

To: National Grid Electricity Transmission plc

(Company Number: 02366977)

SP Transmission Ltd

(Company Number: SC189126)

Scottish Hydro Electric Transmission plc

(Company Number: SC213461)

(each a "licensee")

28 DAYS NOTICE UNDER PART B OF SPECIAL CONDITION 5A (GOVERNANCE OF ET1 PRICE CONTROL FINANCIAL INSTRUMENTS) OF EACH ELECTRICITY TRANSMISSION LICENCE ISSUED UNDER SECTION 6(1)(b) OF THE ELECTRICITY ACT 1989

Impact Assessment

1. Special Condition 5A (Governance of ET1 Price Control Financial Instruments) ("SC5A") of the electricity transmission licence provides that the Gas and Electricity Markets Authority ("the Authority") will give notice of an intended modification of the ET1 Price Control Financial Instruments (the "Price Control Financial Model" and the "Financial Handbook") if, having carried out the assessment set out in Part A of SC5A, the Authority considers that the intended modification would not be likely to have a significant impact on the licensee or any of the other persons referred to in paragraph 5A.4 of SC5A.
2. The Authority considers that the intended modification of the PCFM and Financial Handbook, specified in paragraphs 3 and 4 of this Notice, would not be likely to have a significant impact on the licensee or any of the other persons referred to in paragraph 5A.4 of SC5A, in particular because:
 - a) the amendments referred to in paragraph 3(a) and 3(b) of this Notice are minor modelling and labelling changes;
 - b) the amendments referred to in paragraph 3(c) and 4(a) of this Notice are consequential to the modification of NGET's Special Licence Condition 7D (Arrangements for the recovery of SO uncertain costs), which are being consulted upon separately. The changes to the Financial Handbook explain how the new Electricity Market Reform variable value (SOEMRES) will be updated for the annual iteration process. Amendments to the Financial Handbook will only be made if the modifications to Special Condition 7D are proceeded with following the separate consultation; and
 - c) the amendments referred to in paragraph 4(b) of this Notice are not expected to change the actual level of deficit repair payments made, but rather align the Pension Scheme Established Deficit (PSED) with a value considered to be more reasonable by both the licensee and the Authority.

PCFM Modifications

3. The Authority proposes to modify the Price Control Financial Model (PCFM) referred to in paragraph 1 by:
 - a) amending the annual spread of the Legacy Allowed Revenue (LAR) calculation, which is currently hard coded, to:
 - spread the initial legacy revenue dynamically once the cost of debt has been updated; and

- correct the Weighted Average Cost of Capital (WACC) used to spread legacy revenue;
- b) renaming SHETL to SHE-Transmission; and
- c) enabling National Grid Electricity Transmission Plc (NGET) to recover costs for activities it undertakes as the Electricity Market Reform (EMR) Delivery Body, through the new uncertainty mechanism SOEMRES.

The amendments set out in paragraphs 3(a) to (c) of this Notice are considered necessary to ensure that the correct calculation of values for the term MOD are used in the formula for Base Transmission Revenue set out in Special Condition 3A (Restriction of Transmission Network Revenue), and are produced for each Transmission Network under the Annual Iteration Process for the PCFM.

Financial Handbook Modification

4. The Authority proposes to modify the Financial Handbook referred to in paragraph 1 by:
- a) including the new uncertainty mechanism SOEMRES, as a part of updating SO variable values for the annual iteration process, which enables NGET to recover costs for activities it undertakes as the Electricity Market Reform (EMR) Delivery Body; and
 - b) allowing a mutually agreed deficit value to be substituted for the PSED, if the agreed value is considered by Ofgem and the licensees to be more appropriate.
5. The amendment set out in paragraph 4(a) of this Notice is considered necessary, in order to set out the process for updating the PCFM for the new uncertainty mechanism SOEMRES. The amendments specified in paragraph 4(b) of this Notice are considered necessary to reflect that there may be in some circumstances, a more appropriate value than the existing PSED to use for the purposes of the calculations in the Financial Handbook. This is to ensure that the value that Ofgem and the licensees consider to be the most appropriate is used.
6. The proposed modifications to the PCFM and the Financial Handbook are detailed in Appendices 1, 2 and 3 of this Notice, which consist of:
- a) an oak report setting out the modifications to the PCFM (Appendix 1);
 - b) a copy of the PCFM incorporating the modifications (Appendix 2); and
 - c) a modified Financial Handbook (Appendix 3).
7. Copies of this Notice and other documents referred to in it are available on the Ofgem website (www.ofgem.gov.uk).

Now therefore

8. In accordance with paragraph 5A.9 of SC5A, the Authority hereby gives 28 days' notice to the licensee that it proposes to make modifications to the ET1 Financial Instruments of the licensee as set out in paragraphs 3 and 4 of this Notice above.

9. Any representations on the proposed modifications to the PCFM and Financial Handbook must be made on or before the 15th August 2014, which is 28 days from the date of this Notice, to: Gareth Wu, Regulatory Finance Team, Office of Gas and Electricity Markets, 9 Millbank, London, SW1P 3GE or by email to gareth.wu@ofgem.gov.uk.
10. The proposed modification will take effect from 15 September 2014.
11. 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 form so they can be placed easily on the Ofgem website.



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Ian Rowson
Associate Partner, Regulatory Finance and Compliance
Smarter Grids and Governance
Duly authorised on behalf of the
Gas and Electricity Markets Authority
18 July 2014