

Interested parties

Direct Dial: 020 7901 7000

Email: timothy.wood@ofgem.gov.uk

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RIIO-ED1 Green Recovery Scheme – Statutory Consultation on proposed modifications to the licence conditions and Price Control Financial Instruments

In summer 2020, following the immediate response to the COVID-19 pandemic, Ofgem engaged the energy industry to consider and progress actions that could facilitate a green economic recovery while accelerating the delivery of decarbonisation benefits to energy consumers.

Significant opportunities were identified by Ofgem and the networks under an overall “Green Recovery programme”, broadly split into three main phases and initial areas of focus:

- Enabling the fastest possible ramp-up of investment programs that had required to be scaled back because of COVID-19 restrictions and prevailing Government guidelines
- Accelerating planned investment programs from future years to help reactivate supply chains and deliver earlier benefits to consumers
- Identifying appropriate opportunities to enable new, accelerated investment programs to support future energy user needs and help facilitate the delivery of Government climate change ambitions.

In February 2021 we published an Open Letter¹ covering the third area. This covered the Green Recovery Scheme for the electricity distribution networks, aimed at accelerating low regrets, shovel ready network investment under the remainder of the RIIO-ED1 price control period to 31 March 2023. The Scheme was intended to stimulate economic recovery

¹ <https://www.ofgem.gov.uk/publications-and-updates/open-letter-energy-network-association-green-recovery-scheme>

and support the faster delivery of decarbonisation benefits for consumers, while supporting Government's climate change ambitions.

The Open Letter set out the detail of the main drivers behind the approach and the proposed regulatory arrangements for the DNOs to bring forward low regrets network investment under the RIIO-ED1 price control. The proposed regulatory arrangements include using a combination of existing DNO allowances, together with new funding where existing allowances are expected to be exhausted, to support faster progress towards government decarbonisation targets.

The regulatory arrangements for the DNO Green Recovery Scheme are separate to the development of the new price controls for the electricity distribution sector (RIIO-ED2) which will start on 1 April 2023.

Following a call for evidence process and period of stakeholder engagement, each of the Distribution Network Operators (DNOs) submitted investment proposals under the Scheme for Ofgem assessment and our decisions² were published on 24 May 2021.

The purpose of this statutory licence consultation is to seek stakeholder views on the proposed modifications to the licence conditions and Price Control Financial Instruments that are required to implement the Green Recovery Scheme in line with these decisions.

The licence condition

We are proposing to insert a new licence condition, Special Condition 3N, for inclusion in each of the Electricity Distribution licences held by all electricity distribution network operators. A copy of the proposed licence condition is available alongside this letter.

Price Control Financial Instruments

The proposed modifications to the ED1 Price Control Financial Instruments introduce a new uncertainty mechanism in the ED1 Price Control Financial Model (PCFM) and the ED1 Price Control Financial Handbook (Handbook) to enable DNOs to recover costs in relation to the Green Recovery Scheme.

The proposed modifications in the ED1 PCFM and Handbook allow DNOs to recover the costs associated with the Green Recovery Scheme Projects for 2021/22 and 2022/23.

² [Decision on the RIIO-ED1 Green Recovery Scheme | Ofgem](#)

Table 1 – Location of modifications within the Model and Handbook

Model/ Handbook	Nature of Modification	Sheet reference	Cell / Page reference
PCFM	Introducing new Variable Value for Green Recovery Scheme Projects costs	Input and All licensee input sheets	Row 37
PCFM	Incorporating allocation rates for the Green Recovery Scheme expenditure allowance to feed into base revenue for all DNOs.	Input and All licensee input sheets	E273:AQ280
PCFM	Updating Variant allowances formulas on the summary table for all DNOs	Input and All licensee input sheets	E282:AQ288
PCFH	Introducing new Variable Value and new licence condition	Chapter 7/ Section 1	
PCFH	Introducing new Section of the Methodology for determining relevant adjustments in respect of Green Recovery Scheme Project Costs	Chapter 7/ Section 7 (Section 13 for SSEH and 5 for WPD)	
PCFH	Updating to include new Variable Value	Chapter 7/ Section 8 (Section 14 for SSEH and 6 for WPD)	

Reason and effects

The reason for the proposed modifications is to establish the Green Recovery Scheme and the regulatory treatment of Green Recovery Scheme expenditure as determined by Ofgem in our decision on projects proposed by DNOs.³

The licence condition

The new licence condition will provide a mechanism for excluding expenditure on Agreed Schemes from the Totex Incentive Mechanism by determining an allowed cap, equal to the sum value of all of a licensee’s Agreed Schemes (less any projected RIIO-ED1 underspend), to which the Totex Incentive Mechanism shall not apply. For DNOs who are expected to only use RIIO-ED1 underspend, the cap will be set at zero. The proposed condition also establishes a procedure by which Ofgem can direct changes to the value of Green Recovery Scheme costs to respective DNOs.

We have included in the licence condition the provision that the Authority may, at any time by giving notice to the licensee, direct an increase in the allowed Agreed Scheme costs to accommodate additional Agreed Schemes. The reason for this is to provide flexibility for

³ <https://www.ofgem.gov.uk/publications-and-updates/decision-riio-ed1-green-recovery-scheme>

new projects to be funded under the Green Recovery Scheme. We have not made a decision at present on any process that DNOs would be required to follow to submit any new projects for consideration for funding under the Green Recovery Scheme. Should we decide to do that, however, we will engage appropriately with DNOs and other stakeholders and notify them of any proposed process.

The proposed licence condition excludes expenditure on Agreed Schemes that are in excess of existing allowances and below the total cap, from the totex incentive mechanism. Expenditure on Agreed Schemes below existing allowances is also excluded from the totex incentive mechanism by virtue of reducing the licensee's underspend. There is no need for the licence condition to do anything to achieve this exclusion, it is the natural consequence of reducing the licensee's underspend. However, for the avoidance of doubt we confirm here that our clear policy intention is that expenditure on Agreed Schemes whether below or above existing allowances, so long as it is below the total cap, is excluded from the totex incentive mechanism.

Price Control Financial Instruments

The reason for the proposed modifications to the Price Control Financial Instruments is to align the PCFM and Handbook with the proposed licence condition and to enable the DNOs to recover the costs associated with Agreed Schemes.

The effect of the proposed PCFM is to introduce a new uncertainty mechanism variable value within the PCFM, which enables DNOs to recover the costs associated with Agreed Schemes without the impact of the Totex Incentive Mechanism.

The effect of the proposed Handbook modification is to introduce, in Chapter 7, the methodology for the Green Recovery Scheme mechanism which describes how the uncertainty mechanism works.

Responding to this consultation and next steps

Stakeholders are invited to provide views on the proposed modifications published alongside this letter by no later than 5pm on 25 June 2021. Responses should be sent to timothy.wood@ofgem.gov.uk, and copying in RIIO2@ofgem.gov.uk.

Subject to feedback received via this consultation, the table below provides an indicative view of the next steps towards the finalisation of the Green Recovery Scheme licence condition.

Milestones on the SIF licence	Date
Publication of this statutory consultation	28 May 2021
Deadline for responses to statutory consultation (28-day consultation)	25 June 2021
Ofgem decision to modify licence (thereafter 56-day standstill)	Early July 2021
Licence comes into effect	Early September 2021

Yours faithfully,

Steve McMahon
Deputy Director, Electricity Distribution