

Response to Ofgem's RIIO-ED2 Informal Licence Drafting Consultation

KEY POINTS

- The proposed licence includes a “toolkit” of uncertainty mechanisms that Ofgem plans to introduce to manage the uncertainty associated with load-related expenditure. These mechanisms need to be designed to operate correctly together to enable licensees to be responsive to changing network demand. Ofgem set out one of its objectives of these mechanisms as “ensuring the networks are not a blocker to net zero by having sufficient funding to invest in network capacity and that low carbon technologies do not face installation or operational delays”. As currently drafted, the conditions fail to achieve this effect. In contrast, the suite of conditions introduces (i) uncertainty about whether load-related activities will be appropriately funded and (ii) unclear processes and a risk of unfunded obligations and double-counted adjustments. For example, it is very unclear as to how indirect costs are treated by the Load Related Expenditure volume driver and re-opener. If licensees have to invest more in the network than Ofgem has assumed in its baseline allowances, the mechanisms must fund the efficient indirect costs of doing so as well as the direct costs.
- The load-related licence conditions do not give effect to any mechanism that would fund implementation of flexible solutions on the secondary network. Ofgem should correct this position.
- We have significant concerns around the clarity of the re-opener conditions in the proposed licence. The CMA confirmed that, for any “self-modification” licence condition to be lawful, it must specify the time, manner and circumstances in or under which a modification can be made. If such criteria are correctly set out in the condition itself, the licensee in question should be able to understand the potential impact on it of a future modification at the outset of the price control simply by reference to the condition.
- We have significant concerns that two aspects of the drafting of the re-opener conditions fail to meet these requirements and lead to it not being possible for licensees to understand the potential impact of a future modification on them. Without change or elaboration, we do not believe that the wording of the “evidence test” sufficiently specifies the circumstances under which a modification can be made. Also, several of the re-openers include provision for the Authority to “instigate the re-opener”. However, the conditions are silent on the process that the Authority would follow when instigating the re-opener and do not sufficiently specify the circumstances under which a modification can be made.
- We have further significant concerns with the inappropriate way in which some of the re-openers operate, particularly related to the application of materiality thresholds and Ofgem’s approach to deciding which re-openers have materiality thresholds and which do not.
- Ofgem has not adequately justified increasing the level of the obligation on licensees when setting Network Charges from the current “reasonable endeavours” to “best endeavours” and should reconsider.
- We fully support the intent of SLC10AA, which is to ensure domestic customers are treated fairly. We also agree with the policy intent explained by Ofgem during policy meetings, including the examples of specific scenarios that would not result in enforcement action. However, we remain concerned that the current drafting of the licence condition and the Fair Treatment Guidance does not fully align obligations with the policy intent and, therefore, leaves licensees exposed to unwarranted risks, including potential enforcement action.
- The proposed package of RIIO-ED2 licence conditions and Associated Documents is incomplete. The critical ED2 Price Control Financial Model (the “PCFM”) has not been shared as part of the consultation meaning that cross-referencing from licence to PCFM is not possible, a number of Associated Documents are not yet ready for consultation and some licence conditions have yet to be shared. In particular, we note that work is ongoing to develop a mechanism to deal with increasing

indirect costs where a re-opener is triggered. This is a key component of the uncertainty mechanisms that needs to be seen in order to ensure that the aim of agile and fast acting uncertainty mechanisms can be met.

Responses to consultation questions

1. Do you have any views on the RIIO-ED2 licence drafting principles, set out in Appendix 1?

- 1.1. We agree with the licence drafting principles set out in Appendix 1.

2. Do you have any views on the definitions and the defined terms set out in Annex 3?

- 2.1. We have commented on the definitions and defined terms set out in Annex 3 in the relevant issues logs.

3. What are your views on the proposed changes to the structure of the SpCs?

- 3.1. We agree with the proposed changes to the structure of the special conditions.
- 3.2. However, the consultation on the proposed RIIO-ED2 licence is incomplete. It is important that licensees are able to view all parts of the licence and the Associated Documents together to be able to understand how the price control components will work together and have a clear and complete set of expectations and obligations. It is not possible for licensees to assess this when significant aspects have not yet been incorporated.
- 3.3. The critical PCFM has not been shared as part of the consultation meaning that cross-referencing from licence to PCFM is not possible. There are several important chapters of the ED2 Price Control Financial Handbook (the "PCFH") that are either missing or incomplete. These are needed to be able to understand and comment on the detailed implementation of the price control.
- 3.4. A number of Associated Documents are not yet ready for consultation and some licence conditions have yet to be shared. We recognise that, in some cases, this is due to policy not being sufficiently complete to support their inclusion. However, in some cases this is due to insufficient progress being made by Ofgem.
- 3.5. There has been no progress to date in developing the Regulatory Instructions and Guidance (the "RIGs") that will be needed to ensure that all necessary data is captured from start of the RIIO-ED2 period.
- 3.6. The consultation acknowledges that further licence conditions may be added prior to the statutory consultation in December. However, it only provides one example of a missing condition (the Smart Optimisation Strategy) making it difficult to assess whether Ofgem is aware of other gaps in the suite of documentation.
- 3.7. We recognise that policy discussions are ongoing on a number of these topics and that policies need to be clear to enable licence drafting. However, we are concerned about the extent of work that is likely to be involved in drafting these in a way that operates correctly.

- 3.8. There is a very significant amount of work remaining to be done in a short period of time to correct issues in the published documents and introduce further conditions that interact appropriately with them. It is important that licensees are provided with adequate opportunity to review these proposed conditions prior to the statutory consultation. We do not believe that the time currently set aside in November for the Licence Drafting Working Group (“LDWG”) meeting will be sufficient to achieve this and suggest that further dates be scheduled.
- 3.9. Please see Appendix 1 for details of licence conditions that were not included in the consultation.
- 3.10. There are also a number of issues from a presentational perspective with the way in which both the special conditions and the standard conditions are structured and formatted e.g. there is incorrect or missing bullet point numbering that Ofgem must address prior to the statutory consultation.

4. *Do you agree with our principles for Associated Documents?*

- 4.1. Although we agree with the principles for Associated Documents, any obligations placed on the licensee by virtue of an Associated Document should be clearly expressed in the Associated Document, defined terms used in the licence should be contained in the licence and not cross-reference to an Associated Document and, where terms that are defined in the licence are used in an Associated Document, that Associated Document should not purport to amend the definition in the licence.

5. *Do you have any views on our proposed list of Associated Documents and the timetable for consulting on and implementing them?*

- 5.1. We do not have any comments on the proposed list of Associated Documents at this stage.
- 5.2. However, in addition to the licence conditions themselves, we note that the consultation only includes a sub-set of the Associated Documents that will be required to implement the price control. Some of those that are included in the consultation are incomplete. These Associated Documents form an integral part of the price control. Please see Appendix 2 for details of those Associated Documents.
- 5.3. Noting Ofgem’s principle that Associated Documents must be published in a timely manner, we would expect Ofgem to abide by that principle such that consultations have taken place in respect of all Associated Documents and those documents are formally in place in good time prior to the start of the RIIO-ED2 price control period.
- 5.4. Our comments on the Associated Documents are set out in the issues log provided with this response.

6. *Are there any areas where the licence drafting has not correctly implemented the proposals set out in paragraph 4.1? If so please describe.*

6.1. We have not identified any areas where the licence drafting has not correctly implemented the proposals set out in paragraph 4.1.

7. *Are there other terms or definitions that would be valuable to standardise with other sectors?*

7.1. We have not identified any such other terms or definitions at this stage.

8. *What are your views on the proposed changes to the SpCs outlined in this chapter (Chapter 1, Interpretation, definitions and common procedure)?*

8.1. Our comments on the proposed changes to the special conditions contained in Chapter 1 are set out in the issues log for the relevant condition provided with this response.

9. *Do you think any other common procedure should be added to Spc 1.3 (Common procedure)?*

9.1. We believe that Ofgem should also take the opportunity afforded by the detailed review of the licence to incorporate learning from COVID-19 in respect of derogations. Either relevant licence conditions should have clauses built into them to enable them to be switched off on request of the licensee and consequent direction from the Authority or an appropriate equivalent clause should be included in SpC 1.3 (Common Procedure) and SLC2 (Interpretation of this licence).

10. *What are your views on the proposed changes to the SpCs outlined in this chapter (Chapter 2, Revenue restriction)?*

Revenue restriction: setting of Network Charges

10.1. We would reiterate for the purposes of this consultation response the comments made regarding this issue in our response to FQ36 in the Draft Determinations and in the correspondence sent to Ofgem on behalf of all licensees by the Energy Networks Association dated 16 December 2021 and 30 March 2022. We continue to believe that Ofgem (a) has inappropriately increased the level of the obligation on licensees from the current "reasonable endeavours" to "best endeavours"; (b) has not adequately justified imposing this more onerous obligation, particularly in the context of the requirement to provide 15 months' notice of Network Charges; and (c) has failed to recognise (i) the increase in costs that will be funded by customers without additional benefit as a consequence; and (ii) the safeguards that are already incorporated into the price control to protect customers from any deviation between Allowed Revenue and Recovered Revenue.

Revenue restriction: Independent Distribution Network Operator ("IDNO") bad debt

10.2. The BDA term excludes "any Valid Bad Debt Claims" which represent bad debt claimed by an IDNO which the licensee in turn pays to the IDNO and recovers from Network Charges as part of its Allowed Revenue (specifically the PT term). If a Supplier ceases to trade, the

amount owed to the licensee would include the unpaid element of the Valid Bad Debt Claim i.e. the debt is transferred from the IDNO to the licensee. Consequently, if Ofgem's intent is that BDA should relate only to the licensee's own bad debt and so any Valid Bad Debt Claims should be excluded from BDA, it is not clear how the licensee would be able to recover the unpaid element of a Valid Bad Debt Claim, if a Supplier ceases to trade.

- 10.3. That scenario leaves the licensees with the risk that they would not be able to recover such an unpaid element of a Valid Bad Debt Claim from the Supplier concerned because it had ceased to trade but the licensees would still have the obligation to pay the full amount of the Valid Bad Debt claim to the IDNO so causing a negative difference between amount recovered and amount paid. In response to this concern, Ofgem has stated (in the relevant issues log) that "any other type of bad debts are allowable through the BDA term" and that, in circumstance as the above, a licensee could "recover that bad debt through the BDA term as the definition excludes only the element of Valid Bad Debt Claims as defined in SLC38C". Whilst this clarity aligns with our understanding, we believe that the BDA term could be clearer.
- 10.4. The definition of BDA should be changed to "means the aggregate value of Bad Debt the licensee has incurred, with respect to Network Charges owed to the licensee by one or more Defaulting Electricity Suppliers" i.e. remove "excluding any Valid Bad Debt Claims under SLC38C (Treatment of Valid Bad Debt Claims)".

Unconstrained revenue adjustments by direction

- 10.5. In addition to the standard wording setting out the required 28 days consultation on any proposed direction, any process where the Authority may direct adjustments to otherwise routinely calculated values must:
- a) Appropriately constrain the extent of any directed adjustment, either by:
 - i) Constraining the quantum of the adjustment value; or
 - ii) Constraining the maximum and minimum permitted magnitude of any value changed by the directed adjustment; or
 - iii) Describing the calculation/scope of the adjustment; and
 - b) Clearly explain the factors that the Authority will take into account in deciding whether to make any adjustment and what quantum of adjustment to make.
- 10.6. Without this clarity on the face of the licence, licensees are exposed to potentially different future interpretations of the intent of any adjustment made by direction, leading to potentially unconstrained revenue adjustments or adjustments that have quite different effect to those that were reasonably expected based on policy discussions.

- 10.7. If this detail is to be provided in an Associated Document, the licence should clearly reference this.
- 10.8. There are various examples of such unconstrained adjustments in the proposed licence including:
- a) The adjustment of MC_t term in the major connections ODI if the Major Connections Survey Threshold has not been met;
 - b) The adjustment to Allowed Revenue under SpC 7.8 *“by the amount that the Authority has determined to be unrecoverable”*;
 - c) The calculation of any allowance adjustment under the Net to gross adjustment for Load Related Expenditure; and
 - d) The calculation of any BPI_t adjustment under SpC 4.7
- 10.9. Our other comments on the proposed changes to the special conditions contained in Chapter 2 are set out in the issues log for the relevant condition provided with this response.

11. What are your views on the proposed changes to the SpCs outlined in this chapter (Chapter 3, Totex Allowance adjustments)?

Load Related Expenditure and associated conditions

- 11.1. The proposed licence includes a *“toolkit”* of uncertainty mechanisms that Ofgem plans to introduce to manage the uncertainty associated with load-related expenditure. These mechanisms need to be designed to operate together to enable licensees to be responsive to changing demand.
- 11.2. Ofgem set out one of its objectives of these mechanisms as *“ensuring the networks are not a blocker to net zero by having sufficient funding to invest in network capacity and that low carbon technologies do not face installation or operational delays”*. As currently drafted, the conditions fail to achieve this effect.
- 11.3. Paragraph 2.9 in the Load Related Expenditure Volume Drivers Governance Document states that, if Ofgem’s checks against the five SRVD metrics produce a red flag and the licensee has exceeded its baseline allowance, the Authority will carry out a review, which could lead to claw-back of allowances. It is not appropriate for a process that could result in modifications to allowances to be included in an Associated Document. Ofgem must set out that process on the face of the licence, including specifying the test it will apply before the Authority can propose modifying the licence to give effect to any such claw-back.
- 11.4. In summary, the issues we have identified are as follows:
- a) The combined scope of the Load Related Expenditure Re-opener and the Load Related Expenditure volume drivers conditions is unclear;

- b) The boundary between the Load Related Expenditure Re-opener and the Load Related Expenditure volume drivers is unclear;
- c) The licence conditions do not give effect to any mechanism that would fund implementation of flexible solutions on the secondary network;
- d) The text and calculations in SpC 3.9 are internally inconsistent and also inconsistent with inputs expected by the PCFM;
- e) The process for potentially modifying the Load Related Expenditure volume drivers condition mid-RIIO-ED2 is not established correctly;
- f) The Load Related Expenditure Re-opener “trigger” does not recognise the expected basis of RIIO-ED2 ex-ante allowances in the Final Determinations;
- g) The process to be followed in the case of failed volume driver “check metrics” is unclear;
- h) The boundary between pass-through and the Load Related Expenditure Re-opener is not clearly defined;
- i) It is premature to assume that all Strategic Investment projects should be subject to evaluative PCDs;
- j) The net to gross adjustment for Load Related Expenditure needs much more consideration;
- k) The net to gross adjustment for Load Related Expenditure basis is unclear, double counts Totex Incentive Mechanism (“TIM”) adjustments and introduces a risk of unconstrained allowance modifications;
- l) Important calculations required for the net to gross adjustment for Load Related Expenditure are unclearly defined;
- m) The submission requirements in the net to gross adjustment for Load Related Expenditure need to be reviewed to reflect the fact that baseline assumptions will be set by Ofgem;
- n) SpC 3.11 Part B suggests that inappropriate expectations will be placed on licensees;
- o) The width of the deadband for net to gross adjustment for Load Related Expenditure requires more consideration;
- p) The timing of load uncertainty mechanism adjustments is inconsistent with Ofgem’s recent proposal that baseline allowances will only be adjusted to take account of the Access SCR for the first two years of RIIO-ED2; and

- q) Interactions between load-related conditions and other RIIO-ED2 conditions also need to be considered.
- 11.5. The importance of getting these conditions right is further increased by Ofgem's proposal to only adjust baseline allowances to take account of the outcome of the Access SCR for the first two years of RIIO-ED2. It is now very likely that all licensees will trigger both the Load Related Expenditure Re-opener and the net to gross adjustment for Load Related Expenditure. It is also possible that they will require the volume driver cap to be increased mid-period to reflect wider behavioural change resulting from the outcome of the Access SCR.
- 11.6. Furthermore, it is essential that ex-ante allowances are established in a manner that is consistent with the expected operation of the various uncertainty mechanisms. Any inconsistency between the way in which baseline allowances are set and the way in which the mechanisms are expected to operate may result in further double counts or gaps in the allowances that are ultimately modified into the licence. Licensees must be provided with detailed information under-pinning the assumptions made by Ofgem in setting allowances in order for the re-opener to operate appropriately.
- 11.7. Consequently, considerable work is required to achieve acceptably drafted conditions in this area. We have proposed the main changes that are required to achieve this.
- 11.8. We have set out our detailed comments and drafting suggestions in Appendix 3, Appendix 4 and in the issues log for the relevant condition provided with this response.

Uncertain costs re-openers

- 11.9. We have significant concerns with the inappropriate way in which some of the re-openers operate and around the clarity of the re-opener conditions in the proposed licence. Given the number of re-openers in RIIO-ED2 and the scale of applications that may be made, we believe the resolution of these issues should be a priority for Ofgem.
- 11.10. Our concerns with the inappropriate way in which some of the re-openers operate are:
- a) Inconsistency in the wording used means that it is not always clear whether the materiality threshold is to be assessed relative to the amount of allowance that has previously been provided. This makes the scope of the re-opener unclear and may lead to some licensees who may legitimately expect an allowance adjustment not being entitled to one;
 - b) The definition of "Materiality Threshold" merits a more prominent location in the licence, such as in an appendix to SpC 3.2; and
 - c) Ofgem's approach to deciding which re-openers have materiality thresholds and which do not is inconsistent with Ofgem's verbal clarification that those re-openers that relate to regulatory change/compliance-related activities would not have a

materiality threshold as licensees should not have to face financial exposure from mandatory requirements.

- 11.11. In addition to our separate feedback regarding concerns with the various load-related and Cyber uncertainty mechanisms, we believe that two further uncertainty mechanisms still require some policy work to ensure that the key definitions are updated to set the correct scope: Wayleaves and Diversions Re-opener and PCB Interventions volume driver.
- 11.12. Our concerns around the clarity of the re-opener conditions can be broadly grouped as follows:
- a) Re-opener drafting that is not consistent with the legal requirements of the Electricity Act 1989 (the “Act”);
 - b) Re-opener drafting that fails to achieve the effect expected by policy; and
 - c) Inconsistency in drafting approach that further confuses the intended operation of the re-openers.
- 11.13. We have set out our detailed comments and drafting suggestions in Appendix 5 and in the issues log for the relevant condition provided with this response.

Strategic Investment Price Control Deliverables (“PCDs”)

- 11.14. We consider that it is premature to assume that all Strategic Investment projects should be subject to evaluative PCDs.
- 11.15. We currently do not expect any licensee to be provided with a baseline allowance to deliver a load-related project that has been designated as a Strategic Investment project. Sub-paragraph 3.2.80(b), along with paragraph 1.1 in Appendix 9 (Load Related Expenditure Re-opener Guidance) of the Re-opener Guidance and Applications Requirements document, currently assume that any Strategic Investment projects that are funded via the Load Related Expenditure Re-opener will be subject to evaluative Price Control Deliverables. SpC 3.3 makes provision for the assessment of delivery against those PCDs along with possible consequential allowance adjustments.
- 11.16. It is unlikely that the generic approach to assessing the delivery of evaluative PCDs would be appropriate for the assessment of Strategic Investment projects. In discussions with Ofgem it has been suggested that targeted delivery assessment mechanisms are likely to be required, possibly through the modification of the licence to introduce a mechanistic PCD. It is, therefore, inappropriate for the licence to presume that an evaluative PCD will automatically be created.
- 11.17. The introduction of any PCDs associated with Strategic Investment should be via a modification made under section 11A (modifications of conditions of licences) of the Act (using the drafting approach used in paragraph 3.6.10 for the Net Zero Re-opener). Changes

to the drafting of SpC 3.2, SpC 3.3 and the Load Related Expenditure Re-opener Guidance will be required to achieve this.

- 11.18. Furthermore, the proposed definition of Strategic Investment is very broad. As drafted, it can even include LV projects that are being deployed in anticipation of longer-term need. We understand from Ofgem's load-related policy meetings that Ofgem's expectation is that there will be far fewer Strategic Investment projects than the defined term currently suggests. Consequently, this term needs to be updated to better reflect the assessment that Ofgem intends to apply when identifying Strategic Investment projects that may merit being subject to a PCD mechanism.

Cyber OT and Cyber IT PCDs

- 11.19. We have identified a number of issues with the drafting of and interactions between the various licence conditions that enact the processes associated with Cyber IT and Cyber OT:

- a) Cyber Resilience OT Re-opener (SpC 3.2 Part G);
- b) Cyber Resilience IT Re-opener (SpC 3.2 Part H);
- c) Evaluative Price Control Deliverables (SpC 3.3);
- d) Price Control Deliverable reporting requirements (SpC 9.3);
- e) PCD Reporting Requirements and Methodology Document; and
- f) The PCFM.

- 11.20. The licensees have previously provided details of a number of issues with these conditions to Ofgem and we were, therefore, expecting much greater change to these conditions and associated guidance relative to previous drafts shared with licensees following various policy discussions.

- 11.21. We note that Ofgem's issues log refers to a number of changes having been made in response to the licensees' note. However, some of these changes are not always apparent in the versions included in the consultation. These are noted in Appendix 6.

Use It or Lose It Allowances - Cyber resilience OT

- 11.22. We note that the "Use it or lose it adjustment for cyber resilience OT allowances" condition, which was included in the June draft (SpC 3.3, part D) has been removed. We have taken this to mean that Ofgem will now be relying on the outcome-based PCDs and re-opener, alongside the licence condition, to report progress against delivery of PCDs that are set in order to ensure licensees are held to account for non-delivery of measures they have identified in their plans. We are supportive of this change and would not expect to see such a condition re-introduced.

11.23. Our other comments on the proposed changes to the special conditions contained in Chapter 3 are set out in the issues log for the relevant condition provided with this response.

12. Should we maintain a combined Evaluative Price Control Deliverable condition in SpC 3.3 (Evaluative Price Control Deliverables) or split out the relevant Re-openers and Price Control Deliverables? What are your reasons and how do you think we should split out the conditions?

12.1. We note Ofgem's question 12 and also note Ofgem's statement at paragraph 7.33 of the consultation that *"The methodology for assessing PCDs would then move to SpC 9.3"*.

12.2. The interaction between the three special conditions that regulate Cyber allowance adjustments is difficult to understand.

12.3. Fundamentally, we think that it is important to address the issues with the operation of the licence conditions in respect of Cyber OT and Cyber IT as outlined in this response. Once those issues have been resolved, we would support the creation of a single condition that covers all aspects of the regulation of Cyber OT and Cyber IT allowance adjustments. However, this objective is secondary to ensuring that the various components operate correctly.

12.4. We disagree with Ofgem's proposal that the methodology for assessing PCDs would then move to SpC 9.3 as this would not address the issue that Ofgem's standard approach to evaluative PCD assessment is not appropriate for the assessment of Cyber PCDs.

12.5. Our reasons for supporting the creation of a single condition are:

- a) It is currently difficult to understand the interactions between the various conditions. It is important that all aspects that may influence the basis of totex allowance adjustments related to Cyber interact with each other properly and can be clearly understood. The creation of a separate condition combining all the relevant elements would better facilitate this; and
- b) The specialist nature of Cyber outputs, combined with the fact that much of the detail associated with these projects is confidential in nature, means that some of the standard approach to the assessment of evaluative PCDs is not appropriate to the assessment of Cyber projects. Bringing all aspects into one condition would also allow aspects of the assessment of PCD delivery evaluation to be better tailored to Cyber projects.

12.6. We propose that the following conditions/Parts of conditions be combined into one condition:

- a) Uncertain costs re-opener (SpC 3.2):
 - Introduction;

- Part A – relevant terms, with wording evolved to recognise that these values will not be placed in the public domain;
 - Part G – Cyber Resilience OT Re-opener; and
 - Part H – Cyber Resilience IT Re-opener.
- b) Evaluative Price Control Deliverables (SpC 3.3):
- Part A – relevant paragraphs;
 - Part C – tailored for the assessment of Cyber outputs, including tailoring of defined terms to better reflect Cyber activities; and
 - Part D – Relevant paragraphs.
- c) Use It or Lose it adjustment basis for Cyber OT (if required).
- d) Price Control Deliverable reporting requirements (SpC 9.3) – Part B and Appendix 1.
- e) Text to create a separate guidance document covering Cyber OT and Cyber IT activities, bringing together the re-opener guidance that is currently set out in the Re-opener Guidance and Application Requirements Document with PCD reporting and assessment requirements that are currently set out in the PCD Reporting Requirements and Methodology Document.

13. *What are your views on the proposed changes to the SpCs outlined in this chapter (Chapter 4, Output delivery incentives)?*

Interruptions incentive scheme output delivery incentive

- 13.1. There are currently provisions in CRC2D.33 and CRC2D.36 whereby protection is given to the licensee in a scenario where the Authority has been unable to make a determination in respect of a severe weather event claim or an other exceptional event claim by the time required for that claim to be processed through the Annual Iteration Process (“AIP”). This was raised at the LDWG and Ofgem’s response was that it was inappropriate for the Authority to have a timing obligation placed on it. The issues log, however, closes off this issue by reference to the ability of the licensee to forecast (for AIP purposes) its view of the likely outcome of the claim and how there is no forecast penalty for incentives. Both responses do not, however, reflect that it is wholly inappropriate for licensees to not have a clear understanding of when the Authority is likely to reach a decision on such potentially material issues. This concern should be considered in the context of the inevitable scale of such claims.
- 13.2. Provisions should be inserted that are similar to those currently in CRC2D.33 and CRC2D.36 i.e. “If the Authority has neither directed the licensee under paragraph XX nor otherwise

notified the licensee of its conclusions with respect to the matter within six months of the submission date of the annual interruptions data for the relevant Regulatory Year, the performance adjustment to which paragraph XX refers will be deemed to have been made.”

13.3. Our other comments on the proposed changes to the special conditions contained in Chapter 4 are set out in the issues log for the relevant condition provided with this response.

14. *What are your views on the proposed changes to the SpCs outlined in this chapter (Chapter 5, Other revenue allowances)?*

14.1. Our comments on the proposed changes to the special conditions contained in Chapter 5 are set out in the issues log for the relevant condition provided with this response.

15. *What are your views on the proposed changes to the SpCs outlined in this chapter (Chapter 6, Pass-through)?*

15.1. Our comments on the proposed changes to the special conditions contained in Chapter 6 are set out in the issues log for the relevant condition provided with this response.

16. *What are your views on the proposed changes to the SpCs outlined in this chapter (Chapter 7, Legacy)?*

16.1. Our comments on the proposed changes to the special conditions contained in Chapter 7 are set out in the issues log for the relevant condition provided with this response.

17. *What are your views on the proposed changes to the SpCs outlined in this chapter (Chapter 8, Governance)?*

17.1. Our comments on the proposed changes to the special conditions contained in Chapter 5 are set out in the issues logs for the relevant condition, the PCFH and the ED2 Price Control Financial Model Guidance provided with this response.

18. *What are your views on the proposed changes to the SpCs outlined in this chapter (Chapter 9, General obligations)?*

Disapplication of Relevant Special Conditions

18.1. We note Ofgem's statement in the issues log that it intends to consult on SpC 9.6 after the ED2 Final Determinations and would encourage Ofgem to do so as soon as possible.

18.2. Our other comments on the proposed changes to the special conditions contained in Chapter 9 are set out in the issues log for the relevant condition provided with this response.

19. *Ofgem’s consultation does not ask any questions in respect of the proposed changes to the standard licence conditions. We comment on those proposed changes here and in the relevant issues logs provided with this response.*

Treating Domestic Customers Fairly

- 19.1. As noted in our Key Points, we fully support the intent of SLC10AA and we also agree with the policy intent explained by Ofgem during policy meetings, including the examples of specific scenarios that would not result in enforcement action. However, we remain concerned that the current drafting of the licence condition and the Fair Treatment Guidance does not fully align obligations with the policy intent and, therefore, leaves licensees exposed to unwarranted risks, including potential enforcement action.
- 19.2. Specifically, the absolute obligations in the licence condition are drafted in such a way that could result in activities that licensees routinely undertake breaching “the letter” of those obligations. As such, under any view, the condition as drafted cannot be construed as a “principles-based” licence condition, contrary to Ofgem’s stated policy intent.
- 19.3. The licensees have collectively provided Ofgem with important, detailed drafting suggestions for both the licence condition (sent to Ofgem on 15 September 2022) and the associated Fair Treatment Guidance (sent to Ofgem on 16 September 2022). At the LDWG on 22 September 2022, Ofgem indicated agreement with a range of our proposed drafting suggestions and presented a further draft of the condition which implemented them. Consequently, we had expected that further version of SLC10AA to be included in the informal consultation for stakeholder consideration. That was not the case and the issues log does not explain why those changes have not been made. Some licensees have requested copies of the version of the licence condition that Ofgem presented at that LDWG but, as yet, have had no response to this request.
- 19.4. We are disappointed that those changes have not been consulted on and, given that position, would question whether the licence condition and the accompanying Fair Treatment Guidance were ready for public consultation.
- 19.5. To avoid duplication, we do not repeat our suggested drafting changes in our response to this consultation. We would emphasise, however, that we believe those drafting changes to be appropriate and that it is essential that Ofgem considers the licensees’ detailed proposals made in the two submissions and at the LDWG.
- 19.6. The main issues that our drafting suggestions sought to resolve are further explained in Appendix 7.

Other issues

- 19.7. Our comments in respect of the other proposed changes to the standard licence conditions are set out in the issues log for the relevant condition provided with this response.

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- 19.8. As SLC3A and SLC10AA are in Part A, Standard Conditions for all Electricity Distributors, of the licence, they will also apply to IDNOs. We note, however, that the informal consultation issued on 29 September 2022 was related specifically to the proposed modifications to the licence conditions required to implement the RIIO-ED2 price control settlements for distribution network operators and so does not include IDNOs.
- 19.9. SLC38 and SLC38A are no longer needed because they apply to a Valid Claim received before 1 April 2019. Those conditions should be removed from the licence and marked as “Not Used”.
- 19.10. Although Ofgem has not mentioned SLC13C, Recovery of Reinforcement Costs arising in respect of Relevant Customers, in the consultation, we would point out that, on 1 April 2016, the Authority issued a direction confirming that SLC13C ceased to have effect in the licences of the licensees to whom the direction was addressed but that it continued to have effect for other licensees until directed otherwise. SLC13C should, therefore, be removed from this part of the licence and inserted in a part of the licence that is applicable only to the other licensees.

Appendix 1**Licence Conditions not included in the consultation**

<u>Missing licence condition(s)</u>	<u>Significance</u>
Opex escalator uncertainty mechanism SpC 3.X	<p>Ofgem has signalled at cost assessment policy meetings that a condition similar to the RIIO-T2 condition will be implemented for RIIO-ED2, but no discussions have yet been held on the drafting of the condition.</p> <p>Assuming that the intention is to mirror the RIIO-T2 condition, it will need to be drafted in a way to interact with all other uncertainty mechanisms. The associated algebra will need careful drafting to ensure that it interacts correctly.</p>
Smart Optimisation Strategy SLC X	<p>The consultation acknowledges the absence of this licence condition from the suite of documents.</p> <p>Elsewhere in this response we highlight a number of important issues with the way that the suite of conditions that relate to load-related activities interact.</p> <p>This condition is likely to introduce obligations that impinge on the same set of load-related activities. It will, therefore, be necessary to carefully word this condition to ensure that it interacts appropriately with all other relevant conditions.</p> <p>It is also unclear what interaction (if any) this new condition will have with the existing SLC7A Whole System licence condition and the accompanying Associated Document.</p> <p>Ofgem's policy needs to be confirmed as soon as possible so that licence drafting can be concluded in time for the statutory consultation.</p>
Absence of modifications to enact Access SCR changes SLC14 SLC12	<p>Three areas of the licence have previously been identified as requiring modification to enact the outcome of the Access SCR:</p> <ul style="list-style-type: none"> • SLC14: Ensuring consistency between the licence and the new voltage rule implemented via the CCCM; • SLC12: Giving effect to the policy intent to enable licensees to strategically reinforce the network; and • Introduction of obligations on licensees to offer curtailable connections to customers.

	<p>We understand from recent working group meetings that Ofgem plans to make these modifications separately to the RIIO-ED2 modifications as housekeeping changes.</p> <p>We do not believe that Ofgem has given itself the ability to make such modifications under the housekeeping provisions, nor do we think that it would be appropriate for Ofgem to do so.</p> <p>Furthermore, we believe that the modifications should come into force at the start of the price control, allowing alignment between charging rules and how uncertainty mechanisms are established.</p> <p>It is unclear why Ofgem is not taking this opportunity to make these changes at this time. Ofgem should revisit this decision and act without delay in order to incorporate them into the RIIO-ED2 licence at the start of the price control period.</p>
<p>Ongoing Network Innovation Competition (NIC) projects with RIIO-ED2 spend</p> <p>SpC 9.X</p>	<p>The draft licence does not include any provision to permit income from the System Operator in respect of NIC projects that were approved in RIIO-ED1 and will continue into RIIO-ED2.</p> <p>An extra condition is required that mirrors the relevant sub-set in CRC5A of the RIIO-ED1 licence.</p>
The PCFM	<p>The PCFM forms part of SpC 8.1. The PCFM that will operate during RIIO-ED2 was not included with the consultation. This is a key omission. Without the PCFM, licensees cannot fully understand how the mechanisms set out in licence conditions will flow through to Allowed Revenues.</p> <p>Furthermore, an early draft of the PCFM that was shared separately with licensees some weeks before the consultation showed misalignment with the way in which many of the conditions have been drafted. For example, several of the variable values anticipated in the proposed special conditions were not included within the PCFM and, conversely, a number of variable values that are included in the PCFM are not described in the draft special conditions.</p> <p>A significant piece of work is required to ensure that the PCFM is fully aligned with the intended licence conditions and operates as expected.</p>
Several important chapters are missing from the PCFH	<p>The PCFH forms part of SpC 8.1. Several chapters were not included in the consultation, including the calculations of the cost of capital and allowances for real price effects.</p>

	<p>Without these chapters licensees cannot fully understand how their Allowed Revenues will be calculated. We urge Ofgem to share drafts of these chapters as soon as possible so they can be discussed no later than the November LDWG.</p> <p>We also note that there is no placeholder in the draft PCFH for the new guidance expected in respect of circumstances where the forecasting penalty under Part G of SpC 2.1 will not be applied. This is a very important new section of the PCFH given the changed basis to the operation of the PCFM and the calculation of Allowed Revenue for RIIO-ED2. Licensees must be able to review and comment on the wording of this section prior to the statutory consultation.</p>
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Appendix 2**Issues with Associated Documents**

<u>Associated Document issue</u>	<u>Significance</u>
Several important chapters are missing from the PCFM Guidance	<p>The PCFM Guidance is an important document that allows licensees to better understand how the price control will operate and the processes that they will need to have in place to implement new procedures and obligations.</p> <p>This is particularly applicable in respect of our discussions with Ofgem regarding our concerns about the proposed new obligations in and the operation of SpC 2.1 in respect of using best endeavours to forecast Allowed and Recovered Revenues, the forecasting of variable values and the recalculation of historical Allowed Revenue. It is clear that the instructions for populating variable values in the PCFM are very important aspects of the price control that licensees will need to assess when making final decisions about the acceptability of this new obligation. These instructions are not included in the draft document.</p>
Some published Associated Documents are incomplete	<p>We note that, for new incentives in particular, the published Associated Documents do not contain all of the information needed by licensees to fully understand the regulatory mechanism or area that the Associated Document is meant to be describing e.g. survey details and appeals processes.</p> <p>This information must be provided as soon as possible.</p>
No progress in developing the RIGs	<p>We note that there has been no progress to date in developing the RIGs that will be needed to ensure that all necessary data is captured from start of the RIIO-ED2 period. It takes time to implement the process changes required to capture the data and the systems changes required to record the data. This work needs to be prioritised if licensees are to be able to capture the data from the start of the RIIO-ED2 period.</p>
Unnecessary delays to consulting on Associated Documents	<p>Ofgem proposes that a very large number of Associated Documents will be consulted on in “<i>first quarter 2023</i>”.</p> <p>It is unacceptable for so many of these to have been delayed to this late stage in the process. Licensees need to be able to review the requirements of these documents in parallel to reviewing the licence condition in order to understand the intended operation of the price control.</p>

	<p>We believe that a number of these should be available to be consulted on in autumn 2022, particularly:</p> <ul style="list-style-type: none">• Digitalisation Strategy and Action Plan Guidance; and• SIF Governance Document. <p>We urge Ofgem to accelerate work on all Associated Documents, including consideration of all feedback previously provided by licensees, so that consultation can be undertaken as soon as possible.</p>
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Appendix 3**Load Related Expenditure and associated conditions**

The core “toolkit” of uncertainty mechanisms that Ofgem plans to introduce to manage the uncertainty associated with load-related expenditure is established via a range of documents including:

- a) SpC 3.2 - Uncertain Costs Re-openers;
- b) SpC 3.3 - Evaluative Price Control Deliverables;
- c) SpC 3.9 - Load related expenditure volume drivers;
- d) SpC 3.11 - Net to gross adjustment for Load Related Expenditure;
- e) SpC 6.1 - Pass-through items;
- f) Load Related Expenditure Re-opener Guidance;
- g) Load Related Expenditure Volume Drivers Governance Document; and
- h) The PCFM.

The issues that we have identified with the scope and operation of this “toolkit” of documents arise due to issues in individual documents and issues with the interaction between them. Those issues are individually material and cumulatively huge. In summary:

- a) The combined scope of the Load Related Expenditure Re-opener and the Load Related Expenditure volume drivers is unclear. This leads to uncertainty as to whether some load-related activities are included at all, as well as the potential for very different interpretations of the required calculations of Load Related Expenditure Re-opener allowance adjustments;
- b) The boundary between the Load Related Expenditure Re-opener and the Load Related Expenditure volume drivers is unclear. This leads to confusion as to whether all load-related activities are addressed within the toolkit of activities. In particular, it is unclear whether several load-related activities at 11kV and below are addressed by either mechanism;
- c) The scope of the Load Related Expenditure Re-opener “trigger” does not recognise that a difference may exist between the licensee’s forecast demand and the basis of Ofgem’s RIIO-ED2 ex-ante allowances in the Final Determinations. It also does not include changes to the proportion of forecast expenditure that will be funded by DUoS customers. It is essential that the condition clearly states that changes due to any difference between Ofgem’s assumptions and the ultimate load constraints on the network may be included in any re-opener application;
- d) The process to be followed in the case of “red flag” volume driver “check metrics” is unclear, incomplete and based on data that have not historically been reported and may be subject to reporting inconsistencies. This leads to a risk that a “failure” of one metric leads to protracted and intrusive discussions about the efficiency of volumes as well as uncertainty of allowances for all relevant volumes. In turn, this introduces the risk of licensees delaying key investment due to concerns about whether volumes will be allowed;
- e) The text and calculations in SpC 3.9 are internally inconsistent and also inconsistent with inputs expected by the draft PCFM shared previously with licensees. It is absolutely crucial that it is clear

whether relevant calculations are to be calculated to replace ex-ante allowances or to make adjustments relative to ex-ante allowances, and that, in turn, these align with the intended operation of the PCFM. The current inconsistency leads to the risk that materially incorrect totex allowances may be calculated;

- f) The process for potentially modifying the load related expenditure volume drivers condition mid-RIIO-ED2 has not been established correctly. It is essential that text is included on the face of the licence setting out the manner and circumstances in or under which such a modification may be made;
- g) The boundary between pass-through and the Load Related Expenditure Re-opener is not clearly defined. It currently seems likely that allowances for transmission connection point charges will be partially double counted;
- h) It is premature to assume that all Strategic Investment projects should be subject to evaluative PCDs. Furthermore, the definition of Strategic Investment is too broad and may result in an inappropriately large number of relatively small projects being subject to PCDs leading to disproportionate processes being introduced;
- i) Ofgem's proposed continuation of the net to gross adjustment for Load Related Expenditure condition into RIIO-ED2 needs much more consideration. Ofgem has not consulted on this proposal and the proposed drafting is unclear. For example, it double counts Totex Incentive Mechanism adjustments and introduces a risk of unconstrained allowance modifications. Additionally, several important calculations that are required to calculate any adjustment are not clearly defined. This leads to a risk of unexpected or unwarranted adjustments to allowances for Load Related Expenditure;
- j) Furthermore, the net to gross adjustment for the Load Related Expenditure condition has not been drafted in a manner that is compatible with Ofgem's proposed approach to setting baseline allowances for years 1 and 2 of RIIO-ED2 on a different basis to years 3 to 5 of RIIO-ED2 in respect of the outcome of the Access SCR. It is highly likely that all licensees will trigger this mechanism as a direct consequence of the difference between Ofgem's assumptions in setting baseline allowances and the charging basis introduced following the Access SCR;
- k) The proposed net to gross adjustment for Load Related Expenditure also does not include a proposed range. More consideration should be given to the width of the deadband, especially in light of Ofgem's approach to setting allowances to reflect the Access SCR;
- l) SpC 3.11 Part B suggests an inappropriate expectation that licensees will deliver a specific percentage of Gross Load Related Expenditure via Specific Customer Funded Reinforcement. This suggests that licensees should somehow manage their investment to keep the ratio of work that is part-funded by connecting customers and that funded by existing customers within a particular range. This would be a very unhelpful and potentially counter-productive obligation that could stand in the way of delivering for customers. In the context of Ofgem's proposed approach to setting

allowances to take account of the outcome of the Access SCR, it may also conflict with the requirements of the Common Connections Charging Methodology. It should be removed; and

- m) The timings of the mechanisms do not align and may lead to “boundary issues” in the operation of the mechanisms. Furthermore, the Load Related Expenditure Re-opener cannot be triggered in time to confirm allowances for year 3 of RIIO-ED2. Given that Ofgem proposes not to adjust baseline allowances for year 3 of RIIO-ED2 to take account of the outcome of the Access SCR, this means that licensees will have no certainty of allowances for year 3 of RIIO-ED2 at the time that they are required to commit to expenditure.

It is also important that baseline allowances are set in a manner that is consistent with the expected operation of the various uncertainty mechanisms. Any inconsistency between the way in which baseline allowances are set and the way in which the mechanisms are expected to operate may result in double counts or gaps in the allowances that are ultimately modified into the licence. These issues are further compounded by the complexities associated with Ofgem’s proposed approach to setting baseline allowances following the outcome of the Access SCR. The overall effect of this suite of issues is to create significant uncertainty as to whether key, load-related activities will be appropriately funded during RIIO-ED2. Licensees must be provided with detailed information under-pinning the assumptions made by Ofgem in setting allowances in order for the re-opener to operate appropriately.

Once the issues in the core “*toolkit*” of documents have been resolved, further work will be required to ensure that the core mechanisms interact correctly with other RIIO-ED2 conditions.

We have identified the following further conditions that need to correctly interact with the toolkit of load-related uncertainty mechanisms:

<u>Condition</u>	<u>Interaction</u>
SpC 3.2 Storm Arwen Re-opener	May result in fundamental changes to planning standards which could include, for example, changes to interconnection standards (normally categorised as Load Related Expenditure).
SpC 3.2 West Coast of Cumbria (ENWL)	Will result in new assets, including new GSPs, resulting in amended Load Related Expenditure (including Transmission Connection Point (“TCP”) requirements. May remove assets that were previously scheduled to be subject to Load Related Expenditure.
SpC 3.6 Net Zero	Definition of Net Zero Development includes “ <i>new investment arising from the agreement of a Local Area Energy Plan</i> ” – commonly these would result in Load Related Expenditure.

SpC 3.7 Co-ordinated Adjustment Mechanism	May transfer Load Related Expenditure projects (including Strategic Investments) between licensees or between electricity distribution and transmission. May move costs from TCP to Load Related Expenditure or vice versa.
SpC 3.8 Green Recovery	Some Agreed Schemes may deliver load-related outcomes.
SpC 3.12 Off-gas grid mechanistic Price Control Deliverable (UKPN)	Relates to provision of capacity ahead of need to Off-Gas Grid Customers
SpC 9.X Whole System Strategies	Policy and condition not yet made available but may affect expenditure that could be categorised as Load Related Expenditure.

Load Related Expenditure and associated conditions: Detailed issues

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
The combined scope of the Load Related Expenditure Re-opener and the Load Related Expenditure volume drivers is unclear					
1	Load Related Expenditure defined term	SpC 3.2.75 SpC 3.9.2 SpC 3.11.9(b)	The definition of Load Related Expenditure does not make it clear whether the various mechanisms that rely on this term operate on a gross or net of customer contributions basis.	<p>Given the likely impact of customer contributions, this difference in basis could result in different calculations of Load Related Expenditure Re-opener allowances.</p> <p>Clarity regarding this issue is also required to inform any adjustment that Ofgem may direct under the net to gross adjustment for Load Related Expenditure. Any assumption that the Load Related Expenditure Re-opener allowances had been calculated on a gross basis could see materiality incorrect adjustments being directed.</p>	<p>Based on discussions with Ofgem, we assume that SpC 3.2 and 3.9 are expected to operate on a net of customer contributions basis.</p> <p>Define the connection element of this definition as: “connections projects that are subject to the apportionment rules under the Common Connection Charging Methodology after deduction of Specific Customer Funded Reinforcement”</p> <p>The definition of Load Related Expenditure would, therefore, be: “means expenditure in the following cost categories:</p> <p>(a) connections projects that are subject to the apportionment rules under the Common Connection Charging Methodology after deduction of Specific Customer Funded Reinforcement;</p> <p>(b) primary reinforcement;</p> <p>(c) secondary reinforcement;</p> <p>(d) fault level reinforcement; and</p>
2	Load Related Expenditure defined term	Gross Load Related Expenditure defined term (SpC 3.11)	The definition of Load Related Expenditure includes “connections” which could be interpreted as including sole user assets.	As the definition of Gross Load Related Expenditure relies on the defined term Load Related Expenditure this could suggest that sole user assets should be included in the net to gross calculations. This	

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
				would be inappropriate and inconsistent with our understanding of baseline percentage calculations.	(e) New Transmission Capacity Charges.” We think this would also work for SpC 3.11.9(b) given the context in which it is used there.
3	Load Related Expenditure defined term		<p>Policy intent in terms of inclusion of indirect costs is unclear.</p> <p>Ofgem’s recent consultation on Access SCR proposes including indirect costs associated with the Access SCR outcome for years 1 and 2 of RIIO-ED2 in LRE baseline allowances.</p> <p>Such indirect costs are not included in the definition of Load Related Expenditure. We understand that the indirect costs for other aspects of Load Related Expenditure have not been included in LRE baselines.</p>	<p>There is a risk that allowances for indirect costs get “over-written” in any re-opener modification resulting in no allowance being provided for these acknowledged costs.</p> <p>It is not clear which uncertainty mechanism will provide for the indirect costs associated with the Access SCR outcome for years 3 to 5 of RIIO-ED2.</p> <p>It is also not clear how extra indirect costs associated with increases in uncertain Load Related Expenditure more generally will be funded.</p>	<p>We are unclear as to the intended policy.</p> <p>We assume that the indirect costs associated with the Access SCR that are to be included in Final Determinations baseline allowances will be allowed on a basis that is internally consistent with the baseline allowances for direct costs associated with the Access SCR.</p> <p>Any further indirect costs resulting from the implementation of the outcome of the Access SCR, and those associated with uncertain load-related expenditure costs, should be allowed for via an uncertainty mechanism.</p> <p>If the additional indirect costs are to be provided via the Load Related UM “toolkit”, the scope of the Load Related Expenditure defined term and the scope of the Load Related Expenditure volume drivers should be expanded to include indirect costs.</p> <p>If the indirect costs are, instead, to be allowed via a different mechanism (e.g. opex</p>

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
					<p>escalator), Ofgem should clarify where those costs will be allowed and move baseline allowances to align with that process.</p> <p>We believe this to be true for any over-baseline indirect costs such that it applies equally to all indirect costs associated with Load Related Expenditure.</p>
The boundary between the Load Related Expenditure Re-opener and the Load Related Expenditure volume drivers is unclear					
4	Secondary Reinforcement defined term	SpC 3.9 Appendix 1	<p>The definition of Secondary Reinforcement appears to include all secondary network activities, not just load-related activities.</p> <p>Some of the “Definition of Capacity Delivered” descriptions could apply to work undertaken under several cost drivers e.g. volumes such as km circuit installed can be undertaken for multiple purposes.</p> <p>The terms in appendices define the activity but not the cost driver (i.e. the “what” but not the “why”).</p>	<p>It is, therefore, unclear which cost drivers are to be included within the volume driver calculations.</p> <p>It is necessary to define which cost drivers are relevant e.g. Just general reinforcement? Connections within price control? Fault level reinforcement? All circuits installed (e.g. including diversions)?</p> <p>Confirmation of this is also needed so that licensees are able to check the basis of ex-ante allowance apportionment. If ex-ante allowances are misaligned with the mechanisms that will operate, it may result in licensees having unfunded costs or double counted allowances.</p>	<p>To fix all these:</p> <p>Redraft SpC 3.9.2 to avoid reference to the terms Secondary Reinforcement and Low Voltage Service and to reflect the intended operation in the PCFM (<i>for PCFM issue description see below</i>):</p> <p>“The effect of this condition is to update totex allowances to fund the licensee for Load Related Expenditure related to certain <u>defined activities</u> during the Price Control Period”</p> <p>Create defined terms for the volume drivers:</p> <p>Define “Secondary Reinforcement Volume Driver” as means “the value determined in</p>

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			<p>We understand from recent policy discussions that it is Ofgem's intention that only volumes associated with general reinforcement will be included in the volume driver calculations and that connections-related reinforcement volumes will be within the scope of the re-opener.</p> <p>We note that allowances for secondary volumes set out in the Draft Determinations did not include connections.</p> <p>The Secondary Reinforcement defined term also only relates to HV activities (between 22kV and 1kV). It excludes activities at LV, which are clearly included in the volume driver (for low voltage circuits).</p>		<p>accordance with Part A of Special Condition 3.9"</p> <p>Define "Low Voltage Services Volume Driver" as means "the value determined in accordance with Part B of Special Condition 3.9"</p> <p>Expand definitions in SpC 3.9 Appendix 1 and Appendix 2 (or in the guidance document) to be clear about:</p> <ul style="list-style-type: none"> • The scope of each "unit"; • Which cost drivers are to be included (i.e. general reinforcement, Specific Customer Funded Reinforcement); • Which voltages are to be included; and • Whether net of associated Specific Customer Funded Reinforcement. <p>Remove Secondary Reinforcement and Low Voltage Service terms from the definitions list.</p>
5	Secondary Reinforcement defined term	SpC 3.9.2 SpC 3.2.75	Definition of Secondary Reinforcement is broader than the anticipated scope of the SpC 3.9.	When inferring the scope of the Load Related Expenditure Re-opener based on SpC 3.2.75 the reader may wrongly assume that all secondary network reinforcement activities should be excluded from Load	

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
				Related Expenditure Re-opener calculations. This would result in activities such as secondary network fault level expenditure potentially being missed from LRE allowances.	
6	Low Voltage Service defined term	SpC 3.9 Appendix 2	The definition of “Low Voltage Service” states that it “does not include the joint and associated components connecting the service line to the distributing main”. However, work on these components would be expected to be included in service unbundling activities etc.	The definition suggests that only a sub-set of service unbundling activity costs etc would be funded via this volume driver. This is not consistent with our understanding of intent of the reinforced service capacity types.	
7	Capacity type definitions in SpC 3.9 Appendix 1 and Appendix 2	Load Related Expenditure Volume Drivers Governance Document	The capacity types are defined as “determined in accordance with Load Related Expenditure Volume Drivers Governance Document”. However, the governance document does not provide this clarification.	There is potential ambiguity in the interpretation of “units”.	
8	Capacity type definitions in SpC 3.9 Appendix 1		Some capacity type definitions refer to “high voltage” and “low voltage” without being clear what voltage levels are being referred to.	There is potential for confusion about which volumes are to be included against which unit costs.	

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
9	SpC 3.2.75	SpC 3.9	<p>The following activities are currently not included in SpC 3.9 and are assumed to fall into the scope of the Load Related Expenditure Re-opener for all voltages:</p> <ul style="list-style-type: none"> • New transmission connection point charges; • fault level; • any work to manage constraints at grid and primary level; • traditional, non-traditional or innovative solutions to manage constraints caused by thermal, voltage, harmonics or reverse power flow issues; • any other service-related reinforcement work; • curtailment and flexibility payments; and • network monitoring i.e. the installation of monitoring equipment to gain network visibility for the management of load-related constraints caused by thermal, 	<p>Confirmation of this is needed to enable licensees to check the basis of ex-ante allowance apportionment. If ex-ante allowances are misaligned with the mechanisms that will operate, it may result in licensees having unfunded costs or double counted allowances once the mechanisms start to operate.</p>	<p>It is essential that Ofgem confirms the intended scope.</p> <p>In particular, recent discussions with Ofgem advise that any connections driven work will sit in the Load Related Expenditure Re-opener and not the volume driver. Ofgem needs to formally confirm this and address via definitions.</p>

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			<p>voltage, reverse power, fault level or harmonic issues.</p> <p>We also understand that Ofgem is considering whether or not the following activities may be included within the volume driver:</p> <ul style="list-style-type: none"> • fuse upgrade; and • upsizing of service cable. 		
Text and calculations in SpC 3.9 are internally inconsistent and also inconsistent with inputs expected by the PCFM					
10	SpC 3.9.2	PCFM	SpC 3.9.2 talks about calculations being “relative to baseline allowances” but calculations in the PCFM are not undertaken on that basis. The PCFM seems to be expecting updated allowances i.e. that baseline allowances are “over-written”.	<p>There is a mismatch between description and calculation.</p> <p>It looks like the PCFM is expecting recalculated values and that, although the algebra in SpC 3.9 is correct, the description in SpC 3.9.2 is misleading.</p>	<p>Redraft SpC 3.9.2 to avoid reference to the terms Secondary Reinforcement and Low Voltage Service and to reflect the intended operation in the PCFM:</p> <p>“The effect of this condition is to update totex allowances to fund the licensee for Load Related Expenditure related to certain defined activities during the Price Control Period”</p>
11	SpC 3.9.4 SpC 3.9.6	PCFM	The PCFM currently includes variable values for Load: Transformers volume driver and Load: Circuits volume driver respectively but these two items are combined in the Secondary Reinforcement Volume Driver term (SRVDt) in the draft SpC 3.9.	<p>There is a mismatch between the licence condition and the PCFM.</p> <p>The licence condition does not show how the values are expected to be calculated by the PCFM.</p>	<p>Undertake a consistency check between the licence and the PCFM variable values.</p> <p>Align ex-ante allowances to the ultimate split between SpC 3.2 and SpC 3.9.</p>

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			The PCFM does not include a row in the DNO input sheets for the Low Voltage Services Volume Driver term (LVSVDt), but this is included in draft SpC 3.9.	The PCFM is missing a value that the licence anticipates being required. It is, therefore, unclear whether revenues will be adjusted correctly.	
12	SpC 3.9.5 SpC 3.9.7		SpC 3.9 is drafted to include two separate expenditure caps. This seems to be inconsistent with the policy position set out at 3.79 of Draft Determinations, which suggests that one combined cap would be introduced.		Ofgem should confirm whether its policy intent is to introduce one combined cap or two separate caps and, if necessary, adjust the drafting.
13	SpC 3.9.5 SpC 3.9.7		Ofgem has yet to consult on the policy for how the value of the caps will be determined.	Licensees cannot comment on whether the unit costs and cap are likely to interact appropriately. If the cap is set inappropriately low, it may frustrate the ability of this condition to operate as intended.	The policy for how the value of the caps will be determined should be shared with licensees.
14	SpC 3.9.5 SpC 3.9.6		The wording of 3.9.5 and 3.9.6 suggests that identical caps will be included for all licensees.	Paragraph 3.80 of the Draft Determinations suggests that different caps will be introduced for each licensee. We think that this would be sensible given the different	We believe that the cap values by licensee should be included in a new appendix and reference should be made to the relevant value in the text of the licence condition.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
				network sizes and programme sizes of different licensees.	This approach would also assist with defining the missing self-modification process discussed below. i.e. the self-modification process may modify the value in the appendix without any adjustment to the text of the licence condition being required.
The process for potentially modifying the Load Related Expenditure volume drivers condition mid-RIIO-ED2 is not established correctly					
15	SpC 3.9	Load Related Expenditure Volume Drivers Governance Document paragraph 4.7	<p>The Load Related Expenditure Volume Drivers Governance Document refers to the potential to change the unit costs and caps after the “Review of LRE volume drivers” under the processes set out in SpC 3.9 or SLC46 (presumably not SpC 46 as stated) processes.</p> <p>No modification processes are set out in SpC 3.9. There is also no process to modify SpC 3.9 included in SLC46.</p>	If an appropriate self-modification process is not set out on the face of SpC 3.9, modification of this condition would be via the statutory modification process.	An appropriate process needs to be included on the face of the licence in SpC 3.9 to allow modification of the licence after the “Review of LRE volume drivers” process.
16	LRE Volume Driver Governance Document section 4		It is not clear whether it is intended that this process can change licence values retrospectively or just for current and future years. The governance document implies that values	There is lack of clarity of the scope and impact of a future licence modification.	<p>The scope of the review of LRE volume drivers and caps needs to be set out much more clearly.</p> <p>In any case, it would be sensible to set out annual values for each of the unit costs in</p>

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			could be amended for all years – and the unit costs are only listed once to apply to all years.		appendices 1 and 2 of SpC 3.9, allowing for unit costs to be modified for certain years.
The Load Related Expenditure Re-opener “trigger” does not recognise the expected basis of RIIO-ED2 ex-ante allowances in the Final Determinations					
17	SpC 3.2.75 (a)	Load Related Expenditure Re-opener Guidance	<p>SpC 3.2.75(a) refers to “an increase in current or forecast demand on the Distribution System” being one of the triggers of the Load Related Expenditure Re-opener whereas the Load Related Expenditure Re-opener Guidance refers to changes in forecast demand relative to “the initial Forecast Demand that was used to set baseline allowances at the start of RIIO-ED2”.</p> <p>The definition in the licence would also not allow for circumstances where the same or similar load-related constraints are forecast but DUoS customers will fund a greater proportion of the associated costs.</p> <p>Furthermore, the second part of SpC 3.2.75(a) refers to “a change in conditions on the Distribution</p>	<p>There is potential conflict between the licence and the guidance.</p> <p>We think the wording in the guidance document better reflects intended policy in terms of against which set of assumptions comparisons should be made. However, given the document hierarchy, the wording in the licence condition would need to be adhered to.</p> <p>Without this qualification in the licence condition itself and because Ofgem may set allowances on a different basis to the licensee’s actual demand or forecast demand, it is possible that legitimate claims for allowances to be re-opened may be disallowed.</p> <p>Additionally, the trigger would not allow licensees to re-open, if DUoS</p>	<p>Amend the wording of SpC 3.2.75(a) to say “an increase in (i) current or forecast load-related constraints on the Distribution System that are in place at the time the licensee makes a Load Related Expenditure Re-opener application relative to the constraints associated with the forecast demand used by Ofgem to set allowances or (ii) the proportion of expenditure associated with load-related constraints on the Distribution System to be funded through Network Charges relative to the assumptions used by Ofgem to set allowances that are in place at the time the licensee makes a Load Related Expenditure Re-opener application”.</p> <p>Forecast Demand and Actual Demand should be defined terms.</p>

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			System” which is unclear and could potentially be interpreted more broadly than load-related expenditure.	<p>customers are expected to fund a much greater proportion of load-related expenditure than was assumed in baseline allowances. This scenario must be allowed for here, given Ofgem’s proposal that it will not adjust baselines for years 3 to 5 of RIIO-ED2 to take account of the outcome of the Access SCR.</p> <p>Similarly, the trigger needs to allow licensees to include extra expenditure, relative to baseline allowances, due to behavioural change associated with the outcome of the Access SCR, for example more connections on constrained parts of the network. Ofgem does not currently propose to reflect these in baseline allowances for any year of RIIO-ED2.</p>	
18	SpC 3.2.75 (b)(ii)		<p>This paragraph does not explain how the materiality assessment should be made for any second or subsequent re-opener process.</p> <p>This is particularly important given the expectation that there</p>	It is unclear whether the materiality threshold only needs to apply for the first re-opener application or whether any second application needs to be materially different to the first.	Further detail should be provided to clarify the necessary calculation.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			will be two licensee-triggered windows for this re-opener.		
19	SpC 3.2.77(a) Load Related Expenditure Re-opener Guidance paragraph 1.6		<p>SpC 3.2.77(a) requires licensees to “[give] details of the circumstances under paragraph 3.2.5 that exist”.</p> <p>This paragraph should refer to paragraph 3.2.75.</p> <p>Paragraph 1.6 of the Load Related Expenditure Re-opener Guidance has a similar requirement.</p> <p>In the case of increases in load-related constraints, licensees will only be able to comply with this requirement if they have access to the detailed information under-pinning the assumptions made by Ofgem in setting allowances.</p> <p>This is particularly important in light of Ofgem’s proposal to only amend baselines for years 1 and 2 of RIIO-ED2 to take account of the outcome of the Access SCR. Ofgem effectively plans to use</p>	Licensees will require data from Ofgem in order to comply with this requirement.	<p>Amend paragraph to refer to paragraph 3.2.75.</p> <p>Licensees must be provided with the detailed assumptions used by Ofgem in setting baseline allowances.</p>

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			different assumptions for different components of the baseline.		
20	SpC 3.2.75	Load Related Expenditure Re-opener Guidance	The “Forecast demand” section of the Load Related Expenditure Re-opener Guidance does not make it clear that the relevant forecast demand to consider is that used by Ofgem to set allowances that are in place at the time of the re-opener application.		The Load Related Expenditure Re-opener Guidance should be updated to align with the licence condition, once the changes outlined above have been implemented.
21	SpC 3.2.77	Load Related Expenditure Re-opener Guidance	<p>The “Application Requirements” section of the Load Related Expenditure Re-opener Guidance is inconsistent with the requirements of SpC 3.2.77.</p> <p>For example, it only refers to forecast demand, whereas details of actual demand may also need to be submitted.</p>	There is confusion about the scope of the required re-opener evidence.	The Load Related Expenditure Re-opener Guidance should be updated to align with the licence condition, once the changes outlined above have been implemented.
22	Load Related Expenditure Re-opener Guidance		Paragraph 1.2 of the “Forecast demand” section of the Load Related Expenditure Re-opener Guidance inappropriately requires licensees to explain how the forecast has been informed	This requirement is inappropriate for a re-opener application.	This paragraph should be removed.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			by the Future Energy Scenarios and Committee of Climate Change assumptions.		
23	Load Related Expenditure Re-opener Guidance		The section “Access Reform costs” is not yet populated.	This is a key section for licensees to have sight of in order to consider whether the allowance adjustment mechanisms and baseline allowances have been set in an internally consistent manner.	This section is very important and needs to be added to the document.
24	SpC 3.2.75(b)(i)		This paragraph only permits Ofgem to make allowance adjustments where the Load Related Expenditure is not provided for in baseline allowances.	Given Ofgem’s approach to allowance setting, it is unclear whether Ofgem will have sufficiently granular information to confirm which activities have or have not been included in baseline allowances.	
The process to be followed in the case of failed volume driver “check metrics” is unclear					
25	Load Related Expenditure Volume Drivers Governance Document Check metrics		The volume driver mechanism places undue emphasis on “check metrics”. These metrics are (a) imperfect indicators of the efficiency and efficacy of load-related expenditure and (b) based on data that have not historically been reported and may be subject to reporting	There is the risk that this process turns a mechanism that is intended to ensure that the networks are not blockers to net zero into a mechanism that materially delays or curtails essential funding. There is the risk of the metrics “failing”, so leading to protracted/	Considerable further work is required to develop these metrics.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			inconsistencies that may affect both the setting of target ratios and their application to different licensees.	<p>intrusive discussions about efficiency of volumes and the risk of no allowances being provided.</p> <p>There is the risk that this process operates differently for different licensees due to differences in interpretation of metric reporting requirements, leading to regional differences in operation.</p> <p>There is the risk that licensees delay investment due to concerns about whether volumes will be allowed.</p>	
26	Load Related Expenditure Volume Drivers Governance Document Paragraph 2.32	SpC 3.9.4 SpC 3.9.6	<p>This paragraph sets out that “If all checks produce green flags then costs and volumes will be rewarded”</p> <p>This suggests that the mechanistic calculations in the licence condition will be “over-ruled” and incurred costs awarded.</p>	There is a potential conflict between the licence and guidance.	Rephrase the paragraph to say “If all checks produce green flags, the volumes will be used for volume driver calculations without any adjustment”.
27	SpC 3.9.4 SpC 3.9.6 SpC 3.9 Appendix 1	Load Related Expenditure Volume Drivers	The process to be followed if any check metric is “red flagged” as incomplete. It also assumes that one “red flag” metric results in all	The process is disproportionate for a mechanism that is intended to be automatic.	As set out above, considerable further work is required to develop these metrics.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
	SpC 3.9 Appendix 2	Governance Document Paragraph 2.33	<p>volumes being investigated, even if the metric only relates to a sub-set of volumes.</p> <p>The process ends with licensees submitting further information to Ofgem, but the governance document does not explain what Ofgem will do with that data and how the values to be used in calculations for SpC 3.9 will ultimately be determined.</p> <p>The process is unclear as to whether the volumes associated with metrics that have been passed will be automatically allowed.</p>	As the volume driver “over-writes” ex-ante allowances, the process could potentially be interpreted as suggesting the possibility of no allowances, or delayed allowances being provided in this key area.	<p>Additionally, when drafting the associated process:</p> <ul style="list-style-type: none"> • Further investigation should be limited to relevant volumes, with any volumes associated with metrics that have been passed being automatically allowed; and • The process needs to include details of how Ofgem will ultimately conclude on the appropriate volumes to use for volume driver calculations. This should include the circumstances under which volumes that are lower than actual volumes will be used in calculations.
28	Load Related Expenditure Volume Drivers Governance Document Paragraph 2.33		<p>The wording “licensees have exceeded the baseline LRE allowances set at the start of RIIO-ED2” is unclear.</p> <p>It does not explain which costs will be compared to which baselines.</p> <p>For example, are costs:</p> <ul style="list-style-type: none"> • in year actuals; 		We are unclear as to Ofgem’s intended policy here.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			<ul style="list-style-type: none"> • cumulative actuals to date; or • actual spend or re-calculated allowances based on adjusted volumes (which could differ to actual spend)? <p>And are baseline allowances:</p> <ul style="list-style-type: none"> • in year baseline allowances; • cumulative baseline allowances to date; or • baseline allowances for the full 5 years of RIIO-ED2? <p>We also do not understand why this test would apply to all LRE baseline allowances rather than just those within the SRVD scope of the volume driver.</p> <p>It is also unclear whether it is only those volumes that cause the relevant baseline allowance to be exceeded that will be subject to extra scrutiny or all volumes.</p>		
29	Load Related Expenditure Volume Drivers Governance Document		These paragraphs place a requirement on licensees to provide independently validated audit of the methodology used		Ofgem needs to articulate why this is necessary and provide more guidance on what is expected.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
	Paragraph 2.13 and 2.14		<p>prior to the start of the price control period.</p> <p>This requirement is not specified sufficiently clearly for licensees to understand what they are obliged to do.</p> <p>We are also unclear why Ofgem believes that the application of licensees' usual data assurance processes will be insufficient.</p>		
30	<p>Load Related Expenditure Volume Drivers Governance Document</p> <p>Paragraph 2.16</p>		The formula at paragraph 2.16 cannot be viewed.	Licensees cannot assess the intended operation of this metric.	Format formula so that the full formula is visible in document.
31	<p>Load Related Expenditure Volume Drivers Governance Document</p> <p>Paragraph 2.29</p>		This paragraph requires licensees to submit an ex-ante forecast estimated number of LCTs installed. However, the licensee's forecast will not have a direct relationship with the baseline allowances set by Ofgem at Final Determinations.		This requirement on licensees should be removed. Ofgem should provide this data to licensees.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
The boundary between pass-through and the Load Related Expenditure Re-opener is not clearly defined					
32	SpC 6.1.3	Load Related Expenditure defined term	The pass through formula includes all Transmission Connection Point Charges (in the TBt term).	There is probably a partial double count of funding of transmission connection point charges.	<p>Based on policy discussions, we assume that Ofgem's policy intent is for the RIIO-ED1 approach to continue.</p> <p>Adjust pass through formula to include Pass-Through Transmission Connection Point Charges</p> <p>Reinstate RIIO-ED1 term "Pass-Through Transmission Connection Point Charges" into the RIIO-ED2 licence.</p> <p>Alternatively, remove transmission connection point charges from the scope of Load Related Expenditure and added into the pass-through formula.</p>
33	Load Related Expenditure defined term		<p>The term "new transmission capacity charges" used in this defined term is not capitalised.</p> <p>It is unclear whether this is intended to match New Transmission Capacity Charges term that is a defined term for RIIO-ED1.</p>	<p>It is unclear whether all Transmission Connection Point Charges are picked up across the combination of the Pass-through and Load Related Expenditure Re-opener conditions.</p> <p>Consequently, there is the potential for unfunded costs or double counting of allowances.</p>	<p>Refer to "New Transmission Capacity Charges" in definition of Load Related Expenditure</p> <p>Reinstate RIIO-ED1 term "New Transmission Capacity Charges" into the RIIO-ED2 definitions list (updated for RIIO-ED2 dates)</p>

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
It is premature to assume that all Strategic Investment projects should be subject to evaluative PCDs					
34	Strategic Investment defined term	Load Related Expenditure Re-opener Guidance paragraph 1.11	<p>The definition of Strategic Investment is very broad. Taken literally it would potentially include even LV projects that are being deployed in anticipation of longer-term need.</p> <p>Paragraph 1.11 of the Load Related Expenditure Re-opener Guidance sets out that all Strategic Investment projects will be set as evaluative PCDs.</p>	If the literal interpretation of the Strategic Investment defined term is used, this would lead to disproportionate reporting and review processes being initiated.	<p>As set out in our feedback on SpC 3.3, it is inappropriate for the licence to presume that an evaluative PCD will automatically be created as that may not be the most appropriate regulatory treatment. The introduction of any PCDs associated with Strategic Investment should be introduced via a modification made under section 11A of the Act.</p> <p>We recognise that licensees may need to provide details of potential Strategic Investment in any re-opener application and so SpC 3.2.77(b) should be retained, but the requirements in SpC 3.2.77(d) and (e) and SpC 3.2.80(b) should be removed and Ofgem can then take the decision on a case by case basis as to what the appropriate regulatory treatment should be and a PCD can be created if deemed appropriate.</p> <p>As Ofgem currently doesn't propose any ex-ante funded Strategic Investment projects, we think Ofgem's expectation is that there will be far fewer Strategic Investment projects than the defined term currently suggests.</p>

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
					This term needs to be updated to better reflect the intent that Ofgem has verbally shared, which is that Strategic Investment projects are very material one-off projects that may merit being subject to a PCD mechanism.
The net to gross adjustment for Load Related Expenditure needs much more consideration					
35	SpC 3.11 general		The need for this condition has neither been justified nor subject to policy consultation.	Introduction of this condition is potentially unnecessary as it has not been considered in the design of other aspects of the toolkit of load-related mechanisms.	Ofgem's proposed continuation of the net to gross adjustment for Load Related Expenditure into RIIO-ED2 needs more consideration. Ofgem has not consulted on this proposal.
36	SpC 3.11 general		Ofgem's proposal to adjust allowances relative to the baseline percentage of Gross Load Related Expenditure is flawed in the context of Ofgem's decision to only amend baseline allowances to take account of the outcome of the Access SCR for two of the five years of RIIO-ED2. The changes to the Common Connection Charging Methodology as a result of the Access SCR will inevitably lead to a much greater proportion of	If Ofgem only amends baseline allowances for years 1 and 2 of RIIO-ED2, it is likely that all licensees will show a material deviation from the percentage assumed in those baselines. If the change also resulted in a material change in net expenditure, this will already have been subject to re-opener applications and changes to volumes recorded in the volume driver. It is, therefore, unclear what purpose this additional adjustment would serve.	This condition has not been drafted in a manner that is compatible with Ofgem's proposed approach to setting baseline allowances for years 1 and 2 of RIIO-ED2 on a different basis to years 3 to 5 in respect of the outcome of the Access SCR. There are a number of very material drafting issues with this condition.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			load-related expenditure being funded by DUOS customers.		
The net to gross adjustment for Load Related Expenditure basis is unclear, double counts TIM adjustments and introduces a risk of unconstrained allowance modifications					
37	SpC 3.11.1		The requirement that the directed value to adjust totex “receives neutral treatment by the Totex Incentive Mechanism” is misaligned with the treatment of associated costs and customer contributions in TIM.	As customer contributions are treated as “negative totex” for TIM purposes, any adjustment that does not correctly interact with the TIM mechanism would seem to partially double count the adjustment e.g. in the event of materially lower customer contributions than expected, licensees would recover ~50% from customers through TIM and then have a NGLREt adjustments applied on top of that (up to a further 100%).	It would seem much cleaner to adjust totex allowances to ensure that relevant interactions operate correctly rather than to write the calculations to determine a totex neutral value that reflects the differing TIM values etc. This drafting assumes this approach. (But if Ofgem prefers to continue with totex neutral we can consider the necessary algebra). Amend paragraph 3.11.1 to include the standard wording “This contributes to the calculation of the Totex Allowance (in relation to which see the ED2 Price Control Financial Model).”
38	SpC 3.11.9		The paragraph places no constraint on the quantum of adjustment that Ofgem can direct.	Licensees face the risk of unconstrained allowance adjustments following a subjective review of a report.	Paragraph 3.11.9 needs to (a) constrain the maximum quantum of adjustment and (b) better explain how the directed value will be calculated/the factors that will be considered.
39	SpC 3.11.7 SpC 3.11.9		Neither the information to be provided by licensees, nor the basis on which Ofgem may modify allowances makes reference to the fact that the		We do not have sufficient understanding of Ofgem’s intended approach to calculating

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			percentage funded by connecting customers will change for years 3 to 5 of RIIO-ED2 due to Ofgem's proposal to not amend baseline allowances to take account of the outcome of the Access SCR.		allowance adjustments to propose the text or algebra required to achieve this. There needs to be a clear record of the basis of the LRE calculations on both a gross and net basis at Final Determinations, including unit costs used in SpC 3.9 to understand what is "provided for" in baseline allowances.
40	SpC 3.11.9		<p>Ofgem's policy for what level of adjustment to totex allowances would be merited if the actual percentage falls outside the Specific Customer Funded Reinforcement Percentage Band is unclear.</p> <p>A number of very different interpretations could, therefore, be made e.g.:</p> <ul style="list-style-type: none"> • adjustment for amount outside deadband or from baseline; • adjustment to reflect actual net expenditure; • adjustment to reflect actual percentage; or • adjustment to reflect actual levels of customer contributions. 	<p>The subjectivity in the possible interpretations of the various adjustment calculations that could be inferred from current wording leads to a very material range of possible outcomes.</p> <p>Licensees cannot predict from the information in the condition how their allowances may be modified.</p>	

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
41	SpC 3.11.9(a)		The intended interpretation of the phrase “has not justified” in this sentence is unclear.	This suggests that, provided the licensee can explain what has driven the change in percentage customer funded, no adjustment will be required. This does not seem to align to Ofgem’s articulation of intended policy.	
42	SpC 3.11.9(b) SpC 3.11.2	SpC 3.2 SpC 3.9	<p>It is unclear how Ofgem will determine whether costs have “been provided for” for under volume driver / re-opener when assessing the need for and quantum of any net to gross adjustment for Load Related Expenditure.</p> <p>Similar unclear words are used in introductory paragraph 3.11.2.</p>	<p>The most likely scenario that would lead to a licensee triggering this mechanism results from Ofgem’s proposal that it will only adjust baseline allowances for the outcome of the Access SCR for years 1 and 2 of RIIO-ED2. This has the effect of setting a baseline percentage of Gross Load Related Expenditure expected to be delivered via Specific Customer Funded Reinforcement that is much higher than is actually expected to be the case. In this scenario, it is likely that licensees will have already triggered the Load Related Expenditure Re-opener to seek allowances for the net costs.</p> <p>In the case of any increased recovery from connecting customers, the costs will often have been provided for.</p>	

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
				Also, as the volume driver mechanism operates annually, adjustments will have already been made to reflect actual activity.	
Important calculations required for net to gross adjustment for Load Related Expenditure are unclearly defined					
43	SpC 3.11.6 (a) SpC 3.11.7 SpC 3.119		The condition relies heavily on the term “Relevant Expenditure”, which is defined as a percentage rather than as expenditure. In turn, this definition relies on the defined term Actual Percentage of Gross Load Related Expenditure, which is not defined.	There is confusion over the scope of key calculations.	The term “Actual Percentage of Gross Load Related Expenditure” should be used instead of “Relevant Expenditure” in all instances in this condition (i.e. use a term that is clearly expected to be a percentage). (see below for comments on how this should be defined) Delete the defined term Relevant Expenditure.
44	Gross Load Related Expenditure defined term		The term is defined as baseline costs (appendix 5) but (a) this references the incorrect appendix and (b) it needs to be applied as an actual calculation in some instances. The definition also refers to SpC 3.13 rather than 3.11.	The definition of a key calculation input value is confusing and could imply that the denominator of key percentage calculations should always be the baseline costs rather than actual costs.	Define Gross Load Related Expenditure as means “the total amount of expenditure incurred by the licensee in respect of cost areas that make up Load Related Expenditure before the deduction of Specific Customer Funded Reinforcement.” This can be prefixed with “baseline” or “actual” to differentiate between key values referred to in calculations and appendices.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
45	Actual Percentage of Gross Load Related Expenditure defined term		This key calculation needs to be defined.	<p>The key metric on which this mechanism is expected to operate is not defined. Different interpretations of this calculation are possible and could result in materially different answers.</p> <p>For example, it is not clear that the calculation is made across the 5 years of RIIO-ED2.</p>	<p>Add the defined term Actual Percentage of Gross Load Related Expenditure: Means “actual expenditure on Specific Customer Funded Reinforcement for the Price Control Period expressed as a percentage of actual Gross Load Related Expenditure (including any expenditure on Strategic Investment projects) for the Price Control Period”.</p> <p>Capitalise this term in SpC 3.11.2.</p> <p>Use this term instead of “Relevant Expenditure” (as explained above).</p>
46	Specific Customer Funded Reinforcement Percentage Band defined term		<p>The definition incorrectly refers to Appendix 2 rather than appendix 4.</p> <p>Also, it states that it “represents the licensee’s Baseline Specific Customer Funded Reinforcement expressed as a percentage of Gross Load Related Expenditure.” Baseline Specific Customer Funded Reinforcement is not a defined term so should have a lower case B.</p>		<p>Define Specific Customer Funded Reinforcement Percentage Band as: “means the interval between the upper and lower threshold percentages set out against the licensee’s name in Appendix 4 where the relevant percentages represent the licensee’s Baseline Specific Customer Funded Reinforcement expressed as a percentage of baseline Gross Load Related Expenditure.”</p>

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			There should also be reference to baseline in relation to the Gross Load Related Expenditure.		
The submission requirements in the net to gross adjustment for Load Related Expenditure need to be reviewed to reflect the fact that baseline assumptions will be set by Ofgem					
47	Part C SpC 3.11.6		Part C of paragraph SpC 3.11, and paragraph 3.11.6 in particular, seem to be phrased assuming that this adjustment will reduce allowances. However, the more likely scenario is that licensees will recover a lower proportion from connecting customers and an increase to allowances will be justified - because of Ofgem's proposed approach to setting allowances to take account of the Access SCR.	There is a risk that this condition is inappropriately interpreted to be an asymmetric adjustment.	Amend paragraph 3.11.6 to read: The licensee must report to the Authority by 31 July 2028 whether: (a) its Actual Percentage of Gross Load Related Expenditure has fallen inside or outside the Specific Customer Funded Reinforcement Percentage Band; and (b) if its Actual Percentage of Gross Load Related Expenditure has fallen outside the Specific Customer Funded Reinforcement Percentage Band, whether there is a justified reason for an adjustment to be made under Part D."
48	SpC 3.11.6		The paragraph is unclear as to whether licenses are required to submit a report if their percentage falls within the deadband.	The obligation is unclear. We assume that Ofgem would require the details of the outturn percentage from all licensees.	
49	SpC 3.11.7		Paragraph 3.11.7 requires licensees to provide detailed information about changes	It is unclear whether licensees will have sufficient information about Ofgem's assumptions in setting	Submission requirements should be taken up a level to allow the licensees to provide the most relevant evidence to Ofgem.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			<p>relative to the baseline assumptions.</p> <p>Baseline assumptions will be set by Ofgem at Final Determinations. It is unclear to licensees whether Ofgem's allowance setting approach will provide details such as insourcing/outourcing assumptions for the notionally efficient licensee that would be required to meet this.</p>	<p>baseline allowances to meet the specific requirements of this paragraph.</p> <p>It also does not require details of some factors that are more likely to drive such a change in the customer funded proportion, such as the impact of the move to the Access SCR basis of charging for connections for years 3 to 5 of RIIO-ED2, or differences between demand assumptions made by Ofgem and actual demand.</p>	<p>Amend paragraph 3.11.7 to read:</p> <p>"Where the licensee's Actual Percentage of Gross Load Related Expenditure has fallen outside its Specific Customer Funded Reinforcement Percentage Band, the licensee must include reasons why the proportion of Gross Load Related Expenditure that was to be delivered through Specific Customer Funded Reinforcement is materially different to the proportion assumed at the outset of the Price Control Period."</p> <p>Ofgem must provide licensees with sufficient detail regarding its assumptions at Final Determinations to allow the licensee to do this.</p>
50	SpC 3.11.7(b)		<p>The statement in SpC 3.11.7(b) is illogical.</p> <p>This sub-paragraph is worded:</p> <p>"reasons why reinforcement that was forecast to be funded through Gross Load Related Expenditure at the outset of the Price Control Period has in fact been delivered through Specific Customer Funded Reinforcement;"</p>	<p>This requires the licensee to report on a scenario than cannot occur.</p> <p>This may also create confusion regarding the interpretation of key terms that are used in calculations.</p>	

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			By definition, Specific Customer Funded Reinforcement is always included in Gross Load Related Expenditure.		
SpC 3.11 Part B suggests that inappropriate expectations will be placed on licensees					
51	SpC 3.11 Part B SpC 3.11.5		<p>This title and paragraph are misleading.</p> <p>SpC 3.11.5 “The baseline percentage of Gross Load Related Expenditure that it is anticipated the licensee will deliver via Specific Customer Funded Reinforcement” is misleading because licensees are not funded to deliver a percentage of Gross Load Related Expenditure. They are funded to deliver Load Related Expenditure.</p>	<p>This Part is confusing and misleading. It suggests an inappropriate target on licensees.</p> <p>In particular, it may suggest a conflict with licensees’ charging obligations under the Common Connections Charging Methodology.</p>	<p>Suggest Part B is completely deleted.</p> <p>No equivalent text has been deemed required in SpC 3.2 or SpC 3.9 so not needed here either.</p> <p>If Ofgem believe some text should be retained (perhaps to introduce appendix 2?), the following could work:</p> <p>“The Specific Customer Funded Reinforcement assumed in baseline allowances expressed as a percentage of Baseline Gross Load Related Expenditure is set out in ...”</p>
Width of deadband for net to gross adjustment for Load Related Expenditure requires more consideration					
52	SpC 3.11 Appendix 4		While Ofgem has not consulted on the issue, we understand that Ofgem proposes that any “deadband” would be set to $\pm 5\%$	Thought needs to be given to how the deadband should be established in this condition.	We suggest that more consideration is given to the width of the deadband, especially in light of Ofgem’s approach to setting allowances to reflect the Access SCR.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			<p>from percentage assumed when setting baseline allowances.</p> <p>This percentage has not been subject to consultation elsewhere.</p>	<p>A number of factors have changed since the $\pm 5\%$ deadband used in RIIO-ED1 was set:</p> <p>(1) For years 1 to 2 of RIIO-ED2, the change to connections charging rules as a result of the Access SCR mean that much tighter rules have been established to determine what connecting customers pay. This removes uncertainty associated with interpretation of connection charging rules, as well as meaning that many more projects will be DUoS funded than was the case in RIIO-ED1;</p> <p>(2) Ofgem's proposal that baseline allowances will only be amended for years 1 and 2 of RIIO-ED2 means that much lower percentage contribution rates than baseline assumptions are likely to be seen for years 3 to 5 of RIIO-ED2;</p> <p>(3) Ofgem's proposal to base baseline allowances on a relative low load growth scenario will result in the same percentage representing a much bigger value in pounds than</p>	

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
				<p>would have been the case if a more central scenario had been chosen; and</p> <p>(4) The introduction of the load-related expenditure volume driver means that allowance adjustments for many of the lower voltage activities are made automatically, rather than subject to the wide deadband of the RIIO-ED1 re-opener.</p>	
Timing of load uncertainty mechanism (UM) adjustments is inconsistent with Ofgem's recent proposal that baseline allowances will only be adjusted to take account of the Access SCR for the first two years of RIIO-ED2					
53	Load UM conditions general		<p>Ofgem's recent consultation position proposing to only amend baseline allowances for the first two years of RIIO-ED2 to take account of the outcome of the Access SCR means that all licensees are now more likely to trigger allowance modifications through all load UMs during RIIO-ED2.</p> <p>That consultation also proposed that two re-opener windows</p>	<p>The re-opener windows in draft SpC 3.2 do not align to those proposed in the Access SCR consultation.</p> <p>The timing of potential allowance modifications means that licensees will not have certainty of year 3 allowances in time for the commencement of that year.</p> <p>Given the material changes to required expenditure that are anticipated, this creates a risk of delays in sufficient funding meaning</p>	Ofgem should review the timings of the various triggers in light of its Access SCR outcome proposals.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			<p>would be required for the Load Related Expenditure Re-opener.</p> <p>The load uncertainty mechanisms are not currently designed to provide for modification of year 3 allowances in time for the commencement of that year.</p> <p>Furthermore, the timing difference between the Load Related Expenditure Re-opener window and the adjustment to Load related expenditure volume driver caps means that Ofgem will not be able to take account of both components at the same time.</p>	that distribution networks become a blocker to LCT uptake.	
54	SpC 3.2.76		Dates do not correspond with the windows proposed in the recent Access SCR consultation.		
Interactions between load-related conditions and other RIIO-ED2 conditions also needs to be considered					
55	Load “toolkit” conditions	Other conditions	Once the issues in the core “toolkit” of documents have been resolved, further work will be required to ensure that the core mechanisms interact correctly		We have focussed our attention primarily on identifying issues with the core “toolkit” of load-related conditions.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			with other RIIO-ED2 conditions. We have identified the following further conditions that need to correctly interact with the toolkit of load-related UMs.		Once issues identified with the core conditions have been resolved, we are happy to move on to support the resolution of these wider issues.
56	Load “toolkit” conditions	SpC 3.2 Storm Arwen Re-opener	<p>The boundary between conditions needs to be clearly defined.</p> <p>The Storm Arwen Re-opener may result in fundamental changes to planning standards which could include, for example, changes to interconnection standards, which would normally be categorised as LRE.</p>		
57	Load “toolkit” conditions	SpC 3.2 West Coast of Cumbria Re-opener (ENWL)	<p>The boundary between conditions needs to be clearly defined.</p> <p>The West Coast of Cumbria Re-opener will result in new assets, including new GSPs, resulting in amended LRE (inc TCP) requirements.</p>		We note the additional re-opener guidance considers interaction with any other UM.

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
			It may remove assets that were previously scheduled to be subject to LRE.		
58	Load “toolkit” conditions	SpC 3.6 Net Zero	<p>The boundary between conditions needs to be clearly defined.</p> <p>The definition of Net Zero Development includes “<i>new investment arising from the agreement of a Local Area Energy Plan</i>” – commonly these would result in LRE.</p>		
59	Load “toolkit” conditions	SpC 3.7 Co-ordinated Adjustment Mechanism	<p>The boundary between conditions needs to be clearly defined.</p> <p>The Co-ordinated Adjustment Mechanism may transfer LRE projects (including Strategic Investments) between licensees or between electricity distribution and transmission.</p> <p>Costs may also be moved from TCP to LRE or vice versa.</p>		

	Reference 1	Reference 2 (for interaction/ conflict issues)	Issue	Consequence	Assumptions/ suggested fix/ alternative drafting
60	Load “toolkit” conditions	SpC 3.8 Green Recovery	<p>The boundary between conditions needs to be clearly defined.</p> <p>Some Green Recovery Agreed Schemes may deliver load-related outcomes.</p>		
61	Load “toolkit” conditions	SpC 3.12 Off-gas grid mechanistic Price Control Deliverable (UKPN)	<p>The boundary between conditions needs to be clearly defined.</p> <p>The Off-gas grid mechanistic Price Control Deliverable relates to provision of capacity ahead of need to Off-Gas Grid Customers.</p>		
62	Load “toolkit” conditions	SpC 9.X Whole System Strategies	<p>The boundary between conditions needs to be clearly defined.</p> <p>Policy and the draft condition not yet available but may affect expenditure that could be categorised as LRE.</p>		

Appendix 5**Uncertain costs re-openers**

In the RIIO-T2 CMA appeal, the CMA confirmed that the Authority can introduce a licence condition which has a mechanism for its later modification (what Ofgem referred to as “self-modification” conditions). This is permitted under section 7(5) of the Act.

However, any ‘self-modification’ licence condition must meet the requirements of section 7(5) of the Act. In the RIIO-T2 appeal, the CMA confirmed, in line with the statutory requirements, that, in order for such a condition to be lawful, the condition must specify (a) the time; (b) the manner; and (c) the circumstances in or under which a modification can be made.

If such criteria are correctly set out in the condition itself, the licensee in question should be able to understand the potential impact on it of a future modification at the outset of the price control simply by reference to the condition.

These comments address the five key issues that we consider must be addressed to ensure that the re-openers can be fully understood, they work in practice and so that they satisfy the requirements of section 7(5) of the Act:

- a) The wording used to require “evidence of efficiency” in order to make a modification is unclear and too ambiguous (see Section 1);
- b) The process that will be followed when the Authority triggers a re-opener is unclear and requires clarification (see Section 2);
- c) Inconsistency in the use and presentation of the materiality thresholds (see Section 3);
- d) Clarification of the scope of certain re-openers (see Section 4); and
- e) The importance of using consistent language throughout the re-openers to remove the potential for confusion and unintentional distinctions (see Section 5).

1. Proposed “evidence test” wording is unclear

Twelve¹ of the re-opener mechanisms set out that the Authority may only make modifications under each of the re-openers if (variations of) “*there is evidence to demonstrate that the modification to allowances is efficient*”.

Without change or elaboration, we do not believe that this wording sufficiently specifies the circumstances under which a modification can be made. It is, therefore, not possible for licensees to understand the potential impact on them of a future modification. It is not sufficiently clear to understand how the requirement will be met in practice.

¹ All re-openers, except the Co-ordinated Adjustment Mechanism (CAM)

Specifically:

- (i) It is not clear whether it is dependent on the licensees providing the requisite evidence to satisfy the test up front or if it could be met following Ofgem's assessment of the representations. For example, it is assumed that Ofgem would carry out an assessment of efficiency after receipt of information on costs from the licensee. In such circumstances, the outcome of Ofgem's analysis could constitute the requisite evidence. However, this is not what the condition says. The requirement is for evidence to *exist* that demonstrates that the modification to allowances is efficient. This, combined with the lack of methodology or criteria relating to any potential assessment by Ofgem of this evidence, means that it is difficult to fully understand the implications of any proposed modification.
- (ii) Given the nature of uncertainty that exists in the areas that have re-opener conditions, it is very likely that there will be situations where it is difficult to show independent evidence or conduct analysis to prove that the modification to allowances is efficient. For instance, where a proposed project or activity is innovative or where there is a lack of historical or comparative data to allow analysis to demonstrate "efficient" costs but where it is obvious an allowance should be made. In addition, in a number of areas the need for additional allowances will be driven by changes in legislation or other requirements, which may not otherwise be justifiable as "efficient".
- (iii) Ofgem does not specify a methodology or set of criteria for what is to be considered "efficient". This has the potential to allow Ofgem to make an arbitrary assessment of efficiency which may not reflect the actual efficient costs to individual licensees of the activities for which funding is being requested or reflect wider benefits of any potential intervention (e.g. environmental or societal).

Whilst section 7(5) of the Act is intended to allow for modifications whose scale is uncertain at the outset of the price control period, there should not be uncertainty about the tests to be applied in determining whether such a modification should be made. The inherent ambiguity in the language proposed by Ofgem does not provide the requisite level of specificity. The uncertainty in the process, combined with the lack of clear methodology or criteria relating to the substance of any potential assessment by Ofgem of this evidence, means that it is difficult to fully understand the implications of any proposed modification, including the circumstances in or under which a modification can be made.

There is a significant concern, therefore, that the ambiguity inherent in the 'evidence of efficiency' wording may be applied in such a way as to result in a legitimate re-opener application being rejected by Ofgem. This is because, by explicitly including "efficiency" as a criteria but failing to provide sufficient clarity about what it means in this particular context, or how it will be assessed, provides an easy route for rejection of re-openers on a basis which, when limited to judicial review grounds, would be very difficult for a licensee to challenge.

We propose two alternative solutions, either of which would mitigate these concerns:

- a) Replace the “evidence of efficiency” test with a provision allowing Ofgem to assess that *“the licensee has provided such detailed supporting evidence as is reasonable in the circumstances”*; or
- b) Replace the “evidence of efficiency” test with a (positive) power to apply an adjustment for inefficiency to licensees' applications where Ofgem has conducted an assessment and has concerns. Suggested wording of a new sub-clause within each re-opener could be *‘Where the modification has been requested by the licensee under paragraph x.x.x, the Authority may undertake an assessment of the efficiency of those costs and, where inefficiency is found, the Authority may reduce the value requested by the corresponding amount’*.

These alternatives would allow Ofgem to act if either it felt that insufficient evidence had been provided, or it had undertaken an assessment and identified areas of inefficiency. For the second option, the re-opener guidance must then expand on the efficiency review process.

2. The process for Authority instigated re-openers is unclear

Seven of the re-openers set out in SpC 3.2 include provision for the Authority to ‘instigate the re-opener’. However, the conditions are silent on the process that the Authority would follow when instigating the re-opener and do not sufficiently specify the circumstances under which a modification can be made. It is, therefore, not possible for licensees to understand the potential impact of a future modification on them.

It is possible that when setting policy in each of these re-opener areas, there may have been some confusion and conflation of the process of Ofgem directing a new and additional window for the re-opener (following which licensees submit their applications as they would under the pre-set windows) and the process for Ofgem instigating a re-opener at any time.

Indeed, under issue number 23 from the issues log for the Electricity System Restoration Re-opener (SpC3.3 Part D), a request for guidance was made on the process around Ofgem instigating the re-opener. This issue was closed by Ofgem because Annex 6 to the Re-opener Guidance and Applications Requirements Document had been drafted to set out the process “that the Authority will undertake when considering whether to direct a re-opener window under the Electricity System Restoration Re-opener”. It should also be noted that such guidance only exists for the Electricity System Restoration re-opener and not for the other eleven re-openers where the Authority can direct an additional window.

To clear up this confusion, we believe Ofgem needs to:

- a) Confirm whether the processes around directing an additional window and instigating a re-opener are the same or different;

- b) Include a new additional sub-condition under SpC 1.3 Common Procedures in the licence, which clarifies the processes around directing an additional window and/or instigating a re-opener under SpC 3.2 (depending on the answer to (i) above); and
- c) Include a new sub-clause within each relevant re-opener licence condition to clarify that, before making a modification as a result of instigating the re-opener, the Authority has:
 - i) Requested from the licensee and been provided by the licensee with such detailed supporting evidence as is reasonable in the circumstances;
 - ii) Given an explanation of the rationale for the proposed direction and the basis of the calculations used in any modified allowance; and
 - iii) Clearly stated that the relevant circumstances under which the Authority may trigger the re-opener are the same as the circumstances under which a licensee may trigger the re-opener.

In the absence of providing this additional clarification, it is questionable whether this aspect of the relevant re-openers is consistent with the legal requirements of Section 7.5 of the Act.

In addition, there are further concerns with the inappropriate way in which some of the re-openers operate and these are outlined below.²

3. **Materiality threshold**

We have both licence drafting and policy-related points to raise in relation to the materiality threshold, as follows:

- a) The wording used to describe the application of the materiality test is phrased inconsistently in different re-openers. It is not always clear whether the materiality threshold is to be assessed relative to the amount of allowance that has previously been provided, either via baseline allowance or under an earlier re-opener application. This makes the scope of the re-opener unclear and some licensees who may legitimately expect an allowance adjustment may not be entitled to one. For those conditions where it is Ofgem's policy that a materiality threshold should apply, we suggest that the following standard wording be used:

"The [XXX] Re-opener may be used where there has been a change in the [XXX] costs the licensee has incurred or expects to incur, relative to any previous allowances for such costs, that exceeds the Materiality Threshold.";

- b) The definition of Materiality Threshold is currently not populated. We are unclear whether Ofgem's intention is to include a table in the definitions list showing the Materiality Threshold that is applicable to each licensee. Given that these are key values that are relied on by many

² The list specifically excludes and issues relating to the LRE re-opener, LRE volume driver, Cyber re-openers and associated conditions, as they are dealt with elsewhere in this response.

different conditions, they would merit a more prominent location in the licence and we suggest adding a new appendix to SpC 3.2; and

- c) Some re-openers have materiality thresholds and others do not. Initial verbal clarification from Ofgem to allow licensees to understand the rationale behind this was that those re-openers that relate to regulatory change/compliance-related activities would not have a materiality threshold as licensees should not have to face financial exposure from mandatory requirements. Following this logic through, the materiality thresholds should be removed from the Environmental and Storm Arwen re-openers.

4. **Clarification of scope**

In addition to our separate feedback on the various load-related and Cyber uncertainty mechanisms, we believe that two uncertainty mechanisms still require some policy work to ensure the key definitions are updated to set the correct scope.

- a) Wayleaves and Diversions re-opener: The definitions of Wayleaves and Diversions Costs must capture:
 - i) All Land Rights i.e. servitudes, easements, leases and freeholds (not just wayleaves) because the type of land right selected affords the licensee the option of securing the most appropriate land right for the apparatus and the ability to obtain a secure land right in perpetuity and deliver the correct compensation due to the grantor, in effect resulting in an economic and efficient approach by removing any future threat to the apparatus;
 - ii) Land rights for existing electric lines and substations as well as for new ones installed as a result of a diversion. It should be clear that the definition covers this;
 - iii) The commercially negotiated compensation to grantors, which is a key cost within this process and grantors have a legal right to receive such compensation; and
 - iv) Those claims received prior to ED2 but not paid until ED2. If Ofgem limits the scope to NEW claims received in ED2, this would create a perverse incentive for Land Agents to abandon a previously lodged, queued claim and resubmit it during RIIO-ED2. The timing of the claim submission is largely irrelevant because it could relate to assets that are decades old. The key date is the payment date or expected payment date.
- b) PCB Interventions volume driver: Although this is a volume driver and not a re-opener, we believe it is important to set out our concerns regarding the current definition of PCB Interventions. Ofgem has recently acknowledged³ that both associated asset interventions and ground-mounted transformers may be required as part of PCB Interventions work in certain circumstances but the definition of PCB Interventions does not currently allow for:

³ Fraser Glen during SPEN bilateral 11/10/22

- i) Associated asset interventions required to support the pole-mounted transformers (such as poles and pole-mounted switchgear). There will be instances where the pole-mounted transformers cannot be replaced without these associated assets also being replaced; or
- ii) Replacement of ground-mounted transformers where the forecast load growth exceeds the capacity that can be supplied by a pole-mounted transformer.

We suggest the definitions are amended as follows:

“PCB Interventions means, in the context and scope of the PCB Interventions Volume Driver, any work undertaken by the licensee on pole-mounted transformers and associated poles and pole-mounted switchgear in order to comply with the PCBs Regulations and such work may involve the installation of a ground-mounted transformer in circumstances where the forecast load growth exceeds the capacity that can be supplied by a pole-mounted transformer.”

“PCBs has the meaning given to that term at Regulation 2(1) of either of the PCBs Regulations.”

“PCBs Regulations” means: In the case of England and Wales, the Environmental Protection (Disposal of Polychlorinated Biphenyls and other Dangerous Substances) (England and Wales) Regulations 2000, and any amendment to it.

In the case of Scotland, the Environmental Protection (Disposal of Polychlorinated Biphenyls and other Dangerous Substances) (Scotland) Regulations 2000, and any amendment to it.”

5. **Inconsistency in drafting approach further confuses the intended operation of the re-openers**

It is helpful to have the opportunity to review all conditions side-by-side as part of this consultation. In doing so, we note that a variety of similar, but not identical, phrases are used to set out the circumstances and conditions that must be met for a modification to be made.

The variation in wording compounds the issues explained above and also introduces more scope for differences in interpretation. We understand that this inconsistency is not intentional. The concern is that anyone trying to interpret them in the future will assume that, as the wording is slightly different, this was to reflect a different policy intention or approach.

In particular, there are drafting inconsistencies across the common re-opener conditions whereby only seven of the Parts in SpC 3.2 state upfront that the re-opener *“may be used where the licensee has incurred or expects to incur”* additional costs. Although this is stated later within the drafting of the other conditions, it is not immediately obvious and it is important that all re-opener conditions within the licence are drafted consistently to avoid any ambiguity. Consequently, a similar statement should be included in those conditions from which it is currently missing e.g. Physical Security, Electricity System Restoration, Cyber OT, Cyber IT and Storm Arwen.

In addition to the drafting changes to address the specific issues that we set out above, we also include details in the table below of aspects of the condition that are phrased inconsistently. Where appropriate, we also include our view of the form of words that should be used consistently throughout the condition.

<u>Section</u>	<u>Comments/wording</u>	<u>Action required</u>	<u>Changes needed to</u>
This part establishes ...	Consistent across all re-openers	No action required	
The *** re-opener may be used where...	Physical Security, Electricity System Restoration, Cyber OT, Cyber IT and Storm Arwen do not have costs incurred or expected to be incurred here	Change to include this clarity	3.2.6, 3.2.21, 3.2.44, 3.2.52, 3.2.68
The licensee may only apply ...	Inconsistency - some Parts say: "during such other periods as the Authority may direct", whilst others say "during such other periods as the Authority directs"	This should be consistent. It should also refer to the process for directing an additional window and/or instigating a re-opener discussed in section 2 above.	All parts of 3.2 should be checked and corrected where necessary
The licensee may only apply ...	Inconsistency - some Parts say: "may only apply to the Authority for modifications to this licence", whilst others say "may only apply for modifications to this licence"	Correct where the words omit "to the Authority"	3.2.15, 3.2.30, 3.2.45, 3.2.53, 3.2.613.2.76, 3.2.84, 3.2.91, 3.2.106, 3.2.113, 3.2.120
The licensee must, when making an application under the... send to the Authority a written application that:	These are naturally different depending on the re-opener itself but the final 3 should be consistent - see below	All parts of 3.2 should be checked and corrected where necessary	
	sets out any modifications to the value of *** in Appendix 1 being sought		

	explains the basis for calculating any modifications requested to allowances and the profiling of those allowances		
	provides such detailed supporting evidence as is reasonable in the circumstances		3.2.8(f), 3.2.77(g)
An application under this Part must:	Again, naturally different depending on the re-opener itself but some should be consistent.	All parts of 3.2 should be checked and corrected where necessary	
	be confined to costs incurred or expected to be incurred on or after 1 April 2023		each re-opener has a slight variation of this wording - suggest all are changed in line with 3.2.9(b) "(b) be confined to costs incurred or expected to be incurred on or after 1 April 2023"
	take account of allowed expenditure which can be avoided as a result of the modifications requested		suggest that all re-openers align to the wording used in 3.2.47(c) "(c) take account of allowed expenditure which can be avoided as a result of the modifications requested"

The following modifications to this licence may be made under the *** Re-opener:	First sub-bullet generally varies to the individual re-opener	All parts of 3.2 should be checked and corrected where necessary	
	modifications to the value of *** set out in Appendix 1		
	modifications confined to allowances for Regulatory Years commencing on or after 1 April 2023		
The Authority may only make modifications to this licence under the *** Re-opener by direction:	This opening sentence differs - in some re-openers it ends with "where", and in others, the corresponding bullets begin with "where"	One style should be chosen and then used consistently in 3.2	
	Sub-bullet 1 usually varies with the individual re-opener	Consistency can be gained	some list all the links to the trigger, but others say "where the circumstances in *** exist" - the latter is a more effective way of addressing this point. This should be the default wording for consistency
	the requirements in paragraphs xx and xx have been met	Consistency can be gained	This may vary depending on whether it is licensee only trigger or licensee and Authority - in which case there are extra links to the trigger paragraph
	where there is evidence to demonstrate that the modification to allowances is efficient (or similar words)		See section 1 above

Appendix 6Cyber OT and Cyber IT PCDs

Our comments in respect of the references in Ofgem's issues log to a number of changes having been made in response to the licensees' note are as follows:

1. The proposed obligation in paragraph 3.3.10 to "take all reasonable steps to deliver the outputs specified" risks duplicating or even contradicting obligations elsewhere

Paragraph 3.3.10 sets out that:

"The licensee must take all reasonable steps to deliver the outputs specified in the Cyber Resilience OT PCD Table and the Cyber Resilience IT Table in accordance with and by the delivery dates specified in those tables."

The licensees have previously highlighted that this is an unnecessary obligation that effectively duplicates a sub-set of obligations contained in the extensive secondary legislation and guidance. Indeed, there is also a chance that this paragraph could contradict the Network and Information Systems (NIS) Regulations 2018 (e.g. in the case of misalignment of timing between changes and re-opener decisions, or differences between specified PCDs and wider activities that licensees must undertake to comply with the NIS Regulations 2018). This drafting also goes against Ofgem's licence drafting principle not to use "all reasonable endeavours".

Ofgem would have powers as the Competent Authority under the NIS Regulations to investigate and levy penalties beyond the removal of associated allowances, if appropriate.

Ofgem's issues log (row 28) sets out that Ofgem agrees with the licensees' position and has made the wording changes requested by the licensees but this change is not apparent in the condition published in the consultation.

If the Cyber PCDs are to remain part of a wider evaluative PCD condition and other mechanisms require the inclusion of Part B, we suggest that the following, alternative form of standard words proposed by Ofgem could be used:

"The licensee is funded to deliver the outputs specified in the Cyber Resilience OT PCD Table and the Cyber Resilience IT PCD Table in accordance with and by the delivery dates specified in those tables."

However, if a separate Cyber condition was to be developed, we do not believe that Part B would be necessary as the revised words do not perform any operative function.

2. Several aspects of the process for the assessment of PCD delivery are not appropriate for the assessment of Cyber PCDs.

The process for the assessment of evaluative PCDs that is set out in Part C of SpC 3.3 was developed as part of the RIIO-T2 and RIIO-GD2 price control reviews. It is a generic process.

Some aspects of this generic process are not appropriate for the assessment of Cyber PCDs. The generic drafting of key defined terms that this condition relies on (such as Consumer Outcome, Efficiency and Innovation) makes it difficult for licensees to understand how Cyber PCDs will be assessed or the likely impact on future allowance modifications. As Cyber PCDs are likely to be the only evaluative PCDs ascribed to licensees at the start of RIIO-ED2, the fact that the generic wording of the condition is not appropriate to Cyber activities is concerning.

The licensees have previously provided Ofgem with details of our concerns. The most significant of our remaining concerns are set out below.

3. The condition does not make it clear that Ofgem will assess PCD delivery based on evidence that was reasonably available at the time that the decisions were made

Cyber security is a relatively fast-moving activity area. Licensees will need to make decisions about the most appropriate course of action based on the information that is available to them at the time. It is possible, once further information becomes available or technologies evolve, that alternative solutions may, with the benefit of hindsight, seem more beneficial. For example, licensees may need to implement new solutions that make relatively recent (i.e. within RIIO-ED2) investments redundant.

It is important to maintain the principle that Ofgem should assess the efficiency/effectiveness of the investment made based on the information that was reasonably available to the licensee at the time of making the relevant investment decision. For new PCDs this will presumably be assessed at the time of the re-opener but the principle should also be incorporated in the principles for assessment of Fully Delivered With An Alternative Specification and both Partially Delivered options.

This important principle was enshrined in the DPCR5 and RIIO-ED1 close out processes and should be continued for RIIO-ED2.

The licensees have previously suggested drafting that would achieve this. We cannot see reference in the issues log that sets out Ofgem's rationale for not including this extra drafting.

4. The assessment process is likely to result in inappropriately intrusive ex-post efficiency assessment of any partially delivered outputs

Cyber security is subject to multiple external requirements. These requirements change relatively frequently. The threats that Cyber activities seek to address can also evolve rapidly, as does external best practice as to how best to address the threats. As a consequence, licensees may be required to amend their Cyber work programmes during RIIO-ED2. These programme changes may sometimes lead to licensees deciding to only partially deliver previously agreed outputs and to focus on new outputs instead.

Ofgem has acknowledged the potential need to change Cyber work programmes by introducing specific re-openers.

While a decision to cease the delivery of planned Cyber outputs in such circumstances would be sensible as it would be inappropriate to incur unnecessary expenditure, licensees are at risk of being penalised because such decisions would not meet the definition of “Efficiency” proposed in the licence. This is because many changes will arise due to *“factors beyond the reasonable control of the licensee”* and also result in *“lower Consumer Outcome than would have been achieved if the licensee had delivered the output as specified”* both of which are explicitly excluded from the definition of “Efficiency”.

In addition, it is possible that some outputs may be partially delivered as a result of innovative alternatives being deployed. However, it may often be the case that the reasons for ceasing an output may not meet the definition of Innovation as the application of technology, systems or processes may well have been proven (in other relevant contexts) as at the time of submission of the Business Plan.

This leaves licensees with a risk that any Cyber outputs that are ceased for good reason during the price control period would be subject to ex-post efficiency review. The licensees have previously highlighted to Ofgem the difficulties of such an approach for Cyber activities. We do not believe that historical benchmarking or bespoke engineering and cost assessments (as described in 3.3.13(e)) are likely to be appropriate or effective for assessing the efficiency of the expenditure associated with specialised, and generally mandated, Cyber activities. The process is likely to result in Ofgem (and customers) incurring costs associated with conducting reviews that will not provide meaningful information about the efficiency or otherwise of expenditure.

The prospect of such a process might well incentivise a licensee to continue with the delivery of an output, even if it is no longer the best thing to do.

We urge Ofgem to reconsider the assessment and allowance adjustment process and the associated wording of the licence and to introduce a practical, workable approach to adjustment of allowances for Cyber projects that are cancelled before the associated output is fully delivered.

5. Further examples should be included in the PCD Reporting Requirements and Methodology to aid understanding and interpretation

We recommend that the following scenarios be included in further *“hypothetical examples”* in the Associated Document to aid understanding:

The treatment of a Partially Delivered output where costs are “front end loaded”

The licensees have previously raised concerns with the fact that the formula for determining allowances for Partially Delivered PCDs incorrectly assumes that the output and Consumer Outcome delivery are likely to be proportional to expenditure incurred.

It will often be the case that Cyber projects target specific Cyber resilience outcomes rather than other wider components that appear in the definition of Consumer Outcome. If a Cyber output is cancelled and can be demonstrated to be attributable to Innovation (for example because an alternative, innovative solution is to be deployed but where that new solution does not meet the

specified output for the PCD set out in the Cyber Resilience IT (or OT) PCD Table), a more likely occurrence will be that the licensee has delivered lower output/Consumer Outcome than originally planned but that the costs associated with delivering that outcome would be higher than the strict pro-rate approach set out in 3.3.13(d).

Ofgem's issues log (row 25) sets out that, in such a scenario, Ofgem would be able to fund the efficiently incurred costs via the processes in 3.3.13(a) (although we think Ofgem means 3.3.13(e)). We do not understand how Ofgem would be able to use this branch of 3.3.13 instead of 3.1.13(d). We also do not understand what approach the licensee should take to reporting the delivery status of a PCD in this situation. Paragraph 1.12 of the PCD Reporting Requirements and Methodology Document does not permit the licensees an option to indicate that assessment under 3.3.13(e) is appropriate. It would be helpful if Ofgem could include a "*hypothetical example*" in the Associated Document explaining this process.

The treatment of any PCDs that are delayed into RIIO-ED3

Cyber programmes have multiple external drivers, which can result in re-prioritisation of tasks in order to accommodate addressing new Cyber risks or requirements. It is, therefore, possible that the delivery a Cyber OT or Cyber IT PCD could be delayed into the RIIO-ED3 period.

It would be helpful if Ofgem could confirm that the re-profiling of any allowances associated with Delayed PCD delivery set out in 3.3.13(c) would extend to any PCD that is delayed into the RIIO-ED3 period. A "*hypothetical example*" to confirm this treatment would be helpful.

6. It is unclear whether Cyber OT is still subject to a potential additional Use It or Lose It (UIOLI) adjustment

SpC 3.3 does not include any UIOLI adjustment for Cyber OT. We agree that the presence of the re-opener, PCD delivery mechanism and the PCD reporting provisions means that a UIOLI adjustment is not needed. However, we note from Ofgem's issues log that a UIOLI mechanism is expected.

Any UIOLI adjustment needs to interact correctly with any allowance adjustment made under Assessment of the Evaluative Price Control Deliverables (currently Part C of SpC 3.3) to avoid any risk of double counting of adjustments.

Ofgem's issues log (row 29) sets out that the following text has been included in SpC 3.3 Part D:

"Cyber resilience OT PCD assessment will take place as part of close out of the price control. This is because of the two-stage assessment that is required. We will first consider whether any adjustment is required as a result of following the methodology for Evaluative PCDs in this document. We will then consider whether any Use It Or Lose It Adjustment is required. The Use It Or Lose It Adjustment will be determined by assessing the licensee's total efficient spend for qualifying cyber resilience OT activities against the total use-it-or-lose-it allowance for cyber resilience OT. We will make one adjustment, if required, to reflect both assessments"

However, this paragraph has not been included in the licence.

The proposed paragraph is not sufficiently precise to avoid the risk of any double count. For example, it is not clear how “*the licensee’s total efficient spend*” or “*total use-it-or-lose-it allowance*” will be determined. It also does not explain how adjustments would be made to the separate Cyber Resilience OT Baseline Allowances and Cyber Resilience OT Re-opener Allowances.

The licensees have previously submitted text and associated algebra that could enact this adjustment if it is required.

7. Process for variant baselines for Cyber in the PCFM is unclear.

The treatment of allowances associated with Cyber OT and Cyber IT in the PCFM seems to create variant baseline allowances. This is quite different to the more familiar approach of creating fixed baseline allowances and/or separate variable values and is not consistent with how the draft PCFM operates.

It would be helpful if Ofgem could explain how it envisages these allowances operating in the PCFM and also provide guidance to licensees on how it expects licensees to adjust these values when setting Network Charges. This will help us to check whether the allowance adjustments envisaged in these conditions are being specified in a manner that is consistent with the intended operation of the PCFM.

Appendix 7**Treating Domestic Customers Fairly****1. SLC10AA**

Ofgem has confirmed at policy meetings that the specific examples that concern us of where the absolute phrasing of the licence condition could result in licensees breaching “the letter” of those obligations simply by undertaking routine activities would not be expected to breach the requirements of the licence condition. Ofgem also expressed the view that a principles-based licence condition is not intended to stipulate definitive steps which must or must not be taken. Changes should, therefore, be made to align the wording of the licence condition with the interpretation shared by Ofgem at policy meetings and to better reflect how Ofgem has described a principles-based licence condition would operate.

Most importantly, the licence condition must be drafted to make it clearer that failure to meet “the letter” of the Standards of Conduct does not constitute a breach of the licence condition provided that the licensee has complied with the requirements to act in a manner consistent with the Customer Objective and to deliver a Fair outcome for Domestic Customers.

We believe that there are a few different drafting approaches that could achieve this:

- a) Place a “reasonable endeavours” obligation on the licensees and make changes/qualification to those specific aspects of the Standards of Conduct that are of greatest concern to Ofgem (the approach proposed by the licensees on 15 September 2022); or
- b) Change the wording of paragraph 10AA.4 so that it is clear that the Standards of Conduct are not to be interpreted prescriptively, as long as paragraphs 10AA.2 and 10AA.3 have been complied with. This could be achieved, for example, by amending paragraph 10AA.4 to read: *“The Standards of Conduct in the procedures and processes which the licensee must put in place are that the licensee and any Representative must: ...”*. This would need to be accompanied by changes/qualification to those specific aspects of the Standards of Conduct that pose the biggest concern; or
- c) Make detailed changes to the wording of all aspects of the Standards of Conduct so that all aspects are drafted in a way that “the letter” of each aspect could be readily met by licensees when carrying out their routine activities.

2. Fair Treatment Guidance

The Fair Treatment Guidance currently adds very little to what is set out in the licence and does not provide any meaningful “guidance” to the licensee.

Sections 2 and 3 of the Fair Treatment Guidance do not provide any guidance on the interpretation of the licence condition. They simply repeat or paraphrase aspects of the licence condition itself. Furthermore, the Fair Treatment Guidance seems to introduce a new concept of “customer

outcome” which is not anticipated by the licence condition itself, is not included in the licence definitions and is, therefore, unclear.

It is essential that the Fair Treatment Guidance is expanded considerably to provide guidance and actual examples.

Section 4 (How Ofgem applies the Standards of Conduct) does not fully align with the process that Ofgem has explained in policy meetings. It also introduces concepts of a “fairness test” and “compliance threshold” which are not explained. In particular, it is essential that this section is refined to clearly set out the tests and logic that Ofgem will apply in enforcing this licence condition and the Standards of Conduct, as outlined by Ofgem at the various policy discussions for this condition.

The detailed drafting suggestions we provided previously will enable this to be achieved.

It is essential that amended versions of the licence condition and Fair Treatment Guidance are brought to the next LDWG, to allow further review prior to the statutory consultation.