

# Governance Document

## Net Zero and Re-opener Development Fund Governance Document

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### Overview:

This Governance Document is for the Net Zero and Re-opener Development Fund use it or lose it allowance ("NZARD UIOLI"), referred to under Special Condition 3.5 of the Electricity Transmission Licence and the Gas Transporter Licence.

The purpose of the NZARD UIOLI is to enable Network Licensees to fund small Net Zero facilitation projects, and also to allow for early development work on projects that network companies intend to bring forward at a later stage through other RIO-2 Net Zero-related mechanisms.

This Governance Document sets out the detailed arrangements for this allowance, including scope and maximum spend available. Network Licensees are required to comply with this document under their NZARD UIOLI licence condition.

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## Context

In December 2020, we published our Final Determinations<sup>1</sup> for the RIIO-2 price control for the Electricity Transmission (ET), Gas Distribution (GD) and Gas Transmission (GT) sectors for 2021 to 2026. This included our approach to uncertainty around developments during the price control period in respect of Net Zero.

To enable necessary development work on Net Zero projects and the progression of low-regret Net Zero facilitation capital projects for the gas sector, we introduced the Net Zero and Re-opener Development Fund use-it-or-lose-it allowance ("NZARD UIOLI").

This followed feedback that our uncertainty mechanisms framework as set out at Draft Determinations left a funding gap for the early development work that Network Licensees need to do on projects that they may bring forward through re-openers. Respondents also highlighted that there was a funding gap for very small Net Zero facilitation projects in the gas sectors that may be low in materiality but high in impact and consumer value.

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<sup>1</sup> <https://www.ofgem.gov.uk/publications-and-updates/riio-2-final-determinations-transmission-and-gas-distribution-network-companies-and-electricity-system-operator>.

See Chapter 8 of the RIIO-2 Final Determinations Core Document for specific information on the NZARD Fund UIOLI.

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## 1. Introduction

### **The Net Zero and re-opener development allowance**

1.1. The NZARD UIOLI is a RIIO-2 fund designed to enable small gas Net Zero facilitation capital projects and to allow early development work on projects that network companies may bring forward under the following re-openers:

- ET, GT, and GD – Net Zero Re-opener
- GT and GD only - Net Zero Pre-construction and Small Projects Re-opener (NZASP)
- GD only – Heat Policy re-opener, and New Large Load Re-opener (if Net Zero related)
- ET only – Medium Sized Investment Projects (MSIP) Re-opener

1.2. The NZARD Licence Condition provides the following total allowances for Network Licensees:

- NGET - £16.0m
- SHET - £12.0m
- SPT - £12.0m
- Cadent - £19.8m
- NGN - £4.5m
- SGN - £10.8m
- WWU - £4.7m
- NGGT - £8.3m

1.3. These allowances are available to be spent over the price control period. The Network Licensee can manage the profile of its spending, so it does not need to spend its total allowance equally over each year of the price control.

### **NZARD UIOLI Governance Document**

1.4. This document is the NZARD UIOLI Governance Document issued under Special Condition 3.5 of the Electricity Transmission and Gas Transporter licences (the “NZARD Licence Condition”). It sets out the regulation, governance and administration of the NZARD UIOLI.

1.5. In this document we use the terms ‘Ofgem’ and ‘the Authority’ as well as the terms ‘we’, ‘us’ and ‘our’ interchangeably. Ofgem is the Office of the Gas and Electricity Markets. The Authority is the Gas and Electricity Markets Authority and is the governing body of Ofgem, consisting of non-executive and executive members.

- 1.6. Defined terms are capitalised throughout the text, with the definitions set out in chapter 4.
- 1.7. In this document “Network Licensee” means the holder of an Electricity Transmission Licence, or a Gas Transporter Licence in relation to its gas distribution or gas transmission activities, regulated through the RIIO price control framework.

### **Compliance**

- 1.8. Network Licensees are required to comply with this governance document in accordance with Special Condition 3.5 in the Gas Transporter License and Electricity Transmission Licence.

### **Review**

- 1.9. Ofgem may from time to time, following consultation with Network Licensees and other interested parties, revise this NZARD UIOLI governance Document in accordance with Part B of Special Condition 3.5.

## 2. Allowable NZARD Expenditure

- 2.1. Expenditure under the NZARD UIOLI allowance may be incurred in relation to two broad areas:
- **small Net Zero facilitation capital projects** in the GD and GT sectors; and
  - **early development work** on projects that Network Licensees intend to bring forward under specific re-openers<sup>2</sup> across the ET, GD and GT sectors.
- 2.2. This chapter sets out the specific types of work that are included under the above areas, which constitute 'allowable RDF expenditure'<sup>3</sup> and any restrictions on Network Licensees using the allowance.
- 2.3. The use of this fund does not involve an up-front process of Ofgem approving projects, however, if Ofgem finds that a project does not meet the requirements set out in this document, we reserve the right to claw back the associated funding.

### **Small Net Zero facilitation capital projects (GD and GT only)**

- 2.4. The NZARD allowance may be used to fund low and no regret capital projects in the GD and GT sectors that have a high Net Zero impact but are not captured by other mechanisms.
- 2.5. 'Low regret' in this context recognises that whilst there is significant uncertainty that surrounds the future of the gas networks, there are some areas the GD and GT sectors can invest in which hold relatively low policy risks – and there is a certainty of outcomes, with clear evidence of the need and benefit for consumers.
- 2.6. Low and no regret projects are those which do not expose consumers to material stranding risk due to uncertainty in Great Britain's pathways to decarbonisation, particularly in heat. This may be because the project itself has low materiality or is part of a business-as-usual upgrade (for example companies selecting a slightly higher cost option when replacing an asset to help future-proof the network for decarbonisation).
- 2.7. GD and GT Network Licensees should not use the NZARD UIOLI for Net Zero facilitation capital projects that are expected to cost more than £2m. Such projects can instead be brought

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<sup>2</sup> As per paragraph 1.1 in this document

<sup>3</sup> As per Special Condition 3.5.8 (a) in the Electricity Transmission Licence and Gas Transporter Licence

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forward under other regulatory mechanisms, such as the Net Zero pre-construction and small projects re-opener (“NZASP”) which is available to both the GD and GT sectors.

- 2.8. Where Network Licensees use their NZARD allowance for Net Zero facilitation capital projects, a common proforma must be used – which licensees must develop and agree with us. This common proforma may evolve over time and Ofgem may require changes to be made.

### **Early development work (GD, GT and ET)**

- 2.9. Network Licensees may need to undertake early development work on a project prior to a submitting a full funding request through a re-opener, but it may not have been funded to do so elsewhere in the price control. In such instances, the NZARD UIOLI may be used for early development work, such as:

- Front End Engineering Design (FEED) studies. This could include early desk-based research and design, comparison of different options and development of project plans.
- Pre-FEED work. This can also include risk assessment and establishing a needs case.
- Detailed technical design and engineering development of the chosen option.
- Work required to secure planning consent for the project, including planning consultations, wayleaves, legal costs, and planning applications.
- Associated customer and stakeholder engagement, including Local Area Energy Planning.

- 2.10. NZARD expenditure in relation to early development work should not exceed £2m per project. This will ensure that the total allowance can be used across a variety of potential projects, and that the Network Licensee’s NZARD UIOLI is never exhausted on one project (which would be especially detrimental to consumers if that project didn’t ultimately progress). Where £2m is not sufficient to cover all costs associated with early development work, Network Licensees may use the relevant RIIO-2 re-openers<sup>4</sup>. Approval of such requests will not be guaranteed and will be subject to the relevant re-opener process.

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<sup>4</sup> As per paragraph 1.1 in this document



### **3. Annual regulatory reporting for NZARD projects**

- 3.1. The reporting requirements for each Network Licensees' NZARD expenditure are set out in Condition B15 (Regulatory Instructions and Guidance) of the Electricity Transmission Licence Standard Conditions, and Condition A40 (Regulatory Instructions and Guidance) of the Gas Transporter Standard Licence Condition.
- 3.2. For GD and GT there are additional reporting requirements as per paragraph 2.7 of this document.

## 4. Definitions

Any terms used in this document and not defined below will have the same meaning as defined in Special Condition 1.1 of the Electricity Transmission Licence and the Gas Transporter Licence.

### *Heat Policy re-opener*

Means the Re-opener described in Special Condition 3.19 in the Gas Transporter Licence (Heat Policy and energy efficiency Re-opener). Created to respond to policy decisions on the future of gas and heat.

### *Medium Sized Investment Projects (MSIP) re-opener*

Means the re-opener described in Special Condition 3.14 in the Electricity Transmission Licence. An annual RIIO-ET2 re-opener which allows ETOs to bring forward funding requests for sub-£100m projects across a range of different areas, most of which are driven by third parties.

### *The Net Zero and Re-opener Development use-it-or-lose-it allowance*

Means the allowance described in Special Condition 3.5 in both the Electricity Transmission Licence and the Gas Transporter Licence (Net Zero and Re-opener Development Fund use it or lose allowance).

### *Net Zero Pre-construction and Small Projects re-opener*

Means the Re-opener described in Special Condition 3.9 in the Gas Transporter Licence (Net Zero Pre-construction Work and Small Net Zero Projects Re-opener). Created to capture pre-construction work and small value Net Zero facilitation projects.

### *Net Zero re-opener*

Means the re-opener described in Special Condition 3.6 in both the Electricity Transmission Licence and the Gas Transporter Licence. Created to allow changes in policy, the role of the network companies, as well as technological or market changes to be reflected in company allowances.

### *Network Licensee*

Means the holder of an Electricity Transmission Licence or a Gas Transporter Licence, regulated through the RIIO price control framework.

### *New Large Load re-opener*

The Re-opener described in Special Condition 3.22 in the Gas Transporter Licence. Created to increase baseline allowances to fund specific network reinforcement driven by the connection of large loads and gas producers.