

## To interested parties

### **Notice, under Part D of Special Condition 3L (Pre-construction Engineering Outputs for prospective Strategic Wider Works) of the Electricity Transmission Licence, of a proposal to direct modifications to Table 1 in Part A of that condition in order to amend details of Pre-Construction Engineering Outputs**

1. Scottish Hydro Electric Transmission plc (the "licensee") is the holder of an Electricity Transmission Licence (the "licence") granted or treated as granted under section 6(1)(b) of the Electricity Act 1989.
2. Under Special Condition 3L (Pre-construction Engineering Outputs for prospective Strategic Wider Works) of the licence ("SC 3L"), the Gas and Electricity Markets Authority (the "Authority"<sup>1</sup>), may direct modifications to Table 1 in Part A of SC 3L ("Table 1") in order to amend details of Pre-construction Engineering ("PE") Outputs.
3. In accordance with Part C(i) of SC 3L, the licensee has given notice that there has been a significant change in the future outlook for generation connections or demand requirements and that to deliver certain PE Outputs in Table 1 is no longer economical and efficient.
4. In accordance with Part C(ii) of SC 3L, the Authority has determined that certain Output Substitutions to the PE Outputs in Table 1 are justified and it has determined the adjustments to be given effect through modifications to Table 1.
5. In accordance with Part D of SC 3L, the Authority hereby gives notice that it proposes to direct the modifications to Table 1 that are specified in Appendix 1 to this Notice. The proposed modifications are shown in tracked changes. The Authority proposes that this direction should take effect on 28 May 2018.
6. The reasons for our proposed direction are set out in Appendix 2.
7. In summary, the effect of the modifications we propose to direct will be to alter the details of the PE Outputs that the licensee is required to deliver during the RIIO-ET1 period and to specify the allocation of associated Allowed Expenditure to the outputs.

### **Further information**

8. Copies of this Notice and other documents referred to in it are available on the Ofgem website ([www.ofgem.gov.uk](http://www.ofgem.gov.uk)). Alternatively they are available from our Research and Information Centre, 9 Millbank, London, SW1P 3GE (020 7901 7003).
9. Any representations on our proposal to make this direction must be made on or before 18 May 2018 to Anthony Mungall at Ofgem, 3rd Floor, Commonwealth House, 32 Albion Street, Glasgow, G1 1LH, or by email to [Anthony.Mungall@ofgem.gov.uk](mailto:Anthony.Mungall@ofgem.gov.uk).
10. You can ask us to keep your response confidential, by clearly marking it confidential and providing reasons, and we'll respect this, subject to obligations to disclose information such as the Freedom of Information Act 2000 or the Environmental Information Regulations 2004. However, we would like to publish as much of your response as we can. To help us achieve this goal we would appreciate it if confidential material could be provided in a separate appendix to your main response. This should also be clearly marked as confidential with reasons provided.

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<sup>1</sup> The "Authority", "Ofgem", "we" and "our" may be used interchangeably in this document. The Office of Gas and Electricity Markets (Ofgem) supports the Authority in its day to day work.

Unless you mark your response confidential we'll publish it on our website,  
www.ofgem.gov.uk, and put it in our library.

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**Steven McMahon, Associate Partner RIIO Networks, Electricity**  
**Duly authorised on behalf of the Authority**

**11 April 2018**

## Appendix 1:

### Modifications to Table 1 in Part A of Special Condition 3L of Scottish Hydro Electric Transmission plc's electricity transmission licence

#### Part A: Baseline expenditure for Pre-construction Engineering Outputs

**Table 1: Baseline expenditure for Pre-construction Engineering Outputs**

| <b>Prospective Strategic Wider Works</b>  | <b>Baseline expenditure<br/>£m (2009/10 prices)</b> |
|---|---|
| <del>Beauly — Blackhillock 275kV</del>  | <del>0.528</del>                                    |
| <del>Orkney Isles</del>   | <del>13.840</del>                                   |
| <del>Caithness Moray B0/B1 Boundary Reinforcement Phase 1<br/>(Caithness Moray)</del>   | <del>2.270</del> <u>5.764</u>                       |
| <del>Shetland link</del>  | <del>0.400</del> <u>7.569</u>                       |
| <del>400kV East Coast</del>   | <del>1.449</del>                                    |
| <del>Inner Hebrides HVDC (Islay)</del>  | <del>7.000</del>                                    |
| <del>Errochty Reconfiguration</del>   | <del>0.165</del>                                    |
| <del>Kintore — Tealing (XT1 / XT2)</del>  | <del>1.056</del>                                    |
| <del>Beauly — Keith 400kV B0/B1 Boundary Reinforcement Phase 2</del>  | <del>13.350</del> <u>4.993</u>                      |
| <del>Eastern HVDC — second circuit B2/B4 Boundary Reinforcement<br/>Eastern Onshore, Eastern Offshore, reactive support</del> | <del>9.800</del> <u>14.723</u>                      |
| <u>Prospective future Strategic Wider Works Pre-construction<br/>Engineering Outputs</u>                                      | <u>9.547</u>  |
| <del>Future design costs</del>  | <del>15.700</del>                                   |
| <del>Two public planning enquiries</del>  | <del>2.000</del>                                    |
| <u>Kintyre Hunterston</u>   | <u>1.151</u>  |
| <u>Outer Hebrides (Western Isles and Lewis)</u>   | <u>9.971</u>  |

## Appendix 2: Reasons for direction

1. This appendix explains our determination on a pre-construction engineering (PE) output substitution request<sup>1</sup> received from the licensee and a related amendment to reallocate the allowed expenditure.
2. We allowed £67.6 million<sup>2</sup> in the RIIO-ET1 price control for the licensee to deliver engineering activities in preparation of constructing infrastructure projects expected to be considered under the Strategic Wider Works (SWW) arrangements.<sup>3</sup> The deliverables from these pre-construction activities are known as PE Outputs. Further detail on the PE Outputs is included in Part A of SC 3L.
3. The licensee can raise a request to amend the details of the PE Outputs prescribed in the licence through an output substitution (OS) request. When we receive a request we determine whether the proposed substitution is consistent with the licence requirements and whether it is justified as being economic and efficient, and then the modification to be made to the licence, including the allocation of the allowed expenditure.
4. The table on the following page summarises the key details of the OS request received from the licensee, covering five categories:
  - i. no change to the description or to the allocation of allowed expenditure.
  - ii. re-specification of allowed expenditure associated with the delivery of an existing output.
  - iii. removal of an output where the associated pre-construction activity is no longer required.
  - iv. consolidation of two existing outputs into a single output category to cover activities not directly associated with a specific prospective SWW output.
  - v. introduction of new outputs and reallocation of the allowed expenditure made available as a result of steps ii, iii and iv above. Categories of new output have been defined in terms of:
    - a) activities focussed on the scoping of specific transmission boundary reinforcements on the licensee's system within RIIO-ET1, and
    - b) activities required in preparation of constructing specific projects currently expected to be considered under the SWW arrangements within RIIO-ET1.
5. Appendix 3 sets out further background information on the SWW arrangements.

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<sup>1</sup> Submitted in accordance with paragraph 9 of SC 3L of the licence.

<sup>2</sup> Up to a total of £67.558 million (2009/10 prices) can be spent by the licensee during RIIO-ET1.

<sup>3</sup> Under these arrangements, TOs are able to initiate a regulatory assessment of a proposal for the construction design of a major reinforcement project by providing a notice to us. More detail on the SWW arrangements is available from our website: <https://www.ofgem.gov.uk/publications-and-updates/guidance-strategic-wider-works-arrangements-electricity-transmission-price-control-riio-t1-0>

**Table 1: summarising the licensee's OS request<sup>4</sup>**

| Driver | Current PE Outputs            | Current allowed expenditure | Description of proposal                                     | Proposed allowed expenditure | £m change |
|--------|-------------------------------|-----------------------------|---|------------------------------|-----------|
| i.     | Orkney Isles                  | 13.840                      | No change   | 13.84                        | -         |
| ii.    | Shetland link                 | 0.400                       | No change   | 7.569                        | +7.169    |
| iii.   | Inner Hebrides HVDC (Islay)   | 7.000                       | Scheme terminated   | -                            | -7.000    |
| iv.    | Future design costs           | 15.700                      | Prospective future SWW Pre-construction Engineering Outputs | 9.547                        | -8.153    |
| iv.    | Two public planning inquiries | 2.000                       |   |                              |           |
| va.    | Caithness Moray               | 2.270                       | B0/B1 boundary reinforcement Phase 1                        | 5.764                        | +3.494    |
| va.    | Beaully-Blackhillock 275kV    | 0.528                       | B0/B1 boundary reinforcement Phase 2                        | 4.993                        | -8.885    |
| va.    | Beaully-Keith 400kV           | 13.350                      | B2/B4 boundary reinforcement                                | 14.723                       | +2.253    |
| va.    | 400kV East Coast              | 1.449                       |   |                              |           |
| va.    | Errochty Reconfiguration      | 0.165                       |   |                              |           |
| va.    | Kintore Tealing (XT1/XT2)     | 1.056                       |   |                              |           |
| va.    | Eastern HVDC – second circuit | 9.800                       |   |                              |           |
| vb.    | -                             | -                           | Kintyre Hunterston  | 1.151                        | +1.151    |
| vb.    | -                             | -                           | Outer Hebrides (Western Isles and Lewis)                    | 9.971                        | +9.971    |
|        |                               | <b>£67.558m</b>             |   | <b>£67.558m</b>              | <b>0</b>  |

**The licensee's current PE Outputs**

6. Under the price control framework, the licensee is required to put forward a well-justified business plan setting out what it anticipates delivering during the price control period. We assessed this plan as part of the making of the price control settlement.
7. In its business plan, the licensee identified clusters of prospective transmission reinforcements in their 'best view'<sup>5</sup> plan that it considered suitable for future consideration under the SWW arrangements for delivery during the RIIO-ET1 period.
8. Appendix 4 provides an overview of the various clusters of reinforcement schemes which form the basis of the licensee's current funding allowance for SWW pre-construction activities during the RIIO-ET1 period.<sup>6</sup>
9. A total pre-construction allowed expenditure of £67.558m was set to enable the licensee to deliver agreed PE Outputs across the following range of activities:
  - subsea links to Shetland and Orkney isles
  - upgrades to specific electricity transmission network boundaries
  - connection of offshore wind located in the Inner Hebrides
  - provision for future design works and potential public planning inquiries

<sup>4</sup> All financial values shown are in 2009-10 prices.

<sup>5</sup> An estimate of total expenditure (totex) based on a central scenario of the generation and demand background changes as well as connection activity.

<sup>6</sup> Appendix 4 also includes planned reinforcements which were in development and the licensee expected construction activities to commence prior to the RIIO-ET1 period, and no provision for pre-construction funding was requested.

10. In broad terms, the outputs were focussed on the delivery of activities to include: routing, siting and optioneering studies, project design, environmental assessments, technical specifications for cost tenders, and planning consents.
11. The total value of the allowed expenditure available to fund pre-construction activities is fixed.

### **Developments since 1 April 2013**

12. The development of the licensee's electricity transmission network has been impacted by a number of factors since the finalisation of the RIIO-ET1 settlement. In particular, changes to the generation outlook for offshore and island generators along with a changing background for delivery of transmission boundary upgrades have altered the drivers that existed at the time of the RIIO-ET1 submission. This has resulted in the licensee re-evaluating its approach to development of certain schemes. In some cases this has led to some works being delayed indefinitely and additional works in the development of other schemes.

#### *Links to connect the Scottish islands to the mainland transmission network (island links)*

13. The licensee's planned island links are dependent on connection applications from specific generation schemes that can underwrite the liabilities and associated security requirements needed to secure capacity on future transmission links.
14. Development of island generation schemes has been impacted by uncertainty over the commercial viability of the wind and marine generation schemes on all of the Scottish islands within existing electricity generation support frameworks.<sup>7</sup>
15. The OS request confirms that the continuing uncertainty over financial viability has had an impact on the progress of the proposed transmission links to the islands. This has resulted in delays and changes to the scope of pre-construction engineering activities associated with the development of the island links.
16. In the case of the proposed Shetland link, the uncertainty has resulted in the requirement for additional pre-construction activity and expenditure, including further detailed design and survey works. As a result, the licensee proposes to increase the value of pre-construction allowed expenditure within RIIO-ET1 associated with the delivery of the associated PE Output.
17. The licensee planned for the proposed transmission link to the Western Isles to be in the construction phase by the start of the RIIO-ET1 period. Pre-construction activities associated with the development of the project were therefore not included within the initial funding for the current price control period. The licensee has confirmed that the scheme has not reached the level of maturity expected, due to the uncertainty surrounding the support frameworks described above. However there has been activity to further develop the scope of the proposed project; an optioneering exercise has been undertaken and a competitive tender for the link is currently underway.
18. The licensee has confirmed its intention to add pre-construction activity associated with the development of the proposed Western Isles transmission link project to the PE Outputs specified in Table 1 of SC 3L.
19. In the case of the Orkney transmission link, the contracted position on Orkney has changed dramatically with the termination of some marine developments in recent years. It continues to change with the emergence of new potential generation

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<sup>7</sup> Including: Contracts for Difference, Feed-in-Tariffs and the Renewables Obligation.

schemes. As a consequence the licensee is re-evaluating the connection options. However, until the assessment process is complete the licensee is proposing no change under the OS request to the existing level of allowed expenditure to deliver the associated PE Output.

20. The licensee proposes to fund the additional costs of the proposed Western Isles and Shetland transmission link PE Outputs (a combined value of £17.14m) by re-allocating a proportion of the value made available from the proposed reductions in the allowed expenditure allocation for the following PE Outputs.

- Future Design Costs PE Output (re-specified as part of the "Prospective Future Strategic Works" PE Output)
- Beaully-Keith 400kV PE Output (re-specified as part of the 'phase 2' works deemed necessary to upgrade the B0/B1 boundary PE Output), and
- Inner Hebrides HVDC (Islay) PE Output (scheme cancelled).

21. The licensee has confirmed that the proposed OS relevant to the Western Isles and Shetland PE Outputs does have an implication for other PE Outputs; the newly formed "Prospective Future Strategic Wider Works" PE Output category and the newly formed "B0/B1 boundary reinforcement Phase 2".

#### *Transmission boundary upgrades*

22. A total pre-construction allowance was fixed on the basis of the portfolio of projects in the licensee's original business plan. An element of this allowed expenditure was based on clusters of schemes that the licensee anticipated would be required to upgrade boundaries<sup>8</sup> on the transmission network at the time of finalising its business plan. The clusters originally identified are summarised in Appendix 4.

23. The OS request confirms that the drivers that existed at the time of the RIIO-ET1 submission have significantly changed since finalisation of the business plan. The following factors have impacted the overall level of future generation:

- reductions in the level of island generation, offshore wind generation and marine generation anticipated to connect during the RIIO-ET1 period
- changes in the operating regime of the Peterhead power station, the effect of which is to increase the available capacity across eastern boundaries
- a change in the central generation modelling background scenario used to reflect a lower confidence level in the future anticipated level of new generation

24. The OS request proposes to re-specify elements of the allowed expenditure on a boundary reinforcement basis rather than a specific scheme basis. The revisions are briefly summarised below.

- 1) To cluster the existing allowed expenditure associated with three existing named schemes into two separate PE Outputs covering the pre-construction works associated with upgrade work across the B0/B1 boundaries. These outputs have been redefined in terms of:
  - a. activities focussed on the completed pre-construction works associated with phase 1 of the boundary upgrade work (Caithness Moray, CM), and

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<sup>8</sup> The licensee has five transmission boundaries. These boundaries are used to determine the power transfer capability across each geographical region in its transmission area. For example, B0 is the mainland area north of Beaully (including Orkney and Shetland) and B4 forms the interface between SHE Transmission's system and the SPT network in the south of Scotland.

- b. activities focussed on the delivery of the ongoing works associated with phase 2 of the proposed boundary upgrade work (Beauly-Keith and Beauly-Blackhillock).

- 2) To cluster the existing allowed expenditure associated with four schemes into a single PE Output covering the pre-construction works associated with upgrade works across the B2/B4 boundaries.

25. These are briefly discussed in turn below.

#### *B0/B1 phase 1 works: CM project*

26. The licensee has confirmed the successful delivery of the pre-construction outputs for the CM scheme; it is now in the construction phase. The expenditure incurred in the delivery of the associated PE Output has exceeded the existing allowed expenditure provision. Additional pre-construction activity has been driven by extended evaluation of technical options (to incorporate future connection of the Shetland scheme) and additional site investigation and ground condition assessment work (reducing civil construction costs).
27. The OS request proposes to re-specify the PE Output for the CM scheme as 'phase 1' of the works deemed necessary to upgrade the B0/B1 boundary and to increase the allowed expenditure for such works to reflect the cost of additional pre-construction activity undertaken since the commencement of RIIO-ET1.
28. The licensee proposes to fund the additional costs by re-allocating a proportion of the value made available by the proposed reduction in the allowed expenditure allocation for the PE Outputs described in paragraph 20.

#### *B0/B1 phase 2 works*

29. Preliminary routing and optioneering works commenced in 2014 to identify potential design solutions for the B0/B1 boundary reinforcement works between Beauly – Keith/Blackhillock.
30. The licensee has confirmed that activity on these schemes is currently on hold in line with the most recent analysis of future network requirements (Network Options Assessment, "NOA").
31. The licensee is currently of the view that a future NOA process may provide a direction to develop a reinforcement across the B0/B1 boundaries. The OS request proposes to include provision to fund future development costs in the event that the NOA provides a signal to proceed with pre-construction activity during the RIIO-ET1 period.
32. The proposed allowed expenditure for the PE Output associated with the phase 2 work (£4.993m) is lower than the original allowed expenditure allocation for the Beauly – Keith/Blackhillock schemes combined (£13.878m).
33. In summary, the OS request proposes to:
  - re-specify the PE Outputs for the separate named schemes into a single category reflecting 'phase 2' works deemed necessary to upgrade the B0/B1 boundary
  - reallocate allowed expenditure associated with the separate named schemes to the new single PE Output. The reduction in funding provision reflects the reduced activity to date, driven by the current 'on hold' status of the underlying schemes,



and a small provision for future costs associated with progressing potential upgrade works across the remaining RIIO-ET1 period

- make available the residual value of allowed expenditure to the delivery of other PE Outputs.

34. The licensee has confirmed that the proposed OS relevant to the B0/B1 boundary upgrade PE Outputs (phase 1 and phase 2) does have an implication for other PE Outputs.

#### *B2/B4 boundary*

35. The licensee's original business plan identified schemes that would provide increased capacity across the B2/B4 transmission boundary. Two of these schemes – '400kV East Coast' upgrade and 'Eastern HVDC I' subsea cable scheme – were originally identified as the first stage in upgrading the boundary capacities with the anticipation that both schemes would commence either before, or during, the first year of the RIIO-ET1 period.

36. A pre-construction allowance for the 400kV East Coast scheme was included in Table 1 of SC 3L to recognise the anticipated overlap of pre-construction activities into the RIIO-ET1 period.

37. There was recognition that future upgrades would be required and future provision was requested and made for pre-construction funding for the development of three additional named schemes ('Eastern HVDC second circuit'<sup>9</sup>, 'Kintore – Tealing XT1/XT2' and 'Errochty Reconfiguration'). Provision was made to fund pre-construction works for these named projects in Table 1 of SC 3L.

38. At the beginning of the RIIO-ET1 price control it became clear that both the 400kV East Coast and Eastern HVDC 1 schemes had not progressed as quickly as anticipated. A further detailed optioneering exercise was undertaken in 2013/14, in conjunction with the other onshore transmission owners (TOs)<sup>10</sup> to determine a co-ordinated strategy for upgrade across all three network areas. This concluded that, based on the expected future generation levels, the original scope of boundary work was no longer robust. The revised recommendation was that a staged reinforcement strategy should be adopted for the provision of additional capacity across the B2/B4 boundaries.

39. Stage 1 of the revised upgrade strategy was focussed on Scottish onshore reinforcements (including the 400kV East Coast upgrade). A key aspect of the onshore reinforcement optioneering recognised that the development of an integrated approach involves an assessment of multiple transmission configurations to determine the optimal solution. As a consequence, named schemes in the business plan (Kintore – Tealing and Errochty Reconfiguration) are now assessed as part of the overall onshore reinforcement strategy and, therefore, these schemes will no longer be separately identified as individual schemes in Table 1 of SC 3L.

40. Stage 2 of the revised B2/B4 boundary reinforcement strategy includes the possibility of a constructing a subsea HVDC link for delivery beyond RIIO-ET1 timescales. The approach recognises that the Eastern HVDC I scheme has not progressed in line with the original business plan expectation and that pre-

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<sup>9</sup> Intended to follow on from the completed Eastern HVDC I scheme.

<sup>10</sup> There are currently three owners of onshore electricity transmission networks, each known as a "TO": National Grid Electricity Transmission (NGET), which owns the England and Wales transmission system; Scottish Power Transmission (SPT), which owns the network in the South of Scotland; and Scottish Hydro Electric Transmission (SHE Transmission), which owns the network in the North of Scotland.

construction activity associated with this scheme has continued within the RIIO-ET1 period.

41. The licensee has also confirmed that the named scheme in the Table 1 (Eastern HVDC second circuit) will no longer be developed during the RIIO-ET1 period and will no longer be identified as part of the overall strategy for the reinforcement of the B2/B4 boundary.
42. The NOA process is now in place to provide an annual review of all strategic transmission schemes including the requirements for the eastern B2/B4 boundary upgrades. The most recent NOA (2017) has indicated a requirement for both stage 1 and stage 2 reinforcements during the RIIO-ET2 period. As a result, the licensee currently anticipates a requirement for ongoing pre-construction activities covering both onshore and offshore options. The exact spend and split will be determined from the NOA recommendations.
43. The OS request proposes to increase the allowed expenditure associated with the delivery of pre-construction activities to upgrade the B2/B4 boundary from £12.470m to £14.723m. The licensee proposes to fund the additional costs by re-allocating a proportion of the value made available by the proposed reduction in the allowed expenditure allocation for the PE Outputs described in paragraph 20.
44. In summary, the OS request proposes to:
  - re-specify the PE Outputs for the current individual named schemes as a single category reflecting the pre-construction works deemed necessary to upgrade the eastern B2/B4 boundary.
  - re-allocate the existing allowed expenditure from the separate named schemes to the new PE Output, and
  - increase to the allowed expenditure value of the new boundary-specific PE Output to reflect:
    - the actual costs incurred to progress onshore reinforcement activities incurred to date<sup>11</sup>, and
    - the forecast of costs to be incurred in progressing onshore and offshore pre-construction works associated with the B2/B4 boundary upgrade across the remaining RIIO-ET1 period.
45. The licensee has confirmed that the proposed OS relevant to the B2/B4 boundary upgrade PE Output does have an implication for other PE Outputs.

#### *Kintyre Hunterston*

46. At the time of finalising the RIIO-ET1 settlement, the expectation from the licensee was that the Kintyre Hunterston (KH) project would be in the construction phase by the time RIIO-ET1 commenced. A needs case was submitted in January 2013, a project assessment consultation was carried out during July 2013 and we published a decision on the overall project in November 2013<sup>12</sup>.
47. The submission and subsequent approval dates were later than had been anticipated by the licensee and as a result additional pre-construction expenditure was incurred during the reporting year 2013/14. The majority of the additional pre-construction

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<sup>11</sup> This includes pre-construction activity on the following projects: 400kV East Coast upgrade, the Errochty reconfiguration and the Eastern HVDC I subsea link.

<sup>12</sup> <https://www.ofgem.gov.uk/electricity/transmission-networks/critical-investments/strategic-wider-works/kintyre-hunterston>

expenditure was associated with ground investigation work. Additional expenditure has also been incurred following an overall review of the generation position in Argyll and to review potential options for a third subsea link and other potential onshore reinforcements. The outcome of this review has been to establish a preferred way forward on the phased onshore reinforcement.

48. The licensee proposes to introduce a new category of PE Output associated with the delivery of the KH project and an allowed expenditure value of £1.151m. The licensee proposes to fund the cost by re-allocating a proportion of the value made available from the proposed reduction in the allowed expenditure allocation for the PE Outputs described in paragraph 20.
49. The licensee has confirmed that the proposed OS relevant to the KH PE Output does have an implication for other PE Outputs.

#### *Inner Hebrides HVDC (Islay)*

50. The Inner Hebrides scheme was included in the RIIO-ET1 business plan to accommodate connection of offshore wind schemes around Islay. The OS request confirms that the original drivers that existed at the time of the RIIO-ET1 submission have significantly altered; terminations mean that there are currently no contracted schemes which trigger the requirement for a transmission link to this region. As a result, the proposed investment and associated PE Output, as described in Table 1 of SC 3L, are not currently forecast to be required in RIIO-ET1.

#### *Two planning enquiries*

51. Table 1 of SC 3L contains a specific PE Output to reflect the original expectation that costs may be incurred by the licensee in the progression of public inquiry proceedings associated with the construction of new tower structures in the licensee's transmission area.
52. The licensee has confirmed that no inquiry has yet been triggered and that no expenditure is currently forecast to be incurred within the RIIO-ET1 period.
53. The OS request proposes to remove this specific output category and to incorporate the value of allowed expenditure into a single generic PE Output category. This is further discussed in the next section.

#### *Future design costs*

54. Table 1 of SC 3L contains a funding provision for potential costs that may be incurred by the licensee in carrying out future pre-construction work on schemes yet to be identified within RIIO-ET1. The rationale for this PE Output category was to recognise that a number of schemes were at a very early stage of development and that some were expected to reach sufficient maturity in RIIO-ET1 to require pre-construction activities for a prospective SWW project.
55. The OS request proposes to re-title the PE Output and to reduce the value of the allowed expenditure allocated to this category. The proposed reduction in the level of funding provision reflects an updated view on the likely number and value of potential costs the licensee may incur within the remaining RIIO-ET1 period.
56. For the avoidance of doubt, we expect the licensee to raise future OS request(s) in the remainder of the RIIO-ET1 period as and when there is sufficient clarity on prospective SWW projects (or instigation of a planning inquiry) to enable the licensee to allocate the residual value of allowed expenditure to deliver specific projects.

57. In response to our queries, the licensee has confirmed that there are no ongoing or immediate activities that necessitate the use of the residual value of allowed expenditure. We note also that paragraph 17 of SC 3L sets out the ability to adjust baseline expenditure in the event that the licensee does not deliver or only partially delivers a PE Output. This means that potential non-delivery of the prescribed PE Outputs, including the generic output, and the associated level of allowed expenditure, will be further considered as part of the RIIO-ET1 'close out' process.
58. We will continue discussions with the licensee on how to ensure transparency in the reporting and monitoring of relevant pre-construction expenditure against the PE Outputs.
59. It is our current understanding that if no further OS request is received from the licensee to reallocate the allowed expenditure associated with the PE Output entitled "Prospective future Strategic Wider Works Pre-construction Engineering Outputs" an adjustment to baseline expenditure will be made to reflect the full value of the funding provision.

#### *General*

60. As set out in our January 2018 update on competition in electricity transmission<sup>13</sup>, SWW projects in RIIO-ET1 will be assessed against the criteria for competition. Where they meet these criteria we will assess the suitability of alternative regulatory models to SWW that seek to introduce, or replicate the benefits of, additional competition to the delivery of these projects. Projects included in this OS will still be subject to this assessment.

#### **Our review of the licensee's OS request**

61. To assess the licensee's OS request we have reviewed the main submission and supporting material, as well as supplementary responses provided by the licensee to our follow up queries.
62. We have examined the information provided in the OS request to verify that the scope and quality of the information meets the requirements set out in part B and part C of SC 3L. We then looked at the costs of the main activities and/or deliverables involved in each project to get a break down of total pre-construction costs to ensure these are economical and efficient.
63. We used supporting information provided by the licensee about the scope of tasks included in each activity to determine the specific costs incurred in relation to progressing only pre-construction works. We sought additional information in instances where the breakdown of common activity was not sufficiently explained.
64. We have concluded our cost assessment. Based on the information provided we are satisfied that the estimated pre-construction costs are economic and efficient.

#### **Our determination**

65. Having completed our review of the licensee's submission, we have determined that it is consistent with the OS notice requirements under SC 3L. We are also satisfied, based on the supporting evidence provided, that the estimate of the efficient costs of the alternative PE Outputs are reasonable.

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<sup>13</sup> [https://www.ofgem.gov.uk/system/files/docs/2018/01/nti\\_january\\_2018\\_publications\\_1.pdf](https://www.ofgem.gov.uk/system/files/docs/2018/01/nti_january_2018_publications_1.pdf)

### **Appendix 3: Background to the Strategic Wider Works arrangements**

Transmission projects to strengthen or extend the electricity transmission system are known as 'wider works' outputs in RIIO-ET1. In general, these works are triggered by a combination of different generation connections and are required to increase the capacity or extend the network.<sup>14</sup> As part of RIIO-ET1 we specified the amount of money that the owners of onshore electricity transmission networks (the "TOs") can spend and recover from consumers for the delivery of wider works outputs.<sup>15</sup>

In business plans developed for the price control review, the TOs identified some very large projects that may be needed during the RIIO-ET1 price control period. However, there was some uncertainty as to whether the prospective projects would actually be required as the reinforcements were dependent on factors outside the direct control of the TOs, including generation market developments and the impact on customer-driven requirements.

To help manage this uncertainty we included Strategic Wider Works (SWW) arrangements as part of the price control settlement to allow the TOs to propose very large network developments and additional funding during RIIO-ET1.

The SWW arrangements help ensure decisions are made when sufficient information is available about the drivers, timing and efficient costs of delivering transmission projects. They enable us to apply proportionate scrutiny, on a case-by-case basis, to our assessment of wider reinforcements proposed by the TOs. This helps to manage uncertainty and helps to ensure value for money for consumers by ensuring that the scope of projects are justified and can be progressed at the most appropriate time.<sup>16</sup>

#### *Construction and pre-construction activities for prospective SWW projects*

In RIIO-ET1 Final Proposals we set out that the scope of allowed expenditure for new outputs determined under the SWW framework would only cover the total costs of the construction works associated with the completed asset. Costs associated with pre-construction activities were excluded from this assessment.

A separate licence provision (SC 3L) was developed to complement the SWW arrangements with the aim of providing relatively small levels of funding for pre-construction activity. This approach was intended to address a potential problem that a lack of up-front funding for pre-construction activities could have a disproportionate impact and delay the development of new large reinforcement options needed to facilitate the expected growth in renewable connections.

The funding approach for pre-construction activity was therefore developed to provide certainty on a level of ex-ante funding to progress preparatory work deemed necessary to develop the scope of the proposed reinforcement, without requiring approval from us.

At a high level, the delivery of pre-construction activities is considered necessary to the preparation of large-scale construction activities – it is expected to contribute to defining the required scale and timing of construction work. The deliverables are therefore expected to support the achievement of high quality submissions for a prospective SWW projects for regulatory approval.

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<sup>14</sup> Works will increase electricity transfer capability across system boundaries, or within system boundaries, in accordance with the Security and Quality of Supply Standard (SQSS).

<sup>15</sup> Electricity transmission licence special conditions 6I and 6J.

<sup>16</sup> The transmission licensees have a duty to develop and maintain an efficient, co-ordinated and economical transmission network. Therefore it is for a licensee to decide when it is the right time to initiate a new project.

**Appendix 4:** Overview of planned transmission projects and allocation of SWW Pre-Construction Funding

