OFGEM

OPEN MEETING SERIES

Network Price Control

SHE Transmission (SSE)

Record of Virtual Meeting

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Transcribed by T A Reed (Wiltshire) Ltd
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ATTENDEES

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Rob McDonald	MD – Transmission, SSE plc
Aileen McLeod	Director of Business, Planning and Commercial, Transmission, SSE plc
Maz Alkirwi	Finance Director, Transmission, SSE plc
Michael Ferguson	Head of Regulation, Transmission, SSE plc
Tracy Matthews	Chair of the SHET User Group
Geoff Aitkenhead	Member of the SHET User Group
Roger Witcomb	Chair of the Challenge Group
Robert Hull	Member of the Challenge Group

JONATHAN BREARLEY: Good morning. I'm Jonathan Brearley, Chief Executive of Ofgem, and will be temporarily chairing this meeting. Thank you for joining us today at the Network Price Control Open Meeting for SHE Transmission, delayed from the spring by the impact of COVID-19.

This and similar meetings are the first of their kind for Ofgem and, despite us not being able to be in the same room, we very much encourage you to be involved as it is important that we hear a variety of voices today. I'm confident that this meeting will allow us to have an open and constructive discussion about the consultation responses and key outstanding areas of difference ahead of our final determinations which will be published later this year.

SHE Transmission has told us that the topic areas that they would like to discuss today are: theme one, allowances, so totex and business plan incentive; theme two, net zero; and theme three, a fair RIIO-T2 return.

Companies are first given the opportunity to deliver a 20-minute presentation. We also welcome today's members of the company's User Group and of Ofgem's own Challenge Group. These groups are formed of independent experts convened to review business plans in detail. They will have an opportunity to feed in their views ahead of our opening the floor for questions. It's very encouraging to see such a diversity of voices registered for today's event. Please ask your questions on the chosen topics by using the Q&A function on the side bar. I'm afraid there may not be time to answer every question, but we will consider them all when drafting our final determinations.

Members of our Ofgem senior team will also be asking some questions. We will be making a transcript and recording of this event which you will be able to watch again and will be available on our website once all meetings have taken place.

We start with the knowledge that energy networks in general have delivered a good service, but at a high cost to consumers. This is well-documented through our own and independent evidence. We also know that investment in the energy system is going to have to rise as we meet the net zero challenge at lowest cost to consumers whilst protecting the most vulnerable.

Our overall proposals unlock unprecedented funding for projects that cut carbon emissions to create a green, fair and secure energy system for consumers now and in the future. This will enable our sector to play a key role in the green recovery.

I would like now to hand over to Ofgem's Director of Networks, Akshay Kaul, who will give a brief update and set the scene in terms of where we have reached in the RIIO-2 process.

AKSHAY KAUL: Thank you, Jonathan, and a very good morning, everybody. I'd like to thank in particular colleagues from SHE Transmission, the SHE Transmission User Group, the RIIO-2 Challenge Group and all the other stakeholders who have assembled this morning for your engagement with the RIIO-2 process to date and

particularly for your thought thoughtful and extensive responses to our consultation on draft determinations which we have been reflecting upon these past few weeks.

Since we received your responses, we've had very constructive engagement through a series of technical bilaterals, industry working groups and of course supplementary questions raised directly with the companies or the relevant respondents.

As you can appreciate, we are still in the process of working up our final determination positions, but I wanted to reflect on some of the themes that SHE Transmission will go on to talk about, and in particular to give an account of the progress that has been made in our thinking since draft determinations.

I'm going to talk about totex first, or total expenditure, then about the uncertainty mechanisms. I'll touch upon the outputs and incentives package, and finally I will say something about our thoughts on finance and the cost of capital.

Starting with totex, we have had a number of bilaterals at a working level between the Ofgem teams and SHE Transmission to understand better the justification and evidence submitted for a range of investment projects proposed by SHE Transmission in their spending plan. For example, in the case of SHE Transmission's capital investment programme, we have received much stronger engineering justifications following draft determinations for some projects that we had proposed at draft determinations to disallow. Good progress has been made in assessing this additional evidence that has been submitted.

In addition, we are also actively considering SHE Transmission's data clarification and comments on our cost assessment modelling that was provided after draft determinations and which we think will have a positive impact on SHE Transmission's baseline totex allowance and its business plan incentives at final determinations.

Turning next to uncertainty mechanisms for net zero, we proposed in draft determinations a range of uncertainty mechanisms to ensure that the price control can flex and facilitate delivery of net zero. SHE Transmission were broadly supportive of this approach in their consultation response, but highlighted that these mechanisms need to be agile, flexible and responsive to support the development of net zero projects. We acknowledge and agree with the views expressed by SHE Transmission and its stakeholders that the package of uncertainty mechanisms for RIIO-2 should strike a balance between protecting consumers from less certain costs and introducing regulatory complexity. We have engaged with SHE Transmission to understand better their proposals for how we could make the uncertainty mechanism process sufficiently responsive to high levels of in-period expenditure.

We are continuing to work with all the transmission owners to ensure that the different mechanisms are fit for purpose, that they are coherent and that we actively consider possible changes to the framework that would improve their responsiveness to need. Such changes at final determinations could include providing greater

funding certainty to transmission owners at an earlier stage of the process and improving the reopener processes to ensure a timely and proportionate response from Ofgem to different types of projects that may come forward. For example, looking at our proposed reopener for large onshore transmission investment projects that are worth more than £100m, we have engaged with all the transmission owners to understand what design considerations would allow for greater flexibility in the process. We are actively considering the feedback that we have received ahead of making a firm conclusion at final determinations. Very good progress has been made in this area, but more work is required in the weeks ahead before we can arrive at a final position for final determinations.

Turning then to the outputs and incentives package, the package that we proposed for SHE Transmission at draft determinations reflected both the company's RIIO-1 performance and the information that they provided in their RIIO-2 business plan. Since then, we have received additional information and feedback on our proposed outputs and incentives package from a variety of stakeholders, including the company and their User Group. In particular, I want to highlight the constructive engagement we have had with the electricity transmission owners and the ESO on a proposed common output delivery incentive that targets reductions in system constraint costs. We are actively considering this and other potential changes to our outputs and incentives packages with the overall aim of setting an ambitious challenge for the transmission owners while delivering real value for consumers.

Turning finally to the topic of finance and the cost of capital, we have had significant engagement with SHE Transmission and other stakeholders following draft determinations to discuss the financial parameters of the package and to understand better their responses to our consultation.

We have also received and read with interest the CMA's provisional findings in the matter of PR19 in the water sector. Although these determinations, or these findings I should say, are provisional and we await the final determination, even at this stage we consider it an important contribution to the debate on the cost of capital for regulated utilities. There are likely to be areas of cross-over between the two sectors, but also other areas such as the computation of asset betas, the cost of debt allowances and the particular aiming up arguments that the CMA has used which we think would tentatively perhaps be more specific to sectoral circumstances. We would be interested in stakeholder views on the read-across of the CMA's reasoning for the energy sector.

In summary, the ongoing engagement is absolutely crucial to ensure that we have the ability to fully understand stakeholder responses and develop a robust price control which provides sufficient funding for SHE Transmission and a reliable network to create value for consumers and to play their full part in facilitating net zero. We believe that we're making excellent progress towards developing our position for final determinations and I very much look forward to hearing your reflections later this morning.

I'm going to hand back now to Jonathan to continue the discussion. Back to you, Jonathan.

JONATHAN BREARLEY: Thanks very much. Can we now hand over to SHE-T for their presentation, please.

ALISTAIR PHILLIPS-DAVIES: Hi, Jonathan, Akshay, thank you very much. Hello and good morning, everyone. I'm Alistair Phillips-Davies, the Chief Executive of SSE, and I'm joined today by the senior management team from Transmission led by Rob McDonald, our MD. I'm joined by Aileen McLeod, Director of Business, Planning and Commercial, Maz Alkirwi, who is the Finance Director, and Michael Ferguson, our Head of Regulation.

We're very pleased to be able to have the opportunity to present our plan and our views on the Ofgem draft determination today to the GEMA board and the wider community.

If we go to the next slide, please. I would like to start out by saying that we share Ofgem's ambition for RIIO-T2 and particularly what they have stated they want to achieve around net zero.

We have been engaging extensively with stakeholders to produce and refine our plan which is entitled "Network For Net Zero". It's made clear that stakeholders want a net zero consistent plan at reasonable cost, which is what we want to deliver. I think, as such, our plan is good for consumers, so we'll deliver on net zero and therefore meet Ofgem's primary objective to protect current and future consumers, and the future consumers piece I think will be important as we go forward through this.

Currently, there is a significant gap between our plan and the Ofgem draft determination and we're going to focus on where the differences are, but we obviously acknowledge what Akshay has said earlier about the work that they've done, and we're pleased that we've had such positive and strong engagement to date. I still think there is much to do to actually land what we hope will be a reasonable settlement in everyone's interests.

Next slide, please. SSE Transmission has an outstanding track record of delivery, and there's a number of points across these slides which you can take up, but I would particularly like to mention reliability, which is important for both consumers and customers, to generators; on time and under-budget projects delivery, we're a major project delivery company that has done a considerable amount of investment in recent years and done that very well and that's important for giving value to consumers. Then, finally, I'd like to at this stage call out our clear commitment to sustainability.

Earlier this year we achieved a global first in the transmission business to get accreditation for a science-based target for one and a half degree warming pathway.

We were the first and remain the only business globally to have that accreditation which makes us fully Paris-compliant. I think that's very important.

Also, finally in relation to what this business is doing for the general economy at this particular time, I would call out the huge investments we make, our ability to focus on local sourcing has made us a substantial contributor to the economy, particularly in the north of Scotland, but also more widely throughout the UK where we look to source goods, products and services.

Next slide, please. This review is around looking forward, and briefly we wanted to look forward to what this nation has to do as it starts on its goal of reaching the legally-binding target of net zero. We believe the next ten years are very important. Currently, we have eight gigawatts of renewable generation connected to our networks. We're expecting to see that approximately triple within the next ten years. We're expecting to see that more than double over the period of this price control coming up, and it's therefore essential that we start well, that we have agile and flexible mechanisms that allow us to make a really good start so that those important future consumers can look forward to actually receiving the benefits of more and more renewables and decarbonisation.

Next slide, please. As I mentioned at the start, there is a gap between the draft determination and our plan which is why we were so disappointed with it. As it stands currently, we believe that that plan will not deliver for current or future consumers. I think there were three principal reasons. Rob will go into more detail, but just briefly I'd like to set out those three areas that we think need more work.

The reduction in allowances concerns us. We are clear that they won't meet customer expectations in terms of connections. We also heard Akshay mention earlier that we're looking for improvements in the flexibility mechanisms. Those as originally presented definitely will be too slow and too cumbersome, and indeed in the case of the volume driver provide a disincentive to connect renewables generation, which surely cannot be let to stand.

Overall, this means that on the numbers within the draft determination we would not deliver net zero, something that Ofgem has committed to do publicly.

Finally on returns, again, as mentioned, we have seen in the draft determination the lowest level of returns allowed to any businesses like this internationally, lower than any other sector in the UK, overturning 25 plus years of regulatory precedent with no clear evidence provided as to why. Therefore, it's encouraging to see what has come out of the latest thinking on PR19. We see this as representing a minimum for what is required to attract international investment to this sector and not drive it elsewhere. That return under PR19, plus a premium to reflect the risks for this sector and particularly the huge challenges presented by net zero and the enormous individual construction projects that we'll have to undertake in order to deliver it, is important.

With that, I will hand over to Rob who will take you through some more detail.

ROB McDONALD: Thanks, Alistair. Yes, if we can go to slide 7, that's great, thank you.

I'm going to cover each of the three main areas of concern. As Alistair and indeed Akshay commented at the start, there has been very constructive engagement with the Ofgem team over the last few weeks. We are basing our comments today on the draft determinations as published in July as that remains the only public point of reference.

Against that background, if we take totex first, Ofgem have cut the business plan totex by £800m, or around a third of the certain view.

Before I comment on the individual areas that have been cut, I think it's worth reminding ourselves how we arrived at the business plan cost forecasts. Our plan was co-created with stakeholders after the most comprehensive engagement process we have ever undertaken. The cost estimates were based on actual costs incurred during T1, plus we set ourselves a £100m plus efficiency challenge, and those costs are presented alongside third party consultancy support. We therefore believe that this cut is unjustified, it's not supported by the evidence and will severely inhibit our ability to deliver the outputs that our stakeholders have requested.

If I now take you to the areas in turn. £338m of totex cuts relates to 14 projects which Ofgem rejected in the draft determination. Since that determination, which Akshay touched on, there has been particularly good engagement in this area with the Ofgem team and we've been told that these projects will be reinstated, which is obviously very, very welcome.

The next area is £361m of so-called efficiency cuts. We've presented evidence to the Ofgem team that £250m of this relates to what we would regard as modelling and other errors which need to be corrected in the final determination.

For the remainder, while we support Ofgem's use of benchmarks, it is important that those benchmark costs are applied to our actual expected future work programme, rather than a backward-looking assessment of previous work which will not be repeated. Making that one change alone and correcting those errors would result in reinstatement of the £361m totex disallowed from our plan.

The remainder of the totex cuts relate to pre-construction costs. Effectively, this is totex we need to develop new projects, and while we recognise that there is an element of uncertainty to this cost area, Ofgem's approach would result in us not being able to develop new projects midway through T2. This cannot be right and would stifle the connection of renewable generation. We have therefore proposed an alternative mechanism to Ofgem which would involve returning unspent totex to customers. This would, in our view, strike a much better balance with protecting customers and delivering on net zero.

The last point on the slide relates to the business plan incentive. Effectively, this is a £32m fine imposed by Ofgem because of the totex cuts highlighted above. I have to say, we find this aspect of the draft determination particularly egregious. As we've noted above, we presented a business plan that was co-created with our stakeholders and we consider that Ofgem have effectively fined us for reflecting the ambition of those stakeholders in our plan.

As an aside, we also do not understand how the mathematics work. Other companies have larger cuts to their totex but seem to have a smaller final fine, which seems very, very odd.

We would urge Ofgem to address the business plan incentive in the final determination. Otherwise, we think this will send a very strong signal that stakeholder engagement not only won't be rewarded, it might actually be penalised if Ofgem don't like the answer.

If I could ask us to turn to the next slide, please, I'd like to focus next on a pathway to net zero. Because that's the title of our business plan, it was called a "Network for Net Zero", and we called it that because our plan would demonstrably deliver net zero. We didn't just assert that; we modelled scenarios for delivering net zero and proposed a set of investments, some funded upfront, others through uncertainty mechanisms, that will deliver the volume of generation connections in our area to deliver net zero.

Let me be clear about this, our plan meets UK and Scottish government targets, and more recently the pathway generation connections set out in National Grid's future energy scenarios published earlier this year. It's also consistent with the system operators' Network Options Assessment, or NOA process, and it's also underpinned by our accreditation under the science-based target initiative. I think we've mentioned that already, we're very proud of that accreditation and I'm sure we will mention it again before the morning is out.

So, we've presented a credible and robust plan to deliver net zero at least cost. By contrast, the Ofgem draft determinations do not deliver net zero, and I say that for four reasons.

First, it is just not credible to suggest that we deliver the outputs to achieve net zero for a third less totex than the plan. That's just not possible.

Secondly, as I mentioned earlier, Ofgem have cancelled a substantial proportion of our pre-construction development spend. Effectively, this means the north of Scotland will be closed to development of any renewable generation developments midway through T2 as a consequence of that.

Third, to fund connections of renewables that are already planned, Ofgem propose a volume driver, it's a kind of pay-as-you-go mechanism. We have no issue with this in principle, but the specific model and parameters Ofgem have proposed would

result in making new renewables being significantly loss-making, providing a strong disincentive to connecting new renewable generation.

Lastly, for much of the new large infrastructure required to deliver net zero, Ofgem propose that it is funded through so-called uncertainty mechanisms. We support this, we support these as a way of balancing uncertainty, delivering on time and cost to customers. But the framework Ofgem have proposed just doesn't work, and a few examples might help make the point. For some projects, for example, we will not be able to even apply to Ofgem for additional funding until 2024, nearly the end of the T2 period. For others, Ofgem have suggested it might take the thick end of three years for a decision. This is not agile and it's far too slow to deliver the pace and trajectory of net zero investments illustrated in the graph you can see on the slide in front of you.

If I can turn to the next slide, what is needed? In each of these areas, there has been constructive dialogue with the Ofgem team, I really do want to emphasise that. In each case, we have provided an alternative approach that we constructed with Ofgem and we're always presenting alternatives solutions with supporting evidence.

In brief, we consider that Ofgem should, firstly, provide pre-construction totex that allows net zero, alongside a mechanism that protects customers by returning unused allowances.

Secondly, Ofgem should rethink the volume driver design to ensure that it is not loss-making and therefore incentivises rather than discourages timely connection of renewable generation.

Third, Ofgem should bring forward more agile uncertainty mechanisms, and in this regard we think Ofgem should allow any project for net zero to be brought forward at any time with a target maximum of six months for a decision.

Lastly, we would strongly urge Ofgem to ensure that whatever is brought forward in December is capable of delivering net zero. By that, we mean that the final determination should be modelled in detail to prove that it can deliver a pathway to net zero, including meeting UK and Scottish government targets for connection and renewables, rather than just asserting that as the case and hoping for the best.

If I can move on now to the financial package, please, it's the next slide. There's been much discussion with the Ofgem team about this, particularly in relation to the cost of equity. It's clear that if we are to deliver the ambitious targets for net zero, we will need to attract the necessary investment in a globally competitive market. We recognise that returns have fallen since the last round of price controls, given the macro-economic environment. But we consider that Ofgem's proposals are unsustainable and insufficient to attract that necessary investment.

We believe that's arisen because the overwhelming majority of the proposed reduction in the cost to equity is driven by changes to Ofgem's modelling assumptions, rather than an update to reflect market conditions. That's shown in

the slide. The waterfall chart sets out the key drivers of Ofgem's reduction in the cost of equity. The red blocks represent changes that arise because of Ofgem's methodology changes, and you can see that these represent over 80 per cent of the proposed reduction in the cost of equity. So, the overwhelming majority of the reduction in the cost of equity is driven by Ofgem's methodology and ideology, not a mathematical update, which is key throughout this to reflect market conditions.

What is needed? If we can turn to the next slide. In order to make network companies financeable and attractive to long-term investors, we would urge Ofgem to reconsider the wealth of evidence we've provided, backed up by respective economic consultants, which sets out why the methodology changes set out in the previous slide are not justified. As part of that, Ofgem will clearly need to ensure that companies are financeable in the long-term, particularly the SSE Transmission with the very high capital spend relative to our asset base.

Finally, Ofgem will also need to fully take into account the CMA's recent decision in relation to the water sector, recognising that since privatisation, energy has consistently been accepted as higher risk than water, and Ofgem has not presented any evidence to date to counter that.

If I can turn to the next slide, please, before finishing, I want to comment on stakeholders. As noted earlier, we conducted the most comprehensive stakeholder engagement exercise we have ever undertaken in developing our plan, and that engagement didn't stop after our plan was submitted. In particular, we have been overwhelmed by the response of our stakeholder community to the draft determination. Nearly 60 organisations have written to Ofgem about aspects of our plan in response to the Ofgem consultation. Some of the quotes are on the slide but there are many, many more covering a wide and diverse set of stakeholders. Our business plan was entitled a "Network for Net Zero", but it wasn't our plan, it was co-created with our stakeholders. It is vital that Ofgem listen to those voices and fundamentally rethink the draft determination.

I'll hand over to Alistair for some closing remarks.

ALISTAIR PHILLIPS-DAVIES: Thank you, Rob. I think, as we've set out and despite the comments earlier, there is a significant gap between our original plan and the draft determination. While much work has gone on to deliver that, I still think we need to work hard between now and early mid-December when that comes out. I think there were three areas that we want to see addressed. I think Ofgem need to update their approach to the totex and reinstate allowances and do that at a fair cost and not demand punitive efficiencies which just cannot be delivered. I think the uncertainty mechanisms which we're all working on need to be effective and timely and provide also a fair rate of return. We and stakeholders are aligned with Ofgem's objectives, but the first pass of this will not deliver net zero and, as Rob has said, I think we very much need to focus on what would deliver net zero.

I think overall we'd urge Ofgem to reflect and make necessary changes, challenging our team, but making sure that the proposals are more robust and are more

evidence-based in order that we can ultimately attract the investment we need. We can make the investment we need in our team as well to deliver the scale of projects that we're talking about.

I think, finally, mentioning the CMA provisional findings in water, that is clearly something that we should all look at as well if we wish to avoid any unnecessary delays.

Overall, we all hope that by working together with Ofgem hard over the next couple of months, or even six or seven weeks now, that we can essentially get to a fair and equitable settlement that means we can all start on the journey to net zero from 1 April, rather than be unnecessarily delayed.

With that, and looking forward to seeing that, I'll conclude for now and look forward to your questions later. Thank you.

JONATHAN BREARLEY: Thank you. I would like to hand over to the User Group now to give us their independent review of the draft determinations and proposals.

TRACY MATTHEWS: Thank you for the opportunity to speak here today. In 2018, Ofgem introduced an enhanced engagement model and an independent User Group for each business was established. The primary focus for the User Group was to assess the equity, the extent to which the business plans reflected and would meet the needs of stakeholders. Geoff Aitkenhead and me, Tracy Matthews, are here today from the SHE Transmission User Group.

SHE Transmission undertook over 2,500 stakeholder engagements during the development of their plan, and it's fair to say that the business has learned a lot about effective dialogue with stakeholders. We observed a growing desire by the business to embrace stakeholder engagement and use its stakeholder communities to both express their needs and to continue consulting as the business plan developed.

Stakeholders were clear that they expected a safe and reliable network, an affordable price representing value for money. SHE Transmission *(inaudible – sound distortion)* enabling the transmission to net zero and more services tailored to their needs. We will refer to these expectations here, except price. The subject of price, financeability and allowances, will be covered by other parties here today as you've already heard. These factors are not within the remit of the User Group.

Many aspects of the draft determination are welcomed by the User Group, in particular the continued support for innovation funding, the support for continuous improvement in asset management and the biodiversity no net loss, net gain customer value proposition. We also note and are pleased about the ongoing engagement with the business and Ofgem regarding a number of projects around the proposed business plan.

I will now ask Geoff to speak about reliability and the transition to net zero.

GEOFF AITKENHEAD: Thanks, Tracy. SHE Transmission prepared a number of future energy scenarios using credible information from government poll guidance and the electricity industry's future energy scenarios. They then distilled their thinking into three scenarios with development for the north of Scotland transmission network. These three scenarios were extensively consulted on and resulted in an agreement with stakeholders at one scenario termed the certain view, represented the most credible north of Scotland network development programme. The programme support the continued improvements required for a safe and resilient network and provides a pathway towards net zero. Work proposed in the next five years is based on needs already identified within the Network Options Assessment.

Resilience is important to stakeholders, and this was a theme that SHE Transmission explored in some depth in its business plan. Post-COVID-19, there is greater recognition amongst stakeholders of the importance of some level of redundancy in systems generally as a part of creating resilience. We look to Ofgem to clearly weigh the need for resilience against short-term cost savings.

We scrutinised the development of the strategy underpinning the business plan and tested the contents of the proposed programme of works. We were surprised by the reduction of scope in the capital development programme proposed by Ofgem, but we do now understand that further discussion is going to be needed to review the projects.

A particular proposal to replace the existing control centre facility was scrutinised at length by the User Group. Notwithstanding any background as to why the control centre and back-up facility are in their current condition, the User Group agreed that the facilities were not fit for purpose. This situation is likely to be exacerbated when cyber security requirements are better understood.

Cost is important to stakeholders. Whilst this is not within the remit of the User Group, we wish to make some observations. The scale of SHE Transmission's business has changed radically over T1 and will continue to do so. We ask for assurance from Ofgem that this has been considered in the way this is benchmarked costs. We also ask for assurance that the efficiency targets being proposed recognise the proportion of T1 into T2 cross-over work where delivery is well under way with priced materials, engineering and construction contracts already in place.

Furthermore, evidence should be made available that the company and supply chain efficiencies described in the draft determination remain feasible and a very different investment programme planning process than that used in current benchmarking and cost modelling.

Next slide, please. Stakeholders made it clear that they expect the industry – meaning government, regulatory regime and companies – to lead the way to net zero. We note that the Challenge Group have called upon Ofgem to, "Take a strong leadership role in addressing net zero challenges, developing a strategy, ensuring

the necessary co-ordination and driving change through the regulatory regime". We agree.

Ofgem have made this statement, "We think investment in networks is likely to need to rise perhaps significantly through the next decade to meet net zero targets". Given this statement, which we agree with, there's a very significant question to be addressed regarding the desired rate of increase in capital investment. The SHE Transmission business plan provided a likely view. This is not fully funded through the baseline allowances, but was an important part of providing transparency to stakeholders about the expected investment needed in this next five years to enable the transition to net zero. We would strongly advocate that Ofgem adopt a similarly transparent approach in presenting their final determinations.

We welcome Ofgem's recognition that new requirements will emerge during T2 to support the pathway to net zero and the UK government's recent announcements of their infrastructure investment ambitions. But we have a number of concerns about the proposed mechanism.

A number of net zero enabling project requirements are already established and should be recognised in base allowances now, not be subject to another protracted assessment process. Efficiency and capital programme delivery is, to a large extent, driven by programme planning, co-ordination and visibility. Smooth workflow is required to optimise supply chain efficiency. There is a need for clarity of the processes, roles and responsibilities to introduce and manage this mechanism quickly. Have Ofgem assessed their capacity to manage a change that will result in a significant increase in reopener activity and how will the required additional resources demonstrate value for money?

If the investment programme is backend-loaded due to delays in administering this reopener mechanism, there may be an insurmountable peak of activity resulting in a failure to achieve net zero by the deadline set by the UK and Scottish governments. A fast track option should be scoped to help smooth the workflow and capacity demands on the supply chain.

Pre-construction funding has been removed from baseline allowance. Ofgem should consider allocating pre-construction funding in a way that supports efficient and transparent use of monies, but does not impede companies from timely project scoping and optioneering activity. Tracy.

TRACY MATTHEWS: The three stakeholder-led service proposals Ofgem have rejected for financial incentivisation in the draft determination should be reconsidered. In response to energy policymakers and local authorities, the business plan proposes to offer expertise in support of national, regional and local energy planning. This is an area of expertise that is underserved in local authorities and definitely within community groups. Given the number of consumers classed as fuel poor in the communities with reliance on heating in the north of Scotland, this is an opportunity to reduce the impact of electricity costs on households and is a tangible way that the transmission company can directly support consumers.

In response to regional stakeholders, the business plan proposed two incentives for continued enhanced engagement. Although the User Group recognised that businesses should embrace continuous stakeholder engagement, rejection of both these performance measures is concerning. The business must continue to innovate to combat stakeholder fatigue during a period where increasing engagements and consultations will be critical and where, without a mechanism to measure their performance, in a cost-constrained environment, the business could be under pressure internally to rationalise its consultation commitments.

Thirdly, in response to connections customers, the business plan proposes a revamped service proposition that was designed in conjunction with these customers and that goes well beyond the current service. The User Group encouraged this newly-designed service. As connections increase to facilitate net zero, north of Scotland connections customers will play a major role in the UK energy transition and surety of the connections process is critical for these customers. We ask Ofgem to reconsider these proposals and the other points raised here today by the User Group prior to the final determination.

Thank you very much for allowing us to speak today.

JONATHAN BREARLEY: Thank you. Thank you to the User Group. Now I will hand over to the Challenge Group to give their independent view.

ROGER WITCOMB: Thank you, Jonathan. I'm Roger Witcomb. I'm Chair of the RIIO-2 Challenge Group. I have with me Bob Hull. He is one of the twelve other members of the Challenge Group, all of whom come from a wide variety of backgrounds. They have two things in common: they are all experts and none of them is shy.

I'm going to lead most of this session to Bob to talk about totex, but just quickly I'd like to say first of all that we think the enhanced engagement process is very important. We think that Ofgem could be more explicit about how it's taken account of the input they've had from stakeholders generally. Very quick point.

The second thing I would like to talk briefly about is the process that we were involved in in the production of the draft plan. There were two drafts and then a final plan in December, one in July, and it's fair to say in July all the companies produced pretty thin plans; there was very little meat for us to get our teeth into. When we got to October, most of the companies had put a great deal more justification, both engineering and economic justification, for the numbers they put in there. I have to say the exception was SHE-T. We found the October draft still incredibly thin. The consequence was that when we were submerged in a huge amount of new information when the final plan came out in December, we had very, very little time to look at it in the sort of detail we would have liked.

I think, listening to Akshay earlier this morning, the inference is that there was still yet more information to come which has now come. So, you need to look at our

comments in the light of that, but in the light of that I'm going to ask Bob to say what it was we were able to get out of the plans that we saw in December.

ROBERT HULL: Thanks, Roger. I think the first thing I would say is that clearly RIIO-2 is taking place at a time where it is going to be very tough for customers, and what we really think should be the case is that the minimum necessary expenditure should be included in the baseline.

When we looked at the totex plan, the first thing is that SHE are under-spending during RIIO-1, so they're under-spending their overall totex allowance, and the bid asks for significant increases from RIIO-1, and just to take a couple of examples, non-load related expenditure increases from by 250 per cent from the current run rate, and operating costs increased by 100 per cent by the current run rate. Unit cost increases, when we looked at that, showed very significant increases between the two price controls.

As Roger says, the justification we thought was very poor in the first and second draft of the plans. Additional evidence was provided at the end of the process when it was very difficult to consider that in detail and interact with the company on it. Overall, we had quite a low confidence in the numbers and felt that they didn't have a sound foundation.

Having said that, we asked Ofgem to investigate further and we welcome the discussions that have taken place during that time. It's important that the final decisions are evidence-based.

On uncertainty mechanisms, we feel very strongly that these are needed given the lack of certainty and confidence in some of the numbers. We note in Ofgem's draft determination there are a number of elements that have been included in baseline that could potentially be considered as uncertainty mechanisms. For example, there is some reactive compensation investments that have been included which, arguably, could be provided by non-network solutions, and that's included in baseline. It's not clear to us whether all of the options have been considered. While we absolutely respect the work that SHE have done on future scenarios, there is uncertainty about those, and we think the uncertainty mechanisms should be applied wherever possible for this uncertain expenditure for reinforcement and these other issues.

Project spending should really be designed so that customers get something for their money, rather than allowance being put in there, so things like price control, deliverables and use it or lose it mechanisms, we think are appropriate given the uncertainty.

Having said all that, we welcome the ongoing discussion and that more evidence is being put in place. We think probably where Ofgem are at the moment looks about right, but we look forward to seeing the final determination on totex.

ROGER WITCOMB: Thank you, Rob. So, we did find this quite difficult. We haven't actually seen anything since December, so on totex in particular we recognise we are behind the game, but it's going to be tough for Ofgem as well, I suspect, to go through all the information that they've been given.

I wanted just to say a bit about WACC rates of return because that's something that is out there in the public domain, and we said back in December – and we said it again in our response to the draft determination – that we thought that the rates of return proposed by Ofgem were both appropriate and led to financeable outcomes for all the companies. Since then of course we've had the CMA provisional determination, and that's been quite recent. We haven't done an extensive analysis of it yet, but we have done the one thing which I think we have an advantage on which is going and talking to investors and seeing what they say, investors and other parties on both sides of the market, advisers. The conclusion that we have preliminarily reached is that the Ofgem proposed rate of return makes this sector entirely financeable and, strangely enough – or at least it was to me anyway – the CMA seems to agree with us. I quote from the CMA provisional findings report as follows:

> "The survey evidence we have reviewed strongly suggests that even the most optimistic investors are currently expecting total market returns that are no higher than 5 to 6% and many are expecting returns significantly below this level. Taking all this evidence in the round, we consider that a reasonable total market return range is 5¼% to 6¼%."

Now, there's clearly more to it than I have said there, but on the face of it that is entirely in line with what we have heard from investors, and there's clearly quite a lot of discussion to be had between now and the final determination.

I think that's about everything. Bob, have I forgotten anything?

ROBERT HULL: No, I think that's it.

ROGER WITCOMB: Thank you very much. I'll pass you back to Jonathan.

JONATHAN BREARLEY: I'm going to hand over to Akshay now who will compere the question and answers.

AKSHAY KAUL: Thank you, Jonathan. Thank you to all our speakers for their very lucid and clear presentations.

We have just about 35 minutes, which is excellent, for questions. I will take questions from the floor as well. If you want to ask a question, please do ask a question on the side bar in the chat box on the side. To kick off, let's begin with the first round of questions, and in fact I would like to invite our CEO, Jonathan, to kick off the questioning with the first round of questions. Jonathan, back to you.

JONATHAN BREARLEY: Thank you, Akshay. I want to focus on, in a sense, on net zero and the question of making this price control adaptable to make sure that we get the investment that we need into net zero. Alistair, we have had further conversations since the draft determinations, but are there particular things you want to highlight here that we should be focusing on so that we deliver what I think is a shared ambition to make sure we get the necessary investment in place, but equally to make sure that that investment really is robust on behalf of consumers?

ALISTAIR PHILLIPS-DAVIES: Yes, and I'm absolutely sure you, Akshay and the rest of the team, Min, as well, sorry, she's just appeared on my screen, will make sure that our plans are robust for investors. I think we have a huge challenge in front of us. We saw that from when the slides I flashed up with the amount of additional generation that needs to be connected. I think we will be in a market that is highly competitive for things like cables and materials. I think we're going to see the supply chain run away from us to some extent, and we've certainly seen that in other sectors, I've mentioned it before. One of the other areas our business invests in that it's in the green area has seen huge increases in costs as we move forward basically as we've seen more and more competition for getting hold of a supply chain.

I think overall for us we're pleased with what we've seen from your engineering team in terms of getting totex to a better place. I think you've got to be very careful that we're not going to be able to deliver that at a 10, 20, 30 per cent discount to what we've said. That just isn't credible in today's market.

I think on the uncertainty mechanisms, we talked about it a lot, if we can find workable ones, that's fine. As we've heard I think many times, it is not zero cost to delay making decisions now. If we don't have enough base totex there and agreed now when we've done an awful lot of work on it, then we won't be able to go out to teams of people who have got a chance of delivering that. The team size for one thing, or to deliver £1.6b worth of totex isn't going to be able to deliver £3/3.5b unless there's a substantial delay. So I think it is striking that balance and therefore I think what we need to do is get through the economic work on the engineering work, make sure that the flexibility mechanisms are focused on the right areas, but make sure that we also have the right map base totex.

I don't know whether, Rob, you want to add anything to that.

ROB McDONALD: Just very quickly. The four specific areas, to answer your direct question, Jonathan, that we think you need to focus on is the totex, totex allowances, which I covered in my presentation, a cut of a third really challenges the ability for us to deliver those outputs. We talked about pre-construction. I just think if we put our minds to it, we've got to be able to find a better mechanism that is a better balance between on the one hand protecting customers from uncertainty, but equally funding upfront the necessary investment we need to make in development.

I also discussed in my presentation the volume driver. We've put some proposals in front of your team that we invite you to have a look at.

Lastly, the uncertainty mechanisms, we suggested a mechanism of six months for a decision. That's not the only possible answer, but we do need something that is genuinely agile and flexible. I think if we put our collective minds to it, we should be able to think of something. We managed it in T1 after all and we shouldn't lose sight of that, but I think what's on the table in the draft determination does need a pretty major rethink.

JONATHAN BREARLEY: Thank you. I just wanted to touch on one last thing that the Challenge panel raised. The plans going forward to the run rates in the past, can you explain some of the differences there?

ALISTAIR PHILLIPS-DAVIES: I'll let Rob go through the detail, but obviously there's a huge challenge in front of us. We were facing a substantial amount of investment in the north of Scotland given the Saudi Arabia of renewable energy that we've heard more than one come from recent times. But I think the scale of challenge which we may need to offer around net zero is getting bigger and bigger. We're obviously unfortunate that the Challenge Group didn't think we had all the plans in place before, but obviously we have been running harder as the world has changed very, very quickly around us, and if you just look at the sheer scale of that – and Rob will talk through some of the details – I think that there has been an enormous change in the appetite of people to deliver things when you look at what's required both onshore and offshore now as well.

ROB McDONALD: I think that's right, Alistair. Just to add to that, some numbers to add a little bit of colour, we started the T1 period with a regulatory asset value of £700m. We have currently got a revenue asset value of £3.3b, so there you can see the growth that Alistair is talking about. Even on the Ofgem numbers, we will finish T2 with round about £5b, so you can see the huge growth, 70 times growth in the company, and that's why comparisons between what you're spending on things like operations and maintenance five/six years ago compared to what we're going to spend during the next period is a real apples and pears comparison given the absolutely massive growth, perhaps unlike some of the other companies, but certainly for our company that we've seen during the T1 period. It's as simple as that, Jonathan.

JONATHAN BREARLEY: Okay, thank you. Back to you, Akshay.

AKSHAY KAUL: Thank you, Jonathan. Let me now invite our Non-Executive Director, Christine Farnish, to ask the next round of questions. Christine, please go ahead.

CHRISTINE FARNISH: Thanks, Akshay. We've talked a bit already about the uncertainty mechanism and how important that's going to be over the RIIO-2 period. On the Ofgem's side, we're absolutely committed to making sure that we work at pace and efficiently to deliver the decisions in a timely way, but I'd like to

ask the firm here, the company, the network operator, what they can do, what you think you could do, Alistair and team, to facilitate this process and make sure that we do get to timely and efficient decisions?

ALISTAIR PHILLIPS-DAVIES: I think God is in the detail here, basically, around what we absolutely need to do, so Rob and team, I think you've been involved in the discussions about this and I would be interested to see how far forward we got in terms of delivering something that is truly workable and will deliver what everybody wants. Rob.

ROB McDONALD: Yes, I think that's fair, Alistair. I think the question is accepted that it's incumbent on the companies to put in good submissions. We're asking Ofgem to make quick decisions and it's incumbent on us to make sure that we're providing good submissions and I think that's a totally fair challenge. I do think going beyond that there's a lot of work we can do together, again if we're smart, about agreeing a lot of the conditions, a lot of the policy, if you like, and the framework for these submissions, clear the under-bush almost before we submit these things. So, we tend to, for example, have a discussion almost every time, it almost feels like we reinvent the wheel about how we assess constraints, so should we have a policy and a discussion about how we value constraints in evaluating all of the different options? There are other examples. Carbon pricing, there are lots of different things where we should have a good discussion, agree the policy and that's the standard whatever we agree on – agree is perhaps the wrong word – but whatever is decided upon then applies. That, I think, would mean that we're not reinventing the wheel every time we submit one of these, but the underlying premise of the question that it is incumbent on our company to put in good submissions I think, I will take it.

The only other point I would make is I think we need earlier engagement as well, a bit less formal engagement actually, just so you guys have got good line of sight about what is coming down the pipeline because, as ever, good planning can solve an awful lot of problems in life, and that's something I don't think we're very good at as an industry, certainly it is something we can get better at.

AKSHAY KAUL: Thank you, Christine. If no follow-ups from you, then I'll move on to our Deputy Director for Transmission, Min Zhu, for the next round of questions. Min, please go ahead.

MIN ZHU: Yes, delivering net zero outcome at efficient cost to consumers obviously will require quite a bit of bridging between your local needs and the wider system requirements. How do SHE Transmission see yourselves play an effective role in that space?

ALISTAIR PHILLIPS-DAVIES: I think on a corporate level we're fortunate that we've got a wide range of business interests, whether that be customers, distribution, generation, whether it is flexible thermal generation or indeed renewable generation. So I think at the highest levels in the company we have the broadest, widest and

most detailed view of the energy systems across the UK and how they can work effectively.

Now, I think equally we've always been committed to listening to stakeholders, and we've obviously, particularly on the back of the initiative you've taken here, done more and more work with stakeholders than we've ever done before as part of this overall process, so I think when you put those two things together we start off from a very good, strong position.

Again, Rob, as MD of the business, looking at the detail of what that means, if you comment as well.

ROB McDONALD: Thank you, Alistair. From a transmission perspective, what are we doing in terms of whole system? Well, I think we've got a very, very good track record on this, in fact, sector-leading I would argue. We have in Shetland, I think, the UK's biggest demonstration of a whole system solution, working with distribution colleagues and renewable generators on the island to get an integrated solution that has saved customers in excess of £100m by adopting that solution. So that's a real tangible example of the whole system philosophy that we adopt.

More generally, we're working with people, organisations like the Energy Networks Association and other partners in terms of developing local energy plans. Again, we're making sure that we are thinking about the whole system implications.

I do think we do need to recognise – and Alistair touched on this, I think it was slide number 3 in the pack – the scale of the challenge, the scale of the renewable generation we're facing in our patch. National Grid's numbers, not mine, National Grid's future energy scenarios, and it doesn't matter which one of the squiggly lines on the graphs and National Grid's publications you focus in on, any one of those scenarios you're seeing generation in our patch in the north of Scotland growing from roughly eight gigawatts to 20 gigawatts. We need to build a network that is capable of doing that, so we need to think of whole system solutions where we can, and other technologies where we can, but faced with that significant growth we're going to see huge investment. I think the short answer to your question, Min, I think the track record that we can point to with specific developments that we're going to take speaks for itself.

AKSHAY KAUL: Thanks, Min. If no follow-up questions, then let's take a question or two on finance from our Senior Financial Adviser, Simon Wilde. Simon, please go ahead.

SIMON WILDE: Thanks, Akshay, and thanks, Alistair, Rob and team for very helpful presentations. On slides 10 and 11, you draw our attention to your concerns about the allowed cost of equity. In an international context, do you recognise that rates are coming down in most international markets, and have you had a chance to review the Moody's conclusion where they looked at similar triple A rated regulatory regimes that European returns are coalescing at around 6 per cent nominal, so 4 per cent in CPIH terms, and in that respect the draft determinations are very much

centre of the pack? You can point to countries like France, the Netherlands, Finland, Belgium that are even below the level of return. I'd be just interested in your take on that wider context.

ALISTAIR PHILLIPS-DAVIES: I might get Rob and Maz to go into a little bit of detail but probably not too much to bore all of the audience. I think we absolutely accept that returns are coming down. We're expecting to see returns down, and substantially down, on T1 levels going forward into T2, but equally, as we've discussed with the PR19 findings and elsewhere, I think where you've pitched that at the moment is just too low. I think picking individual items out of that, we can all argue individual items, I'll let the team talk about them. Overall, we need to get to a number that is clearly lower and represents reasonable value, but I think it has to be higher than or considerably higher than what was within the draft determination.

Rob and Maz, you might want to pick up on the detail without killing us all or getting all our brains working too hard.

ROB McDONALD: I think I'll invite Maz to come in and talk about the Moody's, which is the key point we can focus on, particular reports. You have got to look at the evidence in the round and the key point was around the same decision for me.

MAZ ALKIRWI: Yes, I think I recall the points made. In essence, we looked at the evidence, what is observable in the evidence. We acknowledged in our business plan that returns should fall from RIIO-T1 to T2, but what we've pointed out and what the CMA has done is there are a number of factors in here around the evidence that should be based on market data, and I think we have got too quick to conflate the risk-free rates falling and market returns falling mean that we need to half returns, and the evidence just doesn't support that level of cut and the CMA has come out and said what it said. I think Ofgem here have got a responsibility here to make sure they protect consumers, and the CMA have done the same in what they've said. What they believe they're doing will protect consumers and I think that's what we're saying – we're not saying we should get returns that are unwarranted, we're saying we should be attracting investment and we should get returns that are appropriate for the level of risk, and for us that's where it ends. It's not asking for something that is not warranted or evidenced.

SIMON WILDE: Thanks, Maz. Just on the CMA, I don't know if you've had a chance today to look at the fairly lengthy, even punchy, submission made by off Ofwat with respect to the CMA findings, I think they released it at ten o'clock today so you may not have had chance to see it, but if you haven't it's certainly worth a read and worth a discussion.

ALISTAIR PHILLIPS-DAVIES: I think that's definitely something that we will read with interest.

MAZ ALKIRWI: Yes, I am sure there is plenty of submissions, yes.

ALISTAIR PHILLIPS-DAVIES: We will certainly look at that, Simon and team, I'm sure. I suspect this will go right up to the wire in terms of where we are, but overall you've got that CMA number out there, all of our investors understand where that number is. You've got the other two companies in the sector, they're ultimate parent(?) companies, they have got an ability to invest in very different regulatory regimes where the returns are far higher, particularly in the US for both of them. With us, we've obviously got enormous draws on our capital from other places as well. We're looking to find the right answer. We clearly signalled that we're prepared to accept something lower than we put into our original business plan, but we also feel that you'll have to move from where you were in your draft determination and we still hope that we can get an equitable settlement there.

AKSHAY KAUL: Very good, thank you, Alistair. Simon, any follow-up questions from you before I move on?

SIMON WILDE: Thanks, Alistair.

AKSHAY KAUL: I'm going to take stakeholder questions yet.

SIMON WILDE: Not in detail. You didn't mention the fact that you are asking for us to revert the cost of debt mechanism that ---

(Technical issue)

ALISTAIR PHILLIPS-DAVIES: Sorry, Simon, I think you had a follow-up. Do you want to try once more? I think there's occasionally delay, but maybe you could try once more. It's maybe with the cost of debt but we were hard done by because we were getting less than the other two out of that so our cost of capital you can see was the worst of the lot.

(Technical issue)

SIMON WILDE: Understood. In the interests of time, Akshay, why don't you go on.

AKSHAY KAUL: Okay, very good. I think there's a bit of a time delay on the transmission, so apologies for that. I'm going to take a couple of stakeholder questions in a second, but if I could just return to the theme of totex, Alistair and Rob, and the particular critique from Roger and Bob from the Challenge Group, I think they pointed out that your non-load expenditure in particular was going up very sharply, it was in fact tripling in your spending plan compared to the RIIO-1 period. They also pointed out that you have a large-ish under-spend against your T1, your existing price control allowances. Do you want to give a relatively accessible account to the consumer base of what is the underlying reason for this massive growth in non-load expenditure given that most of your recent growth has happened quite recently, and what is the risk that consumers are facing that these non-load allowances are provided but then the money is not spent or the work is deferred into the next control period?

ALISTAIR PHILLIPS-DAVIES: Rob, do you want to take that?

ROB McDONALD: I'll start by picking up the point at the back end of the question, actually, because that is just not true, not for our company. It may be true for some of the other companies you've spoken to but it's not true for our company. We are not massively under-spending in T1. Our under-spend is forecast to be around 3 per cent. I think that is in the ballpark of efficiency savings that actually you should be looking for when you think about incentive-based regulations. Some of the issues you have had with other companies about under-spends, that doesn't apply with our company.

Secondly, just to be absolutely crystal clear, we have not deferred any projects. We have delivered all of the outputs since day one. I know you've got issues with other companies where you think that they may have deferred, then that's for you and them, but for our own account we have not deferred any projects and we are not facing a massive under-spend. So that is actually wrong, that statement. I think the premise of the question needs to be addressed upfront.

In terms of the first part of the question, why then the increase in load-related expenditure – sorry, forgive me, non-load related expenditure during the period, I think we touched on that in relation to Jonathan's question and in relation to the growth and the size of the company. To recap, we started T1 with a £700m company, we are now a £3.3b company, so over four times. So you're seeing a corresponding increase in non-load related expenditure.

Worth recalling as well that all of the individual projects that we put forward in relation to the non-load related expenditure were robustly tested with our stakeholder panel, our User Group and with our wider stakeholder community at the 14 events and 2,500 engagements we had, and latterly with the revised engineering justification packs that we have taken to with your team that have all been approved. So, I don't think that the non-load related expenditure project by project is contentious, and when you put it in the context of the growth, it's entirely reasonable and efficient and I think we benchmark well against the other companies. But I want to push back on – because I think we've got to be careful, this price control has had a few urban myths around it, and one of it is that all of the companies have massive under-spends. That's just not true in the case of our company. It might be with other people, but it's not for us.

ALISTAIR PHILLIPS-DAVIES: I think also with that we've had some tailing off because of COVID as well. So if you look at that 3 per cent, Rob, clearly some of it is probably going to relate to COVID and some delays, particularly in Scotland where it was a much harsher lockdown, it took longer for us to re-establish our working groups and re-establish all of our sites up here.

AKSHAY KAUL: Thank you, Rob and Alistair. Can I also just press on the question of efficiencies. Do you agree that having a strong efficiency challenge is a necessary part of getting to net zero at lowest cost for consumers, particularly as you say given the large increase that you expect will take place to connect a lot more renewable

generation, the efficiency challenge is absolutely fundamental to driving a fair settlement for consumers? In that light, Rob, and Alistair, I think both of you have said that you thought that the draft determination efficiency challenge was, in your words, unworkable or undeliverable. Can you give us a pithy explanation as to why you think the efficiency challenge is undeliverable?

ROB McDONALD: Shall I cover that, Alistair? I totally agree with your statement that the efficiency challenge is absolutely vital to net zero. That's why when we've pulled together our plan it's one of our five goals that are set up on the display behind me. It's one of our five goals and it's a challenge we set ourselves. It's exactly the point, Akshay, that while consumers and other stakeholders are very supportive of net zero, they also want it delivered at reasonable cost, and that's why we set ourselves a challenge, it is baked into the numbers we presented to you, £100m efficiency challenge, so we took our costs from what we've delivered in T1, we applied that efficiency challenge, actually we got closer to £200m than £100m target we set ourselves when we put the plan, and we had those costs verified by consultants, we had Arcadis, we've had – I forget the name of the other consultancy, sorry, I'm getting of an age where you forget some of these things. But we've had a number of different consultancies, and their reports are, and we've made public to you, that backed up the efficient costs. That's what we submitted in our plan. Our issue with the Ofgem determination is that you have then pushed that even further. We think we are at the efficiency benchmark compared to other companies and you are forcing us to go further. The numbers that you've presented for the reasons I set out in my presentation are not achievable against that backdrop, but your general point that efficiencies are important to consumers, we recognised that this time last year and that's why it was the centre piece of one of the five core goals in our business plan.

AKSHAY KAUL: Rob, can I just press you on that. When you say it's not achievable, can you give us some pithy reasons as to why it is not achievable?

ROB McDONALD: Okay, so the 30-second answer would be, of the £360m efficiency savings, £250m that Ofgem identified are what we would call basic mathematical and computational errors, so they're just wrong. We would be happy if you wanted to get a third party firm of accountants in to verify that, a national office whoever looks after these things, then we think that would stand scrutiny. The difference, the remaining £100m or so, is mainly a result of the inaccurate way the benchmarking is applied. In particular, we're very supportive of benchmarking by the way, but as I understand it, you have benchmarked the three companies, you have then come up with a bunch of benchmark costs and you have applied those unit costs to a backward-looking workload. Now, that is just wrong because what you should be doing is doing that exercise, doing that benchmarking, and then applying it to the mix of workload that I am going to do, not what I have done, and actually if you make that one change, just that one change over and above the errors, you unwind all of the efficiency cut, the £361m. This is therefore about £100m of it is about mix and workload, you are applying it to the wrong mix of workload and you've got in front of you the actual mix of work that I'm going to have to do. It's as simple as that, Akshay.

AKSHAY KAUL: Thank you, Rob. I'm going to take a stakeholder question next, which is on your load related programme. I think Martin Young, who I think is from Investec, is asking what would be the impact on your totex if we did go for a co-ordinated expansion of the transmission connections for offshore wind all along the coast, the North Sea and of course along the coast of Scotland?

ALISTAIR PHILLIPS-DAVIES: Rob, I think that's a very difficult question to ask and I think it's quite a complex question as well because ---

(Technical issue)

ROB McDONALD: I think we had IT issues there. So, I think when the offshore OFTO regime was announced and the review was announced, we had already submitted our business plan, so just be clear, in our certain view there is no request for funding and it might not come out of that review, and important to bear in mind that that review has barely concluded the consultation phase let alone come up with any answers. To my mind, the way you reconcile the two is not of a certain view or the things we talked about today in terms of totex, but this does underline the point about getting some really good and agile uncertainty mechanisms. So, if as a result of that review there is any impact on our investment plans, and maybe it's a requirement for us to do more than we are doing in the certain view, I have to say I think that's entirely possible. If we have got some good, agile uncertainty mechanisms, then we will be able to rise to that challenge. That, to my mind, is the key to reconciling the two given they are on a slightly different timescale than the RIIO process.

AKSHAY KAUL: Very good. Thank you, Alistair and Rob. I think we're nearly at the end of our session. Let me hand back to our CEO, Jonathan Brearley, for some closing remarks. Jonathan, over to you.

JONATHAN BREARLEY: I would firstly just like to thank everybody involved in today's event, in particular to SHE Transmission for all the work and preparation that has gone into today, both to the Challenge and the User Groups for their independent review, to all of you who have attended this and all the other hearings we've held, and also, last but not least, to the Ofgem team who have put in so much work into preparing for this.

Equally, I would like to thank everyone involved for the hard work that has gone into the price control. We do recognise that this is an important decision that we're making at the end of this year, not only for UK consumers but for the UK economy as a whole.

Before I conclude, I would like to reiterate some of the things that were said upfront. We know these price controls play a critical role in supporting a green recovery and helping the country hit net zero at lowest cost to consumers. Equally, I do think there is a strong consensus on the strategic direction these price controls must take. We all want lower returns for investors, greater efficiency from

companies, but equally a clear recognition that we need more investment if we are going to make the journey towards net zero. Equally, I do recognise that we differ on the extent of those changes.

Now, since those draft determinations, we have received significantly more evidence from the companies and will consider this before going to the final determination.

Just going on to today's event, again, I think there's a great deal of consensus. We all share the same ambition, in particular around getting to net zero, and equally in making sure that we have a safe and reliable network.

There are areas where we can work together and are continuing to do so constructively, particularly when considering the further engineering evidence that has been provided. Working together on incentives, for example, the incentives on constraints, and on designing a reopener that meets both needs, a need for customers to have commitment to a robust and well thought through investment programme, but equally a process that doesn't get in the way of that investment getting us towards net zero.

As ever, there will continue to be areas of robust debate. I'm sure we will continue to talk about returns, and I note both the comments that SHE-T, the User Group and the Challenge Group have made around this issue. Equally, there will be further conversations around the efficiency and the costs that underpin this programme.

I do want to conclude this and all of our sessions just by again saying thank you to you all. There is an online feedback survey that you will be connected to after this event and we'd encourage you to fill it out. This is the first set of meetings for Ofgem, so we'd appreciate your feedback around what has and what hasn't worked.

Finally, there will be transcripts and recordings available at the end of these sessions and they will be open on our website now that all of these sessions are concluded. What I would like to say at the end of this is this has been an experiment, we are keen to hear from you as to how it's gone, but we are very, very keen to put everyone's interests and voice at the heart of these price controls and we will take account of these open hearings when moving towards our final determination.

Thank you, all, for attending and I bring this session to a close.