice pursuant to section 11A(2) of the Electricity Act 1989 (the Act), as follows:

1. The Authority proposes to modify the electricity transmission licence held by Scottish Hydro Electric Transmission plc ("the licensee") (Company number: SC213461) granted or treated as granted under section 6(b) of the Act by amending:
 - Special Condition 2M (Specification of Network Replacement Outputs).
2. The reason why the Authority proposes to make this modification is to formalise the specification of the licensee's Network Replacement Output targets for the end of RIIO-T1. The licensee was required under paragraph 2M.3 of Special Condition 2M to submit proposed values for Table 1 of Special Condition 2M within 30 days of 1 April 2013. The licensee has complied with this requirement and the Authority has determined that the values in Table 1 of Special Condition 2M should be those proposed by the licensee. These are set out in Annex A.
3. The effect of the proposed modifications is to specify the Network Replacement Outputs the licensee must deliver during the Price Control Period to assist the Authority in assessing any incentive reward or penalty associated with material over or underdeliveries against those outputs.
4. Details of the proposed modifications to Special Condition 2M are outlined in Annex A. Annex B contains the full text of the proposed Special Condition 2M.
5. A copy of the proposed modification and other documents referred to in this Notice have been published alongside this Notice and are available on the Ofgem website (www.ofgem.gov.uk).
6. Any representations with respect to the proposed licence modification must be made on or before 25 July 2014 to Neill Guha, Ofgem, Office of Gas and Electricity Markets, 9 Millbank, London, SW1P 3GE or by email to: neill.guha@ofgem.gov.uk.
7. All responses will normally be published on Ofgem's website. However, if respondents do not wish their response to be made public then they should clearly mark their response as not for publication. Ofgem prefers to receive responses in an electronic format so that they can easily be published on the Ofgem website.
8. If the Authority decides to make the proposed modification it will take effect not less than 56 days after the decision is published.

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Paul Branston

**Associate Partner, Costs and Outputs, Smarter Grids and Governance
Duly authorised on behalf of the Gas and Electricity Markets Authority**

27 June 2014

Annex A: Proposed modifications to Special Condition 2M. Specification of Network Replacement Outputs

- In paragraph 2M.2 of Special Condition 2M, replace “Table 1: Network Replacement Outputs” with the following table:

Table 1: Network Replacement Outputs

Asset categories		Units	Asset distribution based on Replacement Priority at 31 March 2021			
			Replacement Priority (where RP1 is highest risk category)			
			RP1	RP2	RP3	RP4
400KV Network						
1	Circuit Breaker	Units	0	0	0	0
2	Transformer	Units	0	0	0	0
3	Reactors	Units	0	0	0	0
4	Underground Cable	Km	0.0	0.0	0.0	0.0
5	OHL conductor	Km	0	0	0	0
6	OHL fittings	Km	0	0	0	0
7	OHL towers	Units	0	0	0	0
275KV Network						
1	Circuit Breaker	Units	1	0	0	81
2	Transformer	Units	10	0	0	16
3	Reactors	Units	0	0	0	7
4	Underground Cable	Km	0.0	0.0	0.0	4.3
5	OHL conductor	Km	0	0	0	1649
6	OHL fittings	Km	0	0	0	1649
7	OHL towers	Units	0	0	0	2550
132KV Network						
1	Circuit Breaker	Units	4	2	0	201
2	Transformer	Units	2	8	1	141
3	Reactors	Units	0	0	0	0
4	Underground Cable	Km	0.0	0.0	9.6	83.6
5	OHL conductor	Km	56	124	187	2800
6	OHL fittings	Km	0	0	0	3166
7	OHL towers	Units	0	0	0	8462

- Delete paragraph 2M.3.

The wording of 2M.3 to be deleted:

“The licensee must submit proposed values for the terms A1,A2,A3,A4,B1,B2,B3,B4,C1,C2,C3,C4,D1,D2,D3,D4,E1,E2,E3,E4,F1,F2,F3,F4,G1,G2,G3,G4,H1,H2,H3,H4,I1,I2,I3,I4,J1,J2,J3,J4,K1,K2,K3,K4,L1,L2,L3,L4,M1,M2,M3,M4,N1,N2,N3,N4,O1,O2,O3,O4,P1,P2,P3,P4,Q1,Q2,Q3,Q4,R1,R2,R3,R4,S1,S2,S3,S4,T1,T2,T3,T4,U1,U2,U3 and U4 within 30 days of 1 April 2013. The Authority will determine values for these terms taking account of this submission.”

3. Renumber paragraph 2M.4 and subsequent paragraphs as well as the related cross-references.
4. Add “, and the allowed expenditure associated with them” at the end of paragraph 2M.1
5. Replace “Network Output” with “Network Replacement Output” in: paragraph 2M.3(c) (two occurrences), paragraph 2M.5, Part B heading, and paragraph 2M.6(a).
6. In Part C heading, replace “expenditure” with “revenue”.
7. In paragraph 2M.9, split words “revenue” and “in”, add word “in” before “accordance” and delete “ below”.
8. Add “Part D: Allowed expenditure for Network Replacement Outputs” to specify the licensees allowed expenditure on non-load related capex over RIIO-T1 as set out in RIIO-T1 Final Proposals¹.

¹ ‘RIIO-T1: Final Proposals for SP Transmission Ltd and Scottish Hydro Electric Transmission Ltd, Final Decision – Supporting Document’, Table 4.7, pg 29. Available online: <http://www.ofgem.gov.uk/Networks/Trans/PriceControls/RIIOT1/ConRes/Documents1/SPTSHETLFPsupport.pdf>

Annex B: Special Condition 2M. Specification of Network Replacement Outputs

Introduction

2M.1 The purpose of this condition is to specify the Network Replacement Outputs the licensee must deliver during the Price Control Period, and the incentive reward or penalty associated with material over or underdeliveries against those outputs, and the allowed expenditure associated with them.

Part A: Specification of Network Replacement Outputs

2M.2 Subject to paragraph 2M.3 of this condition, by the end of the Price Control Period the licensee must deliver the Network Replacement Outputs in accordance with the specifications set out in Table 1.

Table 1: Network Replacement Outputs

Asset categories		Units	Asset distribution based on Replacement Priority at 31 March 2021			
			Replacement Priority (where RP1 is highest risk category)			
			RP1	RP2	RP3	RP4
400KV Network						
1	Circuit Breaker	Units	0	0	0	0
2	Transformer	Units	0	0	0	0
3	Reactors	Units	0	0	0	0
4	Underground Cable	Km	0.0	0.0	0.0	0.0
5	OHL conductor	Km	0	0	0	0
6	OHL fittings	Km	0	0	0	0
7	OHL towers	Units	0	0	0	0
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5	OHL conductor	Km	56	124	187	2800
6	OHL fittings	Km	0	0	0	3166
7	OHL towers	Units	0	0	0	8462

- 2M.3 The licensee shall also be deemed to have delivered a particular Network Replacement Output for the purposes of paragraph 2M.2 of this condition, notwithstanding a failure to meet the relevant specifications in Table 1 of this condition, if by the end of the Price Control Period:
- (a) it delivers an equivalent level of risk to the Network Replacement Output specified in Table 1 of this condition (a “materially equivalent output”); or
 - (b) it delivers the Network Replacement Output or a materially equivalent output to a lower level of risk than that set out in Table 1 of this condition, but that overdelivery is justified in accordance with the RIIO Principles (a “justified material overdelivery”); or
 - (c) it delivers the Network Replacement Output or a materially equivalent output to a higher level of risk than that set out in Table 1 of this condition, or delivers neither the Network Replacement Output or a materially equivalent output, but that underdelivery is justified in accordance with the RIIO Principles (a “justified material underdelivery”).
- 2M.4 The Authority shall assess the licensee’s performance under paragraphs 2M.2 and 2M.3 of this condition in accordance with the process set out in Part B of this condition for the purposes of determining whether adjustments should be made to allowed expenditure in the second price control period (to commence 1 April 2021) in accordance with the principles set out in the table in Part C of this condition.
- 2M.5 In assessing whether the licensee should be deemed to have delivered a particular Network Replacement Output under paragraph 2M.3 of this condition the Authority will, amongst other things, take account of any trade-offs between asset categories which the licensee is able to demonstrate has or are likely to deliver an equivalent or better set of Network Replacement Outputs to those specified in Table 1 of this condition.

Part B: Procedure for assessing Network Replacement Outputs and associated Price Control Allowed Expenditure Adjustments

- 2M.6 By 31 July 2021 the licensee must provide a report to the Authority (the “Performance Report”) setting out the extent to which it has complied with paragraph 2M.2 of this condition, including (as relevant) detailed explanations together with supporting evidence as to why the licensee considers that it has delivered:
- (a) a Network Replacement Output in accordance with the relevant specifications set out in Table 1;
 - (b) any materially equivalent outputs;
 - (c) any justified material overdelivery; or
 - (d) any justified material underdelivery.
- 2M.7 The licensee must provide such further analysis or information, and in accordance with such timescales, as the Authority considers is reasonably necessary to enable it to undertake its assessment for the purposes of its determination under paragraph 2M.5 of this condition.
- 2M.8 A determination by the Authority under Part B of this condition will be of no effect unless the Authority has first:
- (a) given notice to the licensee and to any other interested parties that it proposes to make the determination:

- (i) stating the reasons for and the effects of its proposed determination; and
 - (ii) specifying the time (which must not be less than a period of 56 days) within which representations concerning the proposed determination may be made; and
- (b) considered any representations in response to the notice that are duly made and not withdrawn.

Part C: Principles for determining adjustments to allowed revenue

2M.9 The Authority will determine whether adjustments should be made to allowed revenue in the second price control period (to commence 1 April 2021) in accordance with the principles set out in Table 2.

Table 2: Treatment of under- and over-delivery of Network Replacement Outputs

Incentives	Justified	Unjustified
Material over-delivery	<p>Cost of over-delivery shall be included in the second price control period allowances</p> <p>The financing cost incurred by the licensee in advancing investment shall be reimbursed</p> <p>Reward of 2.5 per cent of the additional costs associated with the material overdelivery</p>	<p>Cost of over-delivery shall be included in the second price control period allowances</p> <p>The licensee shall incur the financing cost of earlier investment</p>
Under-delivery	<p>Cost of under-delivery shall be excluded from the second price control period allowances</p> <p>The licensee shall benefit from the financing cost of delayed investment</p>	<p>Cost of under-delivery shall be excluded from the second price control period allowances</p> <p>The benefit arising to the licensee from the financing cost of delayed investment shall be clawed back</p> <p>Penalty of 2.5 per cent of the avoided costs associated with the material underdelivery</p>

Part D: Allowed expenditure for Network Replacement Outputs

2M.10 The allowed expenditure figures to deliver the Network Replacement Outputs are set out in Table 3. These allowances have been reflected in the licensee’s Opening Base Revenue Allowance, set against the licensee’s name in Appendix 1 to Special Condition 3A (Restriction of Transmission Network Revenue).

Table 3: Allowed expenditure for Network Replacement Outputs

Relevant Year	Allowed expenditure (£m 2009/10 prices)
2013/14	21.723
2014/15	20.127
2015/16	23.109
2016/17	27.430
2017/18	28.617
2018/19	28.986
2019/20	31.337
2020/21	27.765