Decision

Decision on an Advanced Procurement Mechanism in Electricity Transmission

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Contact:	Joe Slater and Margaret Riach
Team:	Network Price Controls
Email:	RIIO3@ofgem.gov.uk

We are introducing an Advanced Procurement Mechanism into the electricity transmission price control which will enable transmission owners to book supply chain capacity earlier than current arrangements. This follows a consultation in November 2024 from which we received views from transmission developers, organisations with an interest in the global and GB supply chain for electricity transmission, consumer groups and other interested stakeholders.

Any enquiries related to the text of this publication should be sent to Ofgem at:

10 South Colonnade, Canary Wharf, London, E14 4PU.

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Foreword

The UK Government has set out its mission to 'make Britain a clean energy superpower' and its policy objective for Clean Power 2030.

The Clean Power Action Plan published in December 2024 provides clarity on the task: upgrading the network infrastructure and installing clean sources of power at a pace never previously achieved; reforming the connections queue to prioritise projects that are ready and needed; building the right tools to grow low carbon power and storage; and developing a more flexible system that can meet increased demand while managing less predictable supplies from renewable generation.

The drive to create a clean power system by 2030 is a great opportunity both to better protect consumers from volatile gas prices, and also to drive forward growth, not just in the energy sector, but across the wider economy. This will require government, industry and regulatory bodies working in partnership at pace and a more active focus on removing the barriers to its achievement, including supporting greater coordination of supply chains and increasing domestic capabilities.

The Advanced Procurement Mechanism (APM) is a step change in how transmission owners are funded for their procurement of equipment and services. It brings forward c.£4bn in allowances (that would otherwise be approved later once projects reach specific funding milestones) to de-risk the transmission owners in booking capacity for equipment and services years in advance of when it is needed. This will mitigate the detrimental impact that supply chain delays might have on the delivery of this nationally critical infrastructure and enable transmission owners to accelerate project delivery.

We know we need to move quickly, be innovative, and work differently. The APM is a prime example of this new approach. But this needs to be done in a way that continues to protect consumers, keeping promises around delivery and remaining vigilant on costs.

Akshay Kaul

Director General, Infrastructure

Executive Summary

The need for intervention

Electricity networks in Great Britain (GB) require significant reinforcement and new network build over the coming years to help meet the government's ambition for GB to be supplied with clean power by 2030 and meet the UK's statutory net zero target and five-year carbon budgets. This requires significant investment in our onshore electricity transmission (ET) network, but the transmission owners (TOs) are facing considerable constraints to the supply of certain equipment and services that are critical for this network build. These constraints mean that TOs are experiencing extended lead times for equipment and services – if they wait to reserve these until the project-specific cost assessment has been completed this may be too late to deliver the project to the required timelines. These supply chain constraints could result in delays to project delivery and increases to consumer bills through constraint costs.

Therefore in November 2024 we consulted on a new regulatory mechanism for ET to mitigate current and future supply chain constraints which might otherwise result in delays to project delivery or increases in project costs, the Advanced Procurement Mechanism (APM). Having reviewed the 53 responses to that consultation, updated our Impact Assessment and undertaken further policy development, we are now deciding to implement the APM in the RIIO price control for electricity TOs. Our rationale for this is set out in Chapter 2.

The APM will de-risk the TOs in securing supply chain capacity in bulk at a much earlier point in the project development cycle than currently, by funding this spend earlier than would be the case through other mechanisms. We are confident that our design of the APM will limit the risks that consumers could otherwise face by accelerating spend without detailed project review.

Design

The APM will be a c.£4bn ex ante use-it-or-lose-it (UIOLI) allowance accompanied by a governance document and re-opener, as described in Chapters 4 and 5. The APM will enable TOs to spend on procurement of equipment and services up to a pre-agreed cap so that they can then procure at short notice when required without requesting further approval from us. However, this will be subject to controls to limit the risk to consumers. We are also introducing arrangements that will operate during RIIO-ET3 that will allow us to amend the spending cap. The APM Re-opener will allow us to amend the spending cap to reflect updated TO pipelines, and to add items to the APM scope to reflect new supply chain constraints or to remove items if some supply chain constraints ease.

Scope

We have used consultation responses and our engagement with TOs to determine an initial list of equipment that is eligible under the APM, see Chapter 3. Our assessment of what should be eligible under the APM has focused on confirming whether there is a demonstrable supply chain constraint, how the TOs will reduce the risk of stranded procurement, and how the TOs will ensure that all APM procurement is traceable.

To minimise the risk of stranded procurement, the APM is focused on fungible procurement (ie of assets that are transferable between many different projects) or on flexible procurement (ie allowing the TOs time to determine the detailed specification of the asset). More bespoke procurement can be considered on a case-by-case basis to allow us to assess the net benefit and risk of stranded procurement.

The APM should be used to secure supply chain capacity (eg by placing deposits), and as set out in our the APM Governance Document should not be used on any other costs associated with securing supply chain capacity.

Our consultation queried the extent to which services/labour should be eligible for the APM. We have retained our overall position that for services to be eligible we must be able to track their use against eligible equipment types, but have broadened eligibility beyond indirect service contracts to also include direct service contracts, where these can be linked to use of eligible equipment types.

Governance

Today we will also publish a statutory consultation on our proposal to modify the TOs' RIIO-ET2 licences and an associated APM Governance Document to implement our decision on the APM. We will consult on the APM being rolled-over into RIIO-ET3 through our statutory consultation on the RIIO-ET3 licence in December 2025.

As described in Chapter 5, the APM Governance Document will guide the day-to-day operation of the APM, including reporting requirements and how we would go about updating the APM in future, eg in relation to scope, funding caps or bespoke applications.

It is important that in all publications about the APM we consider both the benefits of transparency in supporting the delivery of consumer benefits, and the commercially sensitive nature of much of the information related to the APM. We have therefore published high-level and non-TO specific information wherever possible, but the detailed expenditure under the APM will be kept confidential for our evaluation.

1. Introduction

Context and related publications

1.1 Responding to feedback from electricity transmission owners (TOs) that global demand was affecting the way in which they needed to engage with the supply chain for electricity transmission (ET) equipment, in early 2024 we began exploring whether regulatory intervention was required to address this challenge.

1.2 In November 2024 we sought stakeholder's views on our Advanced Procurement Mechanism (APM) consultation (referred to in this document as the 'APM Consultation').[1] This followed our July 2024 RIIO-3 Sector Specific Methodology Decision which first introduced the APM concept.[2][3]

Table 1: Our decision-making process

Date	Stage description
20/11/2024	Stage 1: Consultation published
18/12/2024	Stage 2: Consultation closed, deadline for responses
20/03/2025	Stage 3: Responses reviewed and published
20/03/2025	Stage 4: Consultation decision/policy statement

Purpose of this document

1.3 This document sets out our decision to implement the APM in the RIIO-ET price control. Stakeholders' responses and further stakeholder engagement have informed our final decision.

1.4 Chapter 2 sets out our rationale for regulatory intervention, Chapters 3 and 4 describe our decisions regarding the scope and design of the APM, and Chapter 5 lays out our intended governance arrangements for the APM.

1.5 Following feedback on the 'impact evaluation' section of our APM Consultation, we have undertaken an updated Impact Assessment to review consumer and wider market impacts of the APM. This is contained in Appendix 1 to this document.

[1] Electricity Transmission Advanced Procurement Mechanism | Ofgem
[2] RIIO (Revenues = Incentives + Innovation + Outputs) is our approach to ensuring that the monopoly companies that run our gas and electricity networks have enough revenue to run and invest in a network that delivers efficiently what customers value.
[3] RIIO-3 Sector Specific Methodology Decision – ET Annex

Next steps

1.6 Alongside this decision we will also publish a statutory consultation on our proposal to modify the TOs' RIIO-ET2 licences and an associated APM Governance Document to implement our decision on the APM. That consultation closes on 17 April 2024, and we expect to publish our decision on it in early May.

General feedback

1.7 We believe that consultation is at the heart of good policy development. We are keen to receive your comments about this report. We'd also like to get your answers to these questions:

1. Do you have any comments about the overall quality of this document?
2. Do you have any comments about its tone and content?
3. Was it easy to read and understand? Or could it have been better written?
4. Are its conclusions balanced?
5. Did it make reasoned recommendations?
6. Any further comments

1.8 Please send any general feedback comments to stakeholders@ofgem.gov.uk

2. Why is regulatory intervention required?

Global supply chain constraints and impact on the TOs

2.1 Electricity networks in GB require significant reinforcement and new network build over the coming years to help meet government's ambition for GB to be supplied with clean power by 2030 and to meet the UK's statutory net zero target and five-year carbon budgets. To link new power sources, mainly offshore wind and nuclear, in 2023 National Grid estimated that it would need to build five times more transmission lines by 2030 than it had in the previous thirty years.[4]

2.2 To achieve this, we, the National Energy System Operator (NESO) and the TOs are working together to improve coordination of the investment plans. This will result in the Centralised Strategic Network Plan (CSNP), scheduled for 2027, while in the interim there are strategic plans and price control funding mechanisms already in place which seek to ensure that the GB network is reinforced at pace.

2.3 We are committed to delivering this investment but there are considerable constraints to the supply of certain equipment and services that are critical for the expansion of the ET network. This was highlighted by government in April 2024 in its UK renewables deployment supply chain readiness study.[5] This flagged that supply chain constraints could be a key delivery risk affecting plans to build offshore generation capacity and the networks (including the GB ET network) to get it connected. These constraints have been caused by a multitude of factors including the war in Ukraine, the COVID-19 pandemic, and the global push towards net zero which has increased demand for raw materials, equipment, and skills.

2.4 The supply chain challenge has recently been re-stated by the International Energy Agency,[6] which describes that "average lead times for cables and large power transformers have almost doubled since 2021" and shows that prices of certain types of transformers and cabling has increased by more than 50% since 2018.

2.5 These constraints mean that TOs are experiencing extended lead times for equipment required for projects, and in some instances supply chain capacity is already booked up several years out. Typically TOs wait to reserve equipment

[4] https://committees.parliament.uk/writtenevidence/121816/pdf/
[5] UK renewables deployment supply chain readiness - GOV.UK
[6] Building the Future Transmission Grid

until the project-specific cost assessment that would occur through, for example, price control setting or a re-opener, has taken place. If they continued to do this we may increasingly see procurement happening too late for equipment to be delivered in time for the TO to deliver the overall project to the required timelines.

2.6 These extended lead times could result in delays to project delivery, which could put at risk the UK's plans to connect cheap, domestic sources of renewable generation, new hubs for demand growth such as data centres and the ability for the UK to be supplied by clean power by 2030 (CP2030).[7] Project delays would likely cause increases to overall consumer bills through additional constraint costs. Delays to network build are also likely to mean fewer renewables on the system, and more fossil fuels in generation. This can be expected to result in higher wholesale electricity prices and higher carbon emissions.

2.7 The early construction funding (ECF) provided under our Accelerated Strategic Transmission Investment (ASTI) framework in RIIO-ET2 has provided funding for TOs to engage the supply chain at an earlier stage than was the case previously on ASTI projects. Building on this we want to ensure that TOs continue to be able to engage the supply chain early but are able to do so in bulk, and across a broader range of projects than under ASTI ECF.

Our consultation position

Questions

Q1. Do you agree with our proposal to introduce the Advanced Procurement Mechanism to address supply chain constraints faced by the transmission owners?

2.8 In November 2024 we consulted on introducing a new mechanism, the APM, to operate across regulatory periods for ET price controls that could mitigate current and future supply chain constraints which might otherwise result in delays to project delivery and/or increases in project costs.

2.9 The APM has been designed to de-risk the TOs in securing supply chain capacity in bulk at a much earlier point in the project development cycle than currently by accelerating provision of a portion of future funding. The APM will allow TOs to place deposits with suppliers based on TOs' current estimates of project pipelines, without needing to wait for existing funding milestones to be met.

[7] Clean Power 2030 Action Plan - GOV.UK

2.10 Given the consumer risks associated with accelerating funding, our consultation included proposals that the APM must be agile, transparent, and ensure consumer protection. Related to this, we also proposed that to justify the use of APM funding the TOs would need to provide evidence through their consultation responses and a subsequent data request of:

- the requirement for APM funding
- mitigations that the TOs should put in place to protect consumers from the risk of stranded procurement; and
- how they can provide transparency regarding what APM funding is spent on.

Summary of consultation responses

2.11 Overall stakeholders were generally supportive of implementing the APM. 28 out of the 43 stakeholders who responded to our first question agreed that the APM was a necessary intervention to address supply chain constraints. Examples given by stakeholders in expressing their support for the APM included helping the UK to secure both local and global supply chain commitments, allowing accelerated project delivery, and enabling the pathway to Clean Power 2030. One stakeholder commented that, without the APM, the UK would struggle to deliver the grid expansion necessary to achieve its Net Zero targets.

2.12 However, ten stakeholders raised concerns on the effects of the APM on the wider market for other supply chain participants, with six of those requesting that Ofgem undertake a wider market assessment before reaching a decision. These respondents suggested that the APM may exacerbate current supply chain constraints for the wider sector. Concerns were raised that the APM would put the incumbent TOs in an advantageous position when procuring equipment that is also procured by developers such as interconnectors or offshore windfarms. One stakeholder suggested that the APM only being available to the incumbent TOs is inconsistent with regulatory objectives of competitive markets. Related to these concerns, a total of 20 stakeholders asked for the APM, or an equivalent mechanism, to be made available to other market participants.

2.13 We received recommendations from seven stakeholders that the APM be used to give priority to UK-based manufacturers.

2.14 A total of 10 stakeholders expressed that they were against the intent and implementation of the APM, raising concerns that the advanced procurement of equipment would undermine the democratic planning process, and the introduction of such a mechanism was unnecessary. They commented that, when

constrained, industry responds by innovating and expanding capacity, thus making the APM an unnecessary intervention.

Decision and rationale

Objectives of the APM

2.15 As part of our decision to implement the APM, we have sought to establish the high level objective of the APM, which has been used alongside responses to the consultation to guide our decision making regarding the more detailed scope, design and governance of the APM.

2.16 Our overarching objective in implementing the APM is as follows:

- To enable the TOs to engage the supply chain earlier than they traditionally have done, in order to book supply chain capacity in bulk and in advance of confirmed project need;
- That this earlier engagement should avoid delays to the delivery of transmission projects that are caused by constraints in the supply chain for equipment (and related services); and
- That the consumer risk introduced by the APM, eg the risk of procuring assets that are not used, is reduced to a level that ensures that the benefits provided by the APM always outweigh the consumer costs it causes.

Introducing the APM

2.17 We have decided to introduce the APM to help mitigate supply chain constraints that might otherwise threaten delayed delivery of projects vital to achieving government's ambition for GB to be supplied with clean power by 2030 and to meet the UK's statutory net zero target and five-year carbon budgets.

2.18 From the consultation responses it was clear that there are supply chain constraints that would risk TO ability to deliver, and a majority of respondents supported the APM as an intervention in ET specifically. This supports our rationale for intervention.

2.19 The respondents that did not support the APM can be split into two general categories, explored below at paragraphs 2.20 and 2.21.

2.20 Some respondents agreed with the principles of why the APM may be needed, but raised concern that the impact of the APM on them and the wider market may be detrimental and that we had insufficiently considered this potential impact in our consultation. Having assessed the potential impact on other market participants,

see Appendix 1 and 'Impact Assessment summary' below, we do not agree that this represents a reason not to implement the APM:

- We do not consider that the TOs have a large enough global market share for the APM to materially distort the market in the manner suggested by the respondents, or to an extent which makes their businesses unviable. For example, through the APM we are providing advanced funding for c.£4bn worth of deposits for services and equipment. By contrast this can be considered against a commitment from TenneT for €30bn[8] of transmission related investment in 2023 and a $40bn commitment from the Chinese State Grid in 2024.[9]
- We see a clear merit in ensuring that the GB transmission network is sufficiently reinforced in advance of additional offshore wind or interconnectors commissioning so that these parties are able to connect and/or are not constrained off at a huge cost to consumers.
- While there may be some impact on other market participants from the TOs booking supply chain capacity in advance, we consider that the qualitative and quantitative elements of our Impact Assessment clearly show that intervention is consistent with our principal objective to protect the interests of existing and future consumers. It shows that even if the APM only contributes to avoidance of delay to 15% of the constraint cost savings that CP2030 would deliver, it will deliver a net consumer benefit.

2.21 Other stakeholders disagreed with the need for the APM at all on the basis that advanced procurement of equipment would undermine the democratic planning process. We do not agree with this argument. The APM is designed to enable procurement in a manner that is largely agnostic to project-specific design decisions (see the Chapter 4 discussion on flexibility and fungibility of APM procurement). As such, we do not agree that the APM would circumvent or undermine the planning process for specific projects.

2.22 In relation to the respondents that asked for the APM, or an equivalent mechanism, to be made available to other market participants, we want to make clear the following:

[8] Around €30 billion: Europe's largest-ever contracting pack-age for security of supply, the energy transition and climate protection launched
[9] See page 16 of the Building the Future Transmission Grid report, and Chapter 1 of that report is generally helpful for setting out the scale of global demand.

- The APM has been developed following feedback from TOs in early 2024 regarding the challenges that they were facing in relation to engaging with the supply chain. The first time that we received similar feedback from other sectors in a clear and coordinated manner was in response to our APM consultation.
- As a result, we are now considering the merits of extending the APM to other sectors that we regulate, and are engaging with government regarding the sectors that it would be better placed to support.
- The APM has been developed and designed very specifically to work within the RIIO regulatory framework for electricity transmission – it could not be copied over directly into other regimes, though its principles and objectives could be applied elsewhere.

2.23 Some respondents argued for there to be priority to GB (and UK)-based manufacturers, which we do not consider to be a viable policy position. This is due to the limited UK supply chain capacity in the medium term and the potential legal limitations of such policies. However, we will ask the TOs to report on where GB-based manufacturers have been used, to allow us to track the GB growth benefits of the APM.

2.24 The overall value of the APM is c.£4bn[10] and is available for the three incumbent TOs to advance procure equipment and services which is constrained within the supply chain.[11] Our decisions on the APM's scope and design are summarised in Table 2, and are detailed throughout Chapters 3-5 of this decision document.

Table 2: APM decision summary

Area	**Decision**	**Ref**
Scope	The APM will be available to the three incumbent TOs to use. The TOs must demonstrate requirement, mitigation, and transparency to use the APM allowance.	Chapter 3
Design	We will provide each TO with an APM allowance to de-risk advance procurement activities. Ofgem will maintain a unique and confidential APM Register for each TO, to enable monitoring of APM spend.	Chapter 4

[10] 2023/24 prices.
[11] The APM values assigned to each TO have been determined by an information submission that they each provided to us in December 2024, and thus vary between each TO. It should not be assumed that each TO has an equal one third share of the total APM value.

Area	Decision	Ref
	The APM will also include an annual re-opener to update the APM Register to reflect real-world market conditions, as required.	
Governance	We are consulting on a Governance Document, which would be implemented alongside the introduction of the licence. The proposed Governance Document outlines reporting requirements, how we will approach cost reconciliation, guidance around usage of the APM Re-opener and how we will approach future licence changes. To implement the APM, we have published a statutory consultation on our proposal to modify the TOs' RIIO-ET2 licences.	Chapter 5
Impact Assessment	Having taken account of consultation responses regarding our impact evaluation, we have undertaken a full Impact Assessment.	Appendix 1

Impact Assessment summary

2.25 Our decision to implement the APM has been supported by an Impact Assessment, which considers views that were raised in the consultation responses including in relation to the scope of the impact evaluation section of our consultation.

2.26 In this section we summarise our Impact Assessment to set out how this has contributed to our decision to implement the APM. The full APM Impact Assessment is included as Appendix 1 to this decision.

2.27 While we are unable to undertake a full quantitative assessment of the APM, we have considered the costs, benefits and risks on a qualitative basis and consider that the risk of inaction – resulting in project delays and network constraint costs – fully justifies intervention.

Policy options

2.28 We considered a longlist of six policy options and chose a shortlist of two options: a 'no intervention' counterfactual and the APM for early supply chain commitments.

2.29 A no intervention counterfactual (business as usual, BAU) approach would see Ofgem take no intervention to mitigate supply chain constraints and keep the current model of regulatory funding. We are against this option due to potential constraint costs resulting from delayed project delivery and the risk of missing delivering infrastructure vital to Clean Power 2030 goals.

2.30 Our preferred option is to implement the APM with the design and scope as described in Chapter 3 and Chapter 4. We consider this the right balance of facilitating the TOs to secure supply chain capacity and minimising the risk of stranded procurement, to maximise net consumer benefit from the APM.

Costs and benefits

2.31 We base our analysis on the minimum constraint savings identified by the NESO in CP2030, consistent with the target of less than 5% of unabated gas in the generation mix. CP2030 shows a constraint cost saving of £8bn in 2030 if the planned network is delivered in time. Timely delivery of this planned network is at risk if steps to speed up procurement, such as the APM, are not taken. Against this potential constraint cost saving we balance costs of approximately £0.4bn if procurement is stranded (ie unused) and up to £0.64bn to allow for social time preference (ie earlier TOs' expenditure and thus bill rises). Dividing the £8bn by these monetised costs implies that the introduction of the APM would break even if it successfully helps to deliver up to **13% of the constraint savings on time. To avoid spurious accuracy, we have rounded this to 15%**. We consider that it is highly likely that the APM will exceed this level, given early indications of the TOs' likely APM activity.

2.32 For our estimate of stranding costs, we have assumed that up to 10% of the full potential APM value of c.£4bn may become stranded. We have confidence that the rate of stranded APM procurement will not exceed this due to the vast volumes of work that we know the TOs will need to do and because we consider that the flexible, fungible and bespoke mitigations to prevent stranded procurement.

2.33 Some non-monetised benefits include:

- A **strengthened TO negotiating position** with suppliers could reduce delays and reduce unit prices.
- The efficiency and certainty provided by procuring in bulk could lead to **economies of scale**, a lower administrative burden, and greater certainty on cost and timing.
- By accelerating network build that facilitates the delivery of renewable electricity, the APM will help to contribute to **reducing carbon emissions earlier** than might otherwise be the case.

2.34 Some non-monetised costs include:

- **Locking in higher prices** at peak of market, but this is traded off against the risk of project delay without action and prices continuing to rise in the meantime.
- **Risk of double funding**. There may be difficulty ensuring full transparency to ensure there is no double funding, but we will implement reporting requirements to mitigate this risk.
- **Market distortion** affecting potential CATO, offshore and interconnector developers, but as discussed at paragraph 2.20 we do not consider this to be a significant or monetisable impact.
- The APM is accelerating spend and therefore bill rises, with **bill impacts** potentially 2-7 years earlier than otherwise expected – up to £1-4 per household per year.[12] Given the uncertainty associated with this, we have not separately estimated the distributional impacts on consumer bills.

[12] 2023/24 prices

3.Scope of the APM

Our consultation position

Questions

Q2. Do you agree with our proposed framework for evaluating eligibility?

Q3. Do you agree with how we have defined supply chain constraints?

Q4. What are your views on which equipment types are most constrained, which are at risk of future constraint, and which are less of a concern, and what are your views on the items we should include within the scope of the APM?

Q5. What are your views on our intention to exclude strategic procurement from the APM, and the potential benefits of later expanding the APM to include it?

Q6. Do you agree with how we have characterised fungible, flexible and bespoke procurement, and our proposed treatments of each of these? Do these definitions reflect real world contracting and engineering realities?

Q7. Do you agree with our proposed approach to funding services contracts through the APM?

3.1 Our consultation set out that the APM is seeking to mitigate the impact of ET supply chain constraints on TOs while reducing the risk of waste or inefficient spend, which could result in consumer detriment. The various components that were proposed in our consultation to achieve this are set out in the sections below.

Evaluating eligibility

3.2 To justify inclusion of any type of equipment/services in the APM, we need to have confidence that the APM funding will bring about a net benefit. We proposed that to enable an asset category's inclusion in the APM, the TOs would need to demonstrate evidence for the following three areas:

- Requirement: any procurement eligible for the APM would need the TOs to demonstrate evidence of constraint to justify its inclusion.
- Mitigation: the TOs would need to set out how they would mitigate the risk of stranded procurement given the provision of finding in advance of project need or detailed design. We expected the TOs to set out how they would achieve flexibility and/or fungibility in respect of the equipment procured.
- Transparency: any expenditure under the APM would need to be traceable in order to ensure that we are able to monitor which projects spend is later allocated to.

Supply chain constraints

3.3 We proposed that to demonstrate eligibility of an expenditure category for APM funding, TOs should provide evidence of constraint (eg through examples of current lead times or capacity) and the impact this would have on project delivery times and any resulting increases in costs to consumers.

Constrained equipment type

3.4 We proposed a list of constrained equipment types that will be necessary to build and reinforce the transmission network in the coming decade.

Strategic procurement

3.5 We asked for views on whether to expand the scope of the APM to include strategic procurement across all TO activities, rather than just constrained areas. We considered the benefits of expanding the scope of the APM such that it could de-risk programmatic bulk purchase agreements, which can offer potential savings from procuring at scale and offer greater resilience to the TOs to unexpected supply chain shocks. However, we set out our consultation position to exclude strategic procurement from the scope of the APM in order to minimise the total APM expenditure at risk.

Flexible, fungible and bespoke procurement

3.6 We outlined our proposal that equipment procured using the APM should be fungible and/or flexible:

- We proposed that **fungible** meant assets that are highly transferable between projects, so there is little risk of wastage if a large volume of assets is procured at an early stage.
- Where assets cannot be procured fungibly, we proposed that **flexible** contracts should be procured, which would allow only high-level detail to be given when securing factory slots such that this can be narrowed down at a later date.

3.7 We recognised that there may be examples of equipment with supply chain constraints that cannot be procured fungibly or flexibly. We proposed that equipment that is neither fungible nor flexible is **bespoke**. Bespoke equipment inherently comes with a higher risk of wastage when procuring in advance, as project need could fall away. Therefore we proposed to approve bespoke procurement on a case-by-case basis, with TOs being required to provide dedicated submissions on each area of proposed bespoke procurement.

Services

3.8 We considered whether to allow the APM to be used to procure services as well as equipment, as these markets are likely to face similar constraints as the equipment. We proposed that indirect procurement of services (ie where a contract delivers a combined scope of services and equipment) be included in the scope of the APM, but that direct procurement of services (ie standalone labour contracts) not be included in the scope of the APM due to difficulties in tracing APM spend on and use of labour when not linked to equipment.

Summary of consultation responses

3.9 Question 2 received 27 responses. There were 13 stakeholders in favour of our proposed framework for evaluating eligibility. Of those 13 responses, one stakeholder suggested that our proposed eligibility framework should be focused specifically on national targets such as CP2030 rather than 'requirement, mitigation and transparency', and another stakeholder suggested that eligibility should be kept simple to avoid undermining the objectives of the APM. A total of 12 stakeholders disagreed with our proposed eligibility framework, with one stakeholder commenting that the proposed eligibility criteria makes the APM inflexible and too slow to respond to changing market conditions. Seven stakeholders said that our proposed qualitative assessment of applications was insufficient and instead a more robust, quantitative assessment should be required.

3.10 We received responses from 17 stakeholders on Question 3 regarding our definition of a supply chain constraint. Four stakeholders disagreed with our definition. One stakeholder reported that our definition of constrained was too ambiguous, and a TO said that our definition of constraint should not be too prescriptive to ensure it does not influence procurement approaches. The other 13 stakeholders expressed broad support for our proposed definition of a supply chain constraint, but we received suggestions to extend our proposed definition of constraint to include anticipated demand and delays.

3.11 Regarding Question 4, all 17 stakeholders that responded to this question stated that the full list of equipment published in the consultation can be defined as constrained. One stakeholder recommended that we expand our proposed list of constrained equipment to cover sub-supply chain constraints such as fencing, earthing and lighting protection, and integrated security systems. This stakeholder highlighted that quarry materials are also at significant risk of becoming constrained due to potential stakeholder resistance to quarry

expansion, the offshore wind industry beginning to build concrete bases in Scotland.

3.12 We had 18 stakeholders respond to Question 5 on whether to expand the scope of the APM to include strategic procurement. 13 stakeholders were in favour of expanding the scope of the APM to include strategic procurement, citing benefits such as supply chain certainty and reducing risk of delayed project delivery. Only one stakeholder supported our proposal to exclude strategic procurement, agreeing that strategic procurement would increase the risk that consumers would face. Two stakeholders asked for a clearer definition of what is meant by strategic procurement.

3.13 Question 6 regarding our flexible, fungible and bespoke categorisations received 25 responses, 15 of which were generally supportive. Of these, nine stakeholders agreed that the flexible and fungible requirements reflect real world engineering possibilities and seven said that the standardisation of equipment would further enhance the fungibility and flexibility of procurement. One stakeholder highlighted that the degree of flexibility which can be provided depends on procurement stage, with decreasing degrees of flexibility as engineering design is approved and a delivery date approaches. This theme was present, albeit less explicitly called out, across several other responses. Two stakeholders disagreed with our proposed flexible, fungible, and bespoke categorisations, with one of these stakeholders commenting that fungible procurement encourages stockholding. Stakeholders were generally supportive of including bespoke procurement within the APM, commenting that bespoke procurement, which is necessary for project delivery, also faces supply chain constraints. Two stakeholders were against our proposal of bespoke procurement going through a separate funding criteria, with one TO raising concerns that the proposed re-opener for bespoke procurement would limit the agility and pace to which they can respond to new constraints in the supply chain.

3.14 Question 7 on services received 22 responses, of which 17 were in favour of including services in the scope of the APM, including all three TOs. Six stakeholders were explicitly supportive of our proposal for indirect procurement of services to be included in the scope of the APM. Seven stakeholders said that they were supportive of direct procurement of services to be within scope of the APM, flagging that services are equally as constrained as equipment. Two stakeholders cautioned against incentivising certain procurement strategies, eg by only including indirect procurement of services, as they said this risks distorting the market and ultimately weakens competition. A stakeholder

recommended expanding the scope of the APM to cover hiring and training skilled labour. We also received a suggestion from one stakeholder for service funding to be provided in escrow and only be released to suppliers in stages against specific, verifiable events, to aid in transparency.

Decision and rationale

Supply chain constraints and APM eligibility

3.15 Our decision on APM Cost Categories is shown in Table 3. This table sets out which APM-specific categories have been designated as APM Cost Categories, and whether these are only eligible for bespoke procurement. Where there are differences within the sub-categories within a category, we have separated that APM-specific category into two rows. The full list, including sub-categories, is set out in the APM Governance Document and can be updated in future through the APM Re-opener.

Table 3: APM-specific categories and whether they are APM Cost Categories

APM-specific category	**APM Cost Category?**	**Bespoke only?**
AC Circuit Cable	Yes	No
AIS Switchgear (Incl. Circuit Breakers)	Yes	No
Batteries	Yes	No
FACTS	No	n/a
GIS Switchgear (incl. Circuit Breakers)	Yes	Yes
HVDC	Yes	Yes
Instrument Transformers	Yes	No
LVAC - Substation Auxiliary Supplies at substations	Yes	No
LVAC - other	No	n/a
Other Switchgear	Yes	No
Overhead Pole Line	Yes	No
Overhead Tower Line	Yes	No
Protection & Control	Yes	No
Wound plant - quad booster	Yes	Yes
Wound plant - other	Yes	No

3.16 We have taken this decision having considered the responses to Question 2 and 3, which were broadly supportive of how we proposed to assess eligibility for the APM and how we proposed to define supply chain constraints, and to Question 4 where stakeholders fully supported the list of eligible equipment that we proposed. These responses showed that there are very few parts of the ET supply

chain that are not constrained currently, with most areas constrained to such an extent which would risk delays to delivery of ET network reinforcement.

3.17 Even where there may be parts of the supply chain that are not as heavily constrained, or constrained at all, responses to Question 5 made clear that if the APM focused strictly on constrained equipment types we may risk affecting the TOs' ability to procure effectively. For example, substations are formed of many parts of equipment, some of which are very constrained and some of which may not be, but often all will be contracted at once through one contractor, so splitting some equipment types out of the APM may be counter-productive to enabling the objectives of the APM.

3.18 In relation to the responses that argued for the scope of the APM to be expanded further, eg to additional equipment types or to support CP2030 targets, we consider that the APM scope we proposed is already sufficient in this regard. This view is based on our engagement with TOs and having had sight of the projects that the APM may support, many of which will support achievement of CP2030 targets. Furthermore, we are confident that the processes we are establishing to update the APM in-period, explored in Chapter 4, will ensure that the APM can be responsive to changing requirements.

3.19 The APM should be used to secure supply chain capacity (eg by placing deposits), and as set out in our the APM Governance Document should not be used on any other costs associated with securing supply chain capacity.

Services

3.20 We have decided that where the use of services can be directly and transparently linked to the use of equipment procured under the APM and the resulting delivery of network infrastructure, regardless of whether these services are directly or indirectly procured, that they should be eligible for APM funding. For example, this may be where we will be able to track how many people-hours were assigned to the installation of the equipment procured.

3.21 Our rationale for this slight change to our consultation position, which was that only indirect services procurement would be eligible under the APM, has largely been driven by engagement that we have had with the TOs since their consultation responses. This has provided us with confidence that directly procured service spend could be robustly tracked through the APM Register. The detail of how this will be done is set out in the APM Governance Document, but in summary:

- All APM Cost Categories are named types of equipment and so any reporting of procurement for APM expenditure on services has to relate to specific equipment.
- There is no specific APM Cost Category for services, and so the TOs will not receive an allowance for generic "services".
- All APM expenditure on services can then be tracked in the same way as equipment.
- If a TO claimed APM expenditure for procured services and is unable to evidence and link the use of the services to an APM Cost Category in the APM Register, this would be classed as ineligible spend.

3.22 We do not agree with the response that suggested that the APM should be used for supporting training and skills development. We consider that there would be huge difficulties in being able to track the expenditure to assess it for efficiency and reduce the risk of double counting in the context of the TOs' wider funding. We also consider supply chain training to go beyond Ofgem's remit.

Flexible, fungible and bespoke procurement

3.23 We have decided that the concepts of fungible, flexible and bespoke procurement remain key to providing consumer protection through the APM. This is consistent with the responses received to Question 6, which were generally supportive of these concepts. We acknowledge the points raised by some stakeholders that we should apply these concepts pragmatically. For example, we accept that contracts cannot meet our definition of 'flexible' indefinitely, and that at some stage TOs will need to commit to a specific design.

3.24 The APM will provide the TOs with funding for the procurement of equipment without needing to demonstrate which projects that procurement is for. While the TOs have provided us with their current understanding of their individual project pipelines to target their APM expenditure, there is a risk that some envisaged needs change or fail to transpire. If procurement through the APM cannot be used for another project, this could result in stranded procurement, with any related expenditure being written off at a cost to consumers. This potential cost is factored into our Impact Assessment in Appendix 1, but as a result of our wider mitigating actions is unlikely to undermine the overall benefits offered by the APM.

3.25 It is therefore important that we minimise the risk of stranded expenditure by treating types of procurement differently based on whether they are fungible, flexible or bespoke. We set out detail on each of these below.

Fungible procurement

3.26 Fungible procurement focuses on the transferability of the asset itself. A highly fungible asset could be used on a variety of different projects, such that there is little risk of wastage if a large volume of assets is procured at an early stage.

3.27 For example, a TO could procure hundreds of steel towers with confidence that these could be used on a variety of projects even if there are some changes to the capacity or location of where that equipment is used following its manufacture. The fungibility of these assets can therefore help to mitigate the risk of waste and asset stranding.

3.28 We are also interested in increasing cooperation between TOs in how they procure. As such, and in line with standardisation recommendations in the Electricity Networks Commissioner's report on accelerating electricity transmission network build,[13] where possible TOs should seek to procure standardised equipment which would be fungible between their networks. Seven responses to our consultation agreed that standardisation should increase the fungibility of assets and thus reduce the risk of asset stranding in the APM.

Flexible procurement

3.29 Flexible procurement focuses on allowing the TOs time to determine the detailed specification of the asset they are procuring. This means that when a TO pays a deposit to reserve capacity with its supplier, the TO will need to give a high-level view of the equipment required but will not provide a detailed specification until later in the procurement process, ie much closer to the delivery date agreed with the supplier. This allows further time for the TO to develop its projects, eg through the detailed design process, to understand the specifications of the equipment required. Standardisation, as discussed under fungible procurement, could also help to facilitate more flexible procurement by reducing the variation and specifications that suppliers need to account for.

3.30 For example, a TO could agree a high-level requirement for Air Insulated Switchgear (AIS) with its supplier if the APM is active in 2025, but could wait to

[13] https://www.gov.uk/government/publications/accelerating-electricity-transmission-network-deployment-electricity-network-commissioners-recommendations

provide further specification until 12-24 months later, when it is certain which project the equipment will be used on.

Bespoke procurement

3.31 There may be bespoke equipment with constrained supply chains, where procurement cannot be flexible or fungible because the equipment is designed in a way which means it is specific to a particular project from a very early stage.

3.32 The risk of wasted APM spending – if the original project need disappears – is much higher with bespoke equipment, due to the limited ability to redeploy the capacity slot or asset. Therefore, there is less of a case for including bespoke equipment in the APM allowance. Nonetheless, we recognise the potential for consumer detriment if there are severe delays to the procurement of bespoke equipment required for critical infrastructure build.

3.33 As such, we propose that bespoke equipment can receive APM funding on a case-by-case basis through the APM Re-opener set out in Chapter 4, and that this funding would remain assigned to a particular project. This offers a balanced approach to provide advanced funding to the TOs to de-risk timely procurement of required equipment, while minimising the risk of stranded procurement (and thus wasted expenditure).

3.34 We have approved c.£400m of bespoke procurement that will be included within the TOs' initial APM allowances.

4. Design of the APM

Our consultation position

Questions

Q8. Do you agree with our rationale for using a UIOLI mechanism for the majority of APM expenditure, rather than other regulatory tools?

Q9. Do you agree with our proposal for the APM allowance to be capped at 20% of the estimated equipment cost?

Q10. Do you agree with the use of a re-opener to update the APM in-period?

Q11. What are your views on our proposed approach to cost reconciliation?

4.1 In our consultation, we proposed that the APM would be an ex ante UIOLI allowance, which would be accompanied by the APM Register and re-opener, to enable Ofgem to have sufficient control and flexibility over the mechanism to best deliver the objectives of the APM.

UIOLI and 20% threshold

4.2 In our consultation, we proposed that the value of the APM UIOLI would reflect a high-level known view of projects submitted to us by the TOs. The UIOLI allowance itself would be a funding pot where allowances are not project specific, and TOs would not need to seek prior Ofgem approval to spend from the allowance (with additional controls on bespoke procurement). We also proposed that the deposits placed using the APM would be capped at 20%, which we understood to be a fair indicative rate for deposits that are placed in the supply chain (some of which are higher than this, and some of which are lower).

4.3 We considered alternative mechanisms to a UIOLI, such as Price Control Deliverables (PCD). We did not consider PCDs as the appropriate mechanism because it would tie procurement to a specific project, and the purpose of the APM is to allow procurement before specific project need or design is determined.

4.4 Alongside the APM UIOLI, we outlined our proposal for a structure of an APM Register, which would enable us to track allowances and spend under the APM. There would be a unique and confidential register for each TO, which would include a list of eligible equipment for APM spend, and an agreed estimated final equipment cost.

4.5 We proposed that the APM Register would be constructed of four distinct categories:

- **APM allowance:** the value of the UIOLI pot, proposed by the TOs and approved by Ofgem.
- **Procurement report:** TOs reporting on their contracts signed and deposits placed.
- **Project allocation:** when the TOs allocate equipment procured using the APM to a project.
- **Cost assessment:** outlines how APM allowances interact with final project allowances.

Re-opener

4.6 We proposed to use a re-opener to make amendments to the APM Register, to allow the APM to remain flexible and reflective of real-world market conditions. The re-opener would be used to add new equipment to the register when new supply chain constraints emerge and remove qualifying equipment from the APM Register when market conditions improve. The re-opener would also be used to adjust TO APM allowances as the fund gets used and new projects, including bespoke projects, enter TO pipelines.

Cost reconciliation

4.7 We proposed that the total cost of equipment would be assessed at the time when full project costs are sought. We suggested that when setting final project allowances, we would net off the relevant APM costs against the total project cost.

Summary of consultation responses

4.8 Regarding whether a UIOLI allowance was the most appropriate funding mechanism for the APM, all 14 stakeholders that responded to Question 8 were broadly supportive of a UIOLI over PCDs or a general totex increase. One TO questioned how the UIOLI will be carried across several price control periods and another stakeholder wanted clarity on whether unused spend would be returned to the consumer. All TOs sought clarity on areas such as how the APM would treat efficient overspends and abortive costs.

4.9 There were 23 responses to Question 9 on whether a 20% deposit cap was appropriate. Eight stakeholders were in favour of our proposal, with some stakeholders agreeing that 20% is reasonable, and a consumer group commented that the 20% cap helps keep the costs efficient. There were 12 stakeholders against the 20% deposit cap, with responses citing that 20% was too restrictive on the TOs as it would not make TO bids more attractive than international

competition. One stakeholder suggested that Ofgem should take a case-by-case approach to the deposit cap.

4.10 Only 11 stakeholders responded to Question 10 on the use of a re-opener to update the APM in-period, seven of which were supportive of our proposal. Five stakeholders said the proposed annual re-opener was too infrequent, and one stakeholder said it should remain open at all times to ensure TO procurement can remain efficient and responsive.

4.11 Question 11 on our proposed cost reconciliation approach received 13 responses. Six stakeholders were supportive, but two others were against our proposed cost reconciliation approach. Those against it commented that an assessment at a later stage creates an unacceptable level of risk for the TOs, eg if it took into account information which was not available to the TO at time of procurement. One stakeholder recommended considering variations in procurement timings and the nature of the supply chain when conducting cost efficiency assessments. A TO said that the use of an international benchmark would be inappropriate due to differences in contracting strategies and portfolios between different countries. Five stakeholders asked for greater clarity in what information will be required for cost assessment, and a consumer group raised concerns over risks of doubling counting and asked for greater clarity on how spend will be monitored and disallowed if necessary.

Decision and rationale

UIOLI design

4.12 We have decided to set the APM as a UIOLI given the broad support from respondents through Question 8 and the fact that it allows for flexibility whilst not having any perverse incentives to not spend the fund. Given feedback on our proposed approach for how the UIOLI would operate, we have slightly changed our approach:

- In our November policy consultation, we described a UIOLI which operated in a manner consistent with many other UIOLIs in RIIO, ie a fund would be set in the licence which would be available to TOs but be returned to consumers if it went unused. The TOs would then report on what has been spent on the UIOLI, and this would be netted off against future allowances that were granted for specific projects.
- The approach shown in our APM licence modification consultation would still only provide TOs with allowances that they have spent, with no sharing factor applied to underspend, as per any UIOLI. However, rather than the APM

acting as a fund which can be exhausted, we are consulting on the APM being an initial zero-sum fund that adjusts up when APM allowances are incurred, and back down when full project allowances have been granted elsewhere in the price control. The upwards adjustments would be capped at the same level that we determined following an information request that we issued to the TOs in December 2024, which results in the same level of allowance as the approach described the APM Consultation. The adjustments would be made annually through updates to the APM Register at the Annual Iteration Process.

4.13 We consider that this approach has two principal benefits, and addresses some of the challenges raised in responses around the flexibility of the APM:

- It will make for a significantly more straightforward reconciliation of costs between the APM and RIIO-ET3 baseline allowances later in 2025 because we will not need to adjust RIIO-ET3 baseline allowances to account for the APM; it will be the APM that adjusts. This will reduce the risk of double-counting and any negative consumer impacts that would result from that.
- It will enable greater in-period flexibility with less (or potentially no) need for TOs to use a re-opener to increase their allowances – if full project funding has been granted against some of their APM spend then the relevant APM allowance would be available again. This is consistent with the numerous consultation responses which called for the APM to be as flexible as possible.

4.14 We will have the ability through the licence to increase or reduce the cap on APM expenditure should such an adjustment be necessary in future, reflecting comments raised in consultation responses that expenditure on the APM may need to increase in future.

4.15 Some consultation responses highlighted the risks that the APM could present to consumers. Overall we consider that the mitigations set out throughout this document should address that concern, but as a further consumer protection measure we have decided that we will be able to disallow expenditure incurred under the APM which:

- does not meet our definition of fungible, flexible or bespoke procurement;
- involves equipment or services not included on the APM Register at the time the procurement occurred;
- relates to procured volumes of equipment or services significantly in excess of what the TO could have reasonably expected to use;

- the TO is able to financially benefit from by novating or otherwise transferring procurement undertaken through the APM to another licensee or a third party for profit;
- relates to equipment or services for a project which had, at the date of procurement, been designated as a CATO project;
- relates to equipment or services for a project where the TO has also received ECF under ASTI;
- relates to services which were not possible to link to an APM Cost Category in the APM Register; and
- cannot be tracked by the licensee through the APM Register to provide evidence to the Authority that there is no double-funding across the price control.

20% threshold

4.16 We have decided to set the overall threshold of average APM expenditure across all APM Cost Categories at 20% of the total expected equipment cost. For each individual TO, this will be calculated on the basis of total APM spend to date as reported in the TO's annual Regulatory Reporting Pack.

4.17 We received a mixture of responses to Question 9 which covered this. Whilst a majority of responses identified that 20% was too low, we have seen sufficient evidence through consultation responses to satisfy ourselves that if used as an average, as we've decided, 20% should be sufficient. This is because there are substantial parts of the supply chain that require deposits that are less than 20% to book capacity, which will net off the parts that require more. We saw no evidence in the consultation responses to indicate that an average threshold of 20% would be insufficient to enable the APM to operate effectively, but equally we saw no evidence to suggest it should be lower.

4.18 We also consider that using the threshold as an average should incentivise TOs to get the best deal possible on behalf of consumers when negotiating with the supply chain, as they must remain below the average 20% threshold.

Updates to the APM

4.19 To support the main fund, we have decided to introduce an APM Re-opener, covering the following areas:

- **Additions or removals of APM Cost Categories**: Responses supported the proposal that we may need to add new APM Cost Categories through a re-opener in the future (especially if not all equipment is included initially). While

not covered in the responses, we consider it may be equally necessary to remove APM Cost Categories if supply chain constraints ease to such an extent that the costs/benefits of the APM no longer show that inclusion in the APM is required.

- **Increases/decreases to the cap on expenditure**: Responses supported the proposal that expenditure under the APM may need to increase to accommodate increasing volumes of network build. We agree with this, but also consider it equally plausible that after overcoming this initial burst of network build activity over the next few years, reduced work volumes in the future may require us reduce the size of funds available under the APM.
- **Additions of allowances for bespoke procurement**: Responses generally agreed with our proposal to allow future submissions for bespoke procurement, given that APM allowances on these areas would be exhausted once the project-specific procurement(s) has taken place.

4.20 Despite the five responses to the contrary, we have decided to limit the frequency of the TO-triggered APM Re-opener window to once per year, in April. If required, eg due to unforeseen circumstances that require urgent action, we are able to trigger the APM Re-opener at any time. We consider that this is sufficient because we have included more equipment within the scope of the APM than originally envisaged (see paragraph 3.17) and because of the flexibility provided by our licence approach described at paragraph 4.12.

APM Register

4.21 The APM Register and proposed APM Governance Document, both of which have been informed by the consultation responses and form part of our statutory licence consultation on the APM, will be key to managing the reconciliation of costs under the APM.

4.22 Question 11 on cost reconciliation received mixed responses, most of which agreed that costs would need reconciling, but queried how best we could do this. These responses, and the challenges provided, have been valuable in informing how we have approached the design and governance of the APM Register and associated reporting requirements.

4.23 The APM Register will be updated annually by the TOs, likely through the RIIO Annual Iteration Process. As part of this update TOs will be required to report on the APM expenditure incurred, which projects the equipment/service procured have been assigned to, and (likely at a later stage) whether those projects have received regulatory approval and funding elsewhere in the price control. To

reconcile these costs, where projects have received regulatory approval and funding elsewhere in the price control, the reporting under the APM will reduce the allowances granted under the APM commensurately with the value originally incurred against the APM Cost Category for that project.

4.24 We consider that this approach addresses the concerns raised by stakeholders regarding the complications and uncertainties associated with reconciling APM costs at a later stage because the APM will only hold TOs accountable for allowances incurred under the APM (and will reconcile these like-for-like). However, for the avoidance of doubt, project specific expenditure which our wider assessments of costs (eg through a re-opener) show to be inefficient may still be removed from TO allowances, as per our usual cost assessment processes.

5. Governance

Our consultation position

Questions

Q12. What are your views on how we should approach in-period updates to the APM?

Q13. Do you agree with our proposal regarding retrospective application of the APM?

Q14. Do you agree that the publication of detailed APM costs and volumes could be commercially detrimental to TOs, and by extension consumers? If so, why?

APM Governance Document

5.1 In our consultation, we proposed that the operation of the APM would be supported by an associated Governance Document which would:

- Describe what information is needed from the TOs in their applications for APM funding, and how we would assess those applications.
- Detail reporting requirements, including timelines.
- Describe how costs incurred under the APM would be reconciled against final project views.
- Describe how the APM Re-opener would operate, and how allowances and the APM Register would be updated.
- Describe how licences would be updated to reflect the APM.

Licence changes and updates to APM cost categories

5.2 We proposed to introduce the APM through a statutory modification to the RIIO-ET2 licences early 2025, with a view to the continuing into RIIO-ET3 (subject to RIIO-ET3 governance and consultation).

5.3 We also proposed an APM Re-opener to enable periodic licence updates to an APM Register, by turning asset types 'on' or 'off' for APM usage.

Retrospective applications

5.4 In our consultation, we outlined that we would consider retrospective applications for APM funding, if the spend:

- Related to contracts which were signed no earlier than the publication date of the consultation.
- Fit the eligibility requirements outlined in Chapter 3 of the consultation.
- Is reported to Ofgem within one month of commencement of the licence taking effect.

Confidentiality

5.5 In our consultation, we considered what degree of transparency would be required under the APM, balancing:

- our duties to provide information to the public, especially on expenditure as material as the APM; and
- the commercially sensitive nature of TO procurement activities and the fact that publicly disclosing information such as the APM Register could have a detrimental impact on TOs' competitiveness in the market.

5.6 We therefore proposed to publish the total sum of the APM allowance, and equipment listed to at least an Asset Category level. We proposed to not publish disaggregated allowances or spend, detailed asset categories or projects.

Summary of consultation responses

5.7 Regarding Question 12, six stakeholders were supportive of our approach to in-period updates, with views that flexibility within the mechanism was key to adapting to the changing market. Four stakeholders were against our position, arguing that using the re-opener to add or remove items from the APM Register would send misleading signals to the market, especially in relation to Ofgem being able to withdraw APM eligibility for certain items. Two stakeholders expressed a preference for the APM Register to include all equipment, not just constrained, to remove the need for in-period updates.

5.8 One stakeholder was against our proposal to allow retrospective applications in the APM, stating that allowing retrospective applications would have a distorting effect on TO planning and procurement priorities. However, 11 stakeholders were supportive of our proposed stance on retrospective applications.

5.9 Question 14 on confidentiality received 13 responses. Two stakeholders disagreed with our view that publishing certain details of the APM could be commercially sensitive and therefore detrimental to TOs. A consumer group said that the lack of transparency proposed could make APM spend difficult to monitor, asking Ofgem to provide transparency in funding bids submitted, and transparency in our cost efficiency assessment. One stakeholder suggested that transparent information around technologies used could increase the benefits of competition. Another stakeholder suggested that the private APM Register be made available to governments and relevant agencies to allow a whole system view of the energy supply chain constraints to be developed. Nine stakeholders agreed that published APM information would be detrimental for the TOs, and expenditure should remain confidential to safeguard competition.

Decision and rationale

APM implementation through the licence and the Governance Document

5.10 Alongside this decision we have published a statutory consultation on our proposal to modify the TOs' RIIO-ET2 licences and an associated APM Governance Document to implement our decision on the APM. That consultation closes on 17 April 2024, and we expect to publish our decision on it in early May.

5.11 We did not ask a specific question in the November 2024 consultation in relation to the APM Governance Document, given that the detail of it is going to be consulted on now. Two stakeholders made suggestions of what could be included in the Governance Document, and sought clarity on certain areas, including:

- the level of evidence required to demonstrate supply chain constraints through future assessments, eg when assessing bespoke procurement; and
- the approach to cost assessment and potential future disallowances.

5.12 Given the importance of ensuring that the APM is used in a manner which minimises the riskiness of spend that is done on behalf of the consumer, and the importance of holding the TOs to account for effective delivery, we will implement a Governance Document to govern how the TOs should use the APM.

5.13 Areas of the Governance Document will relate to in-period updates to the APM. Our views on in-period updates, including where Question 12 influenced our position on these, is set out in Chapter 4.

Retrospective applications

5.14 Given that 11 of 12 stakeholders were supportive of our proposal that retrospective spend should be eligible for APM allowances we have decided to maintain this position, provided that the spend:

- relates to contracts which were signed no earlier than the publication date of the consultation (ie 20 November 2024);
- fits the eligibility requirements outlined in the APM Governance Document and Chapter 3 of this decision document; and
- is reported to Ofgem within one month of commencement of the licence taking effect.

5.15 Allowing retrospective applications such as those described above will have no additional cost to consumers other than those already accounted for in our overall assessment of the impact of the APM, and should have a positive impact in furthering the objectives of the APM.

5.16 We do not agree with the respondent that suggested that allowing retrospective applications would have a distorting effect on TO planning and procurement priorities. This is because TOs are supportive of our position on this question and set out in their responses that allowing retrospective applications would allow them to proceed with planning their procurement activities.

Confidentiality

5.17 Nine respondents agreed that most of the data gathered through the ongoing operation of the APM would be commercially sensitive. As such we intend to keep commercially sensitive APM information confidential.

5.18 We do not consider that publishing a list of APM Cost Categories is commercially sensitive and we consider that consumers should know what they are (and are not) funding through the APM. This list has been set out in Chapter 3, and we would publicly consult on any additions or removals to this list.

5.19 Acknowledging the points raised regarding protecting current and future consumers and maintaining transparency in how consumer funds are used, in this document we have set out the overall value of initial APM funding. We will also report on total APM expenditure through any RIIO annual reports that we publish and when a review of the APM is undertaken, likely in 2028.

Appendix 1 – APM Impact Assessment

1. Introduction

Background

A1.1 Electricity networks in GB require significant build out in the coming years in order to meet government's ambition for GB to be supplied with clean power by 2030. For example, in 2023 National Grid estimated that it would need to build five times more transmission lines by 2030 than it had in the previous thirty years.[14]

A1.2 However, TOs have reported that a significant challenge to delivering this infrastructure is the constrained supply chain of both equipment and services. This has been caused by myriad factors: the war in Ukraine, the COVID-19 pandemic, and the global push towards net zero.

A1.3 As a consequence, the global supply chain is becoming increasingly constrained, with lead times for critical equipment increasing, and manufacturing capacity booked up several years in advance. These supply chain constraints could delay delivery of key transmission infrastructure projects, which in turn could jeopardise GB's plans to connect cheap, domestic sources of renewable energy to demand locations across the country.

Why is Ofgem/regulatory intervention necessary?

A1.4 Regulatory intervention is necessary because the global demand for ET equipment means that the procurement approach typically adopted by TOs under the RIIO regulatory framework may now risk delayed project delivery. This delay to project delivery could put at risk GB's plans to connect cheap, domestic sources of renewable generation, new hubs for demand growth such as data centres and the ability for GB to be supplied by clean power by 2030. Project delays can cause increases to overall consumer bills through additional constraint costs, and fewer renewables on the system, and more fossil fuels in generation – resulting in higher wholesale electricity prices and higher carbon emissions.

A1.5 TOs will typically only commit money to the supply chain once Ofgem has undertaken the project-specific cost assessment (eg through setting the RIIO-

14 https://committees.parliament.uk/writtenevidence/121816/pdf/

ET3 baseline, or through a re-opener) and provided an allowance which will fund the TOs' procurement activities.

A1.6 There is a risk that if TOs wait until this stage to start procuring equipment, lead times for equipment will extend beyond project delivery targets. These delays could result in a rise in consumer bills through constraint costs.

A1.7 TOs will not generally procure 'at risk', ie enter into contracts for equipment which require early payments/deposits without confidence of renumeration from Ofgem. Developing a new regulatory mechanism to support changes to the way TOs want to procure equipment is intended to mitigate the effects that this, considered alongside significant supply chain constraints, may have on project delivery timelines.

Purpose of the Impact Assessment

A1.8 Following feedback on the 'impact evaluation' section of our APM Consultation, we have undertaken an updated Impact Assessment to review consumer and wider market impacts of the APM.

A1.9 The purpose of this Impact Assessment is to assess the possible outcomes of the APM on constraint costs, Ofgem's consumer interest framework and strategic outcomes, carbon values, and the wider market.

Policy options and preferred solutions

A1.10 In this section we first set out the longlist of options that we considered for intervention, followed by a brief overview of the two shortlisted options.

Longlist of options

A1.11 We identified that the no intervention counterfactual (Option 1) would result in unsatisfactory outcomes for consumers – through potential delays to projects that are critical for achieving our target for a decarbonised power system, and could bring about potential increases in consumer bills through:

- constraint costs, as a result of delays to project delivery; or
- higher equipment costs, if the TOs have to pay higher prices due to less effective procurement under the current regulatory regime, or procuring at shorter notice.

A1.12 We therefore developed a longlist of potential interventions that could be taken forward. We set out below some of these longlist options to demonstrate the breadth of solutions that we considered, alongside a high-level explanation of why this option has not been carried forward to the shortlist.

A1.13 The main objective of the APM is to mitigate the impact of the supply chain on TOs, which might otherwise result in delays to project delivery (including of projects critical to net zero targets and/or increase costs to the consumer).

A1.14 In considering the longlist of options, we have placed most weight on the ability of each option to positively further our principal objective to protect consumers now and in the future by working to deliver a greener, fairer energy system. We consider Option 2 to be the most viable option in achieving this.

Option 1: no intervention counterfactual

A1.15 This would involve the TOs waiting until their projects achieve certain milestones before applying for and receiving funding to procure the required equipment and services project-by-project. This would include having a re-opener that allows us to approve individual projects in their entirety once there is confidence in the project need, design, etc. throughout the course of the price control.

A1.16 This option has worked sufficiently well in the past but is at risk of causing delays to project delivery (and potential increased costs for consumers) due to several factors including increased volume of projects and supply chain constraints that have arisen in recent years. The potential costs and benefits of this option are explored in greater detail in this Impact Assessment.

Option 2: ex ante funding for early supply chain commitments

A1.17 This would provide funding for TOs, agreed on an ex ante basis, to book factory slots for certain types of equipment before the project detail or need is certain, ie before we would typically approve the TOs to spend on a project.

A1.18 This option, the proposed APM, is viable as a solution and is deliverable. It would require a new regulatory mechanism, which takes time, but when considering options we identified this as being implementable within a year of identification as an option. When implemented it would give the TOs flexibility to spend as and when required, subject to a cap and specified rules. The main risk to consumers is that by procuring ahead of specific need there would be a risk of stranded procurement, if the envisaged need changes or does not materialise, and the main challenge of this option is to develop the detailed design to minimise this risk. The potential costs and benefits of this option are explored in greater detail in this Impact Assessment.

Option 3: case-by-case ex ante approval of procurement

A1.19 This would allow us to set ex ante funding for procurement commitments, linked to specific projects and made available to TOs in advance of a project achieving

planning permission (ie earlier than in Option 1, but later than in Option 2). This option would be similar to the procurement element of the early construction funding (ECF) provided for the ASTI projects as in our 2022 ASTI decision.[15]

A1.20 We consider that this option could be viable – eg as it has less risk of 'stranded procurement' than Option 2 – but it is less effective at enabling TOs to engage the supply chain in advance and in bulk. Under this option, supply chain commitments would be made later in the project process than in Option 2 (ie once the procurement case is approved for a specific project), potentially meaning a delay to projects (including those critical for the net zero transition) and/or higher costs.

Option 4: principles-based procurement mechanism with ex post review

A1.21 This would require us to set principles that the TOs comply with when spending money on placing deposits to get ahead of supply chain constraints. This would be subject to ex post assessment by Ofgem of efficiency of spend.

A1.22 We consider that this option is not viable. TOs may perceive that the risk of ex post disallowances would be too high to justify using the mechanism. In that case, this option would not resolve any of the objectives of the APM because TOs would still not be willing to spend early and in bulk if they were at risk of these costs being disallowed later. This option may also create cash flow challenges for the TOs, depending on the materiality at stake, which may further their reluctance to use the mechanism. Conversely, a potential challenge of ex post assessment is that the bar for Ofgem to determine ex post disallowances is high, so there would be some potential for inefficiencies that create costs for consumers.

A1.23 The potential advantage of this option in comparison to Option 2 is that in theory it would allow the TOs to make quicker decisions regarding booking supply chain capacity, but we anticipate that use of any such mechanism would be limited because of the perceived disallowance risk.

Option 5: Centralised bulk procurement

A1.24 This would involve the TOs providing a joint order book which can then be procured centrally – perhaps by the TOs, Ofgem, the government, or a third party to be established. It could potentially be industry wide including other developers beyond the three TOs.

[15] https://www.ofgem.gov.uk/decision/decision-accelerating-onshore-electricity-transmission-investment

A1.25 It would be practically very difficult to deliver in a short space of time due to varied procurement requirements among the TOs, as well as concerns about commercial sensitivity and competition law making sharing information difficult. Given the urgency of addressing supply chain constraints, we consider this is not viable at this time.

Option 6: Supply chain training

A1.26 As the supply chain is facing constraints, funding a centralised training programme to support the development of an expanded skilled workforce could help to ease these constraints. This option could be carried out alongside other options.

A1.27 We consider that this option is not viable. It would fail to address the funding gap that currently prevents TOs engaging the market in bulk early in the project development cycle. There would be huge difficulties in being able to track the expenditure to assess it for efficiency and reduce the risk of double counting in the context of the TOs' wider funding. We also consider supply chain training to be beyond Ofgem's remit.

A1.28 Our preferred option (Option 2) would provide a more viable alternative by providing some certainty to the supply chain that can be expected to give them confidence to invest in training their workforce, without facing the issues highlighted above.

Shortlist of options

A1.29 Below we set out a brief overview of the two shortlisted options:

- Option 1, a no intervention counterfactual; and
- Option 2, the APM for early supply chain commitments.

A1.30 Option 2 is our preferred policy option as the proposed scope minimises the volume of expenditure at risk, and the framework minimises the risk of stranded procurement.

A1.31 Throughout this Impact Assessment we will be comparing our preferred intervention (Option 2) to the counterfactual (Option 1).

Option 1: No intervention counterfactual (business as usual – BAU)

A1.32 A BAU approach would be to take no regulatory action in mitigating supply chain constraints, and keep the current model of regulatory funding. Currently, for projects for which a TO seeks allowances within a price control period (eg through a re-opener), the TO will identify a need for new infrastructure, select a

strategic option, and submit a needs case. Ofgem will then assess the needs case. Concurrently, the TO will be completing the ongoing detailed design, surveys, land agreements, and final planning consultation. Procurement for equipment does not typically begin until Ofgem has confirmed the need for the project, which may not occur until 1-2 years before construction is due to commence.

A1.33 This approach may no longer be optimal for the majority of projects, including due to:

- **Supply chain constraints.** Supply chain constraints and the resulting long lead times will delay project delivery, resulting in constraint costs, as well as jeopardising CP2030 ambitions. These constraint costs could be significant – in their CP2030 publication, NESO estimated an additional £7bn of constraint costs annually if the planned network is not delivered by 2030.[16]
- **Accelerated project timelines.** Even without supply chain constraints, we recognise that we are requiring faster project delivery. This acceleration has been influenced by wider decisions including changing the target for a clean power network from 2035 to 2030.
- **The current approach is designed to transfer procurement risk to TOs**. TOs could technically undertake these early supply chain commitments without the APM, but any deposits placed would be at the TOs' own risk. If we expected TOs to take this higher risk under the current framework, this would likely drive up the cost of capital and ultimately result in an increase in consumer bills. The proposed option of the APM aims to de-risk the TOs, avoiding this increase in the cost of capital and corresponding increase in consumer bills.

Option 2: APM for early supply chain commitments

A1.34 Our preferred option to address the challenges surrounding the constrained supply chain is to implement the APM with the design and scope described below. We consider that this design strikes the right balance of:

- Facilitating the TOs transacting with and securing supply chain capacity as early as possible (and earlier than in the counterfactual) to avoid delays to project delivery; and

[16] neso.energy/document/346651/download

- minimising the risk of stranded procurement that would represent a cost to consumers and reduce the net benefit of the overall APM.

A1.35 The APM is designed as an allowance that the TOs can use to procure necessary equipment to enable the rapid build out of the ET network. It serves as a funding pot for TOs to procure pre-agreed equipment, without needing Ofgem approval each time they spend. The APM allowance is accompanied by an annual re-opener, which would allow Ofgem to adjust the allowances, as well as to assess applications for bespoke equipment. The re-opener would also be used to adjust qualifying equipment for APM spend, reflecting any changes in market conditions.

A1.36 To determine whether procurement is eligible for APM funding, we are requiring that the TOs demonstrate three areas to allow us to maximise the benefit of the APM and reduce the risk that consumers are exposed to:

- **Requirement.** To demonstrate requirement, TOs must evidence to us that there is constraint within the supply chain, either through reduced capacity or long lead times. However, these constraints must be linked to consumer detriment. Where lead times are long, they should be provided in the context of what is normal or tolerable, and whether the given lead time will result in delayed project delivery.
- **Mitigation**. To mitigate the risk of stranded procurement, equipment procured under the APM must fit within the fungible/flexible/bespoke framework. Equipment should be highly fungible, meaning it is generic enough to be used across different projects – for example steel towers or wood poles. If it cannot be fungible, it should be flexible. Flexible procurement means that when contracts are signed, only a high-level known detail is given, and specification and project need can be determined closer to the delivery date. There may be some cases where procurement fits neither the fungible nor flexible framework, meaning it will be considered bespoke. Bespoke equipment will only be approved on a case-by-case basis, in order to minimise the risk of stranded procurement, should project need fall away.
- **Transparency**. TOs must commit to providing the required level of reporting on APM expenditure. We will require transparency from the TOs to allow us track and monitor spend of the APM and to reduce the risk of double funding.

Alignment with our statutory duties[17]

A1.37 Ofgem has several statutory duties with which it must comply when exercising its regulatory functions. We briefly highlight below how the proposed intervention aligns with these.

- **Principal objective**. The APM as set out under Option 2 is primarily motivated by our principal objective to protect the interests of existing and future consumers. The APM seeks to facilitate timely delivery of a decarbonised power system and to avoid potential additional costs that consumers may face if supply chain constraints cause delays to critical ET investments.
- **Biodiversity duty.** Ofgem must consider biodiversity when exercising any regulatory functions that may impact upon it. We do not consider that the APM will affect biodiversity, as the APM is focused on the early stage of procurement without considering or approving a design, location, etc of specific projects. Option 2 will not result in more or fewer projects progressing to construction than Option 1. Biodiversity concerns will continue to be considered as part of the relevant investment decision when a TO proposes a project that makes use of any procurement begun using APM funding.
- **Growth duty.** Ofgem must have regard to the desirability of promoting economic growth. The APM will have a positive impact on economic growth by supporting the expansion of the electricity network, including the timely delivery of transmission investments critical to linking new renewable generation to new or growing sources of electricity demand.
- **Net zero duty.** In determining what is in consumers' interests taken as a whole, Ofgem must include their interest in the UK government meeting its net zero 2050 target and interim carbon budgets. The APM will have a positive impact on our ability to meet these targets, by addressing a potential barrier to the delivery of ET infrastructure required to achieve a decarbonised power system.
- **The Public Sector Equality Duty.** Ofgem must have due regard to the need to eliminate discrimination, harassment and victimisation, advance equality of opportunity, foster good relations between groups, and any other conduct prohibited by or under the Equality Act 2010. The APM, and activities funded under it, are not expected to have effects that relate to this duty.

[17] Impact Assessment Guidance Paragraph 1.3

- **Strategy and policy statement for energy policy in Great Britain.** Ofgem must have regard to the strategic priorities set out in this statement. The APM does this as it is supporting delivery of a decarbonised power system, and because it is focused on consumers' best interests in seeking to avoid project delays and subsequent constraint costs that would be passed through to consumers.

2. Monetised and non-monetised costs and benefits of the APM

Summary

A1.38 In this section we set out the costs and benefits of introducing the APM that we have considered in reaching our decision to introduce it.

A1.39 We monetised two costs: those associated with potential stranding of equipment procured under the mechanism and those associated with the fund leading to earlier expenditure than would otherwise be the case. These costs are then compared with the potential constraint savings in 2030 identified by the NESO for CP2030. We make a conservative assumption that, should the APM not be in place, a proportion of the identified saving modelled by the NESO would be delayed by one year. The proportion determines the monetised benefit, and the higher the proportion the greater the benefit. A switching value can be calculated, where the APM changes from being negative for consumers (costs outweigh benefits) to positive for consumers (benefits exceed costs). This value is 15%. In other words, even with this highly conservative model, if the mechanism ensures that 15% of the benefit of CP2030 in 2030 is achieved it will generate a net positive outcome for consumers. Given the large number of projects that the APM is anticipated to affect, we consider it very likely that this switching value will be exceeded by a large margin. This results in a strong cost-benefit case for the mechanism – particularly when considered alongside the strong strategic case for intervention to support the TOs in delivering their commitments as regulated transmission owners and supporting delivery of GB's decarbonisation targets.

A1.40 Across all the monetised and non-monetised costs and benefits that we have not been able to robustly quantify we consider that the qualitative case for the APM is clear, as described across this section and section 3 of this Impact Assessment:

- There are certain potential costs, such as TOs being double-funded, which we do not expect to materialise in any meaningful manner;

- There are certain costs and benefits, such as whether we risk locking in high prices and the environmental benefits of network build-out, which we do not consider can be robustly quantified in the context of the APM; and
- Our qualitative assessment of potential benefits of the APM, including enabling TOs to procure in a manner more attractive to the supply chain and its alignment with Ofgem's objectives, and our review of consultation responses which are largely supportive of it, shows a strong benefits case for the regulatory intervention identified.

A1.41 We discuss all monetised and non-monetised costs and benefits in more detail below. We discuss potential wider impacts of the APM, such as the risk of market distortion, in section 3.

A1.42 We consider that the risk of inaction, which may result in project delays leading to network constraint costs as well as the cost of last-minute procurement, fully justify the intervention of the APM.

Quantified monetised costs and benefits of APM

A1.43 Our approach to quantifying the main benefits of the APM has drawn on the NESO's assessment of the impact of various network build levels and their effect on constraints in CP2030.[18] The main cost elements are stranded cost risks and the cost of adding the fund to RAV early based on the social time preference using the government discount rate of 3.5%.[19]

A1.44 Constraint costs are incurred when there is a physical constraint[20] on the network that means the NESO[21] asks one or more generators to reduce their electricity output, and has to ask one or more other generators to increase their electricity output – to balance the system given physical constraints. When this happens, the generators that reduce or increase their output are paid to do so. Constraint costs were more than £1bn in 2024,[22] continue to rise, and are expected to be the main driver of future balancing costs.[23]

[18] neso.energy/document/346651/download
[19] The Green Book (2022) - GOV.UK
[20] These physical constraints are a result of the electricity system having insufficient capacity to get electricity from where the optimal ("in merit") generation is located, to where demand is located. The optimal generation is determined by a series of factors, including seeking to minimise the cost of generation notwithstanding physical constraints.
[21] What are constraints payments? | National Energy System Operator
[22] Constraint Breakdown Costs and Volume | National Energy System Operator
[23] NESO balancing costs report Summar 2024

A1.45 These physical constraints, resulting in constraint costs, can be eased by increasing the ET network through the delivery of transmission investments such as those that the APM seeks to facilitate.

A1.46 The APM is, by design, not restricting funding to specific projects and so it is not possible to undertake a bottom-up assessment of what constraint costs the APM is helping to avoid. We can only use an indirect approach.

A1.47 NESO has estimated the impact of various network build levels in two pathways (Further Flex and Renewables, New Dispatch) against a baseline of a 2024 network. It anticipates that if the network were unchanged, £12.7bn of constraints would arise in 2030 in the first pathway or £10.9bn in the other. The best-case estimate is of a reduction of constraints to £1.86bn constraints in 2030 in Further Flex and Renewables and £1.07bn in New Dispatch. The NESO report highlights that the delay of even a single project until after 2030 could add over £0.5bn to annual constraint costs and increase emissions. We use the penultimate row of Table 1 in the report which implies a £8.2bn saving (ie average of Further Flex and Renewables and New Dispatch saving) as the basis of our calculations. Discounted to 2025 this has a value of £7bn.

A1.48 The APM will contribute to achieving constraint costs savings by helping to avoid delays to some projects and accelerating the delivery of others. Due to the APM being intentionally designed to not restrict funding to specific projects it is difficult to say how much of this saving the APM will help achieve, but we can identify the minimum proportion of the £7bn to break even. This proportion is referred to as a switching value, as it is the point where technically the proposal switches from being worthwhile to not worthwhile (considering only monetised costs and benefits).

A1.49 We also recognise that many additional benefits of the APM will occur beyond 2030, when the electricity network will need to continue to expand to meet growing electricity demand resulting from the increasing electrification of heat and transport.

A1.50 The initial financial value of the APM will be around £4bn. The APM would bring forward spending that would most likely be incurred anyway later (once projects reach specific funding milestones), rather than approving additional spend to what is proposed as part of wider system planning including CP2030, the tCSNP2 and CSNP. We therefore do not consider the total sum of the APM potential spend to be the "cost" of the APM for the purposes of Impact Assessment. Rather the cost is associated with incurring costs sooner rather

than later. This is reflected in earlier bill rises for consumers due to this expenditure being added to the RAV earlier.

A1.51 Another main cost of the APM for the purpose of Impact Assessment is the cost of any stranded procurement. This is where procurement takes place under the APM but is ultimately written off and not used for any project, and so this spend does not fall under the category of simply being accelerated.

A1.52 We give our views on these two areas below.

Stranded procurement

Change of requirement

A1.53 There is a risk that project need may fall away at a stage when, due to project design being narrowed down and even if the equipment was originally procured flexibly, it is too late to re-purpose the equipment and thus it would go unused or be 'stranded'.

A1.54 We have assumed the same level of project abandonment as in the ASTI Impact Assessment, which used 10%.[24] We have applied this 10% to the approximate £4bn APM spend, resulting in our £0.4bn estimate of stranded procurement.

A1.55 We consider that this estimated cost is an overestimate because:

- High likelihood of projects proceeding. We consider that there is a significant volume of identified and necessary projects which TOs can use APM funding to secure equipment for which are at very low risk of falling away. Many of these projects are already in development, and so we do not consider it likely that a project that has already commenced will be called off, and NESO analysis shows that a significant volume of projects beyond those in development will also be required in the short-medium term.
- High likelihood that contracts can be repurposed for other projects. Our mitigation built into the APM design – ie the requirement for fungibility or flexibility – means that project abandonment does not necessarily result in "stranded procurement".

A1.56 We consider that the cost associated with the small number of circumstances in which stranded procurement may occur is outweighed by the wider benefit of delivering the rapid expansion of transmission infrastructure required to meet net zero targets.

[24] Decision on accelerating onshore electricity transmission investment, Appendix 2.

Earlier bill rises

A1.57 The APM is accelerating spend and this has a cost. For society at large, the time trade-off is known as the 'social time preference rate' and is the discount rate in the Green Book, ie 3.5%.

A1.58 In some cases, APM spend will be around two years earlier than the counterfactual, and in other cases it may be 7 years earlier, but we expect that on average the acceleration will be around 3 or 4 years. The value of this earlier spending is calculated using discounting. An average 3-year advancement of £5bn[25] would cost £490m and a 4-year advancement £642m.

A1.59 This differential would be passed to consumers over many years and depreciated over the same length of time in both scenarios, but that depreciation period would start and finish slightly earlier under the APM. The APM is accelerating spend and therefore bill rises, with bill impacts potentially 2-7 years earlier than otherwise expected – up to £1-4 per household per year.[26]

Competitively Appointed Transmission Owners (CATO)

A1.60 There is further risk of stranded procurement if a TO uses the APM to procure equipment and/or services intended for a project that is later competitively appointed to a CATO.

A1.61 To minimise the risk of stranded procurement through CATOs, the APM is for equipment that is fungible and contracts which are flexible. This means that flexible or fungible procurement originally intended for a project which is later designated as a CATO should be able to be used in an alternative project, subject to the TO's pipeline.

A1.62 Bespoke equipment will only be approved on a case-by-case basis, likely for projects that we know will not be tendered under the CATO regime.

A1.63 As such, we have assumed no monetised cost resulting from this risk in our analysis. We further consider the impact of the APM on potential CATOs in section 3.

Break-even

A1.64 To conclude our consideration of monetised costs and benefits, we observe there is a potential constraint costs saving based on NESO figures of £7bn NPV. The

[25] We have used £5bn in this assessment, rather than the c.£4bn provided under the APM, to acknowledge that the cap on APM expenditure may increase in the future.
[26] 2023/24 prices.

monetised costs of the APM consist of a potential £400m stranded cost and the time value of funds entering the RAV (£490m to £643m). On this basis if the APM is successful in ensuring that at least 15% of the 2030 savings are attained for one year it will have achieved a positive result. This is a conservative estimate, as it includes assumption that the APM is only accelerating projects by one year – as constraint costs are incurred every year that a project is delayed, the true avoided cost could be higher if the APM is successful in accelerating investments by more than one year.

A1.65 The APM allows TOs to allocate funds to a wide portfolio of projects, so we consider it likely that this low threshold for success will be comfortably exceeded.

Non-monetised benefits of the APM

Avoided carbon emissions

A1.66 We discussed the easing of physical constraints and thus avoidance of constraint costs as a monetised benefit of the APM. When physical constraints are faced and the NESO has to ask some generators to reduce or increase their output, often the reduced output is from renewable generators (such as wind farms) and the increased output is from higher-emission generators (such as gas power plants). The net impact of this is an increase in carbon emissions as a result of the physical constraint.

A1.67 Therefore, we consider that by helping to deliver projects that ease physical constraints on the network, the APM is likely to help to reduce the use of high-emission electricity generation.

A1.68 The ambition of the government is that by 2030 clean sources will produce as much electricity as GB consumes (95% of generation). This will reduce average carbon emissions of generation from 171gCO2e/kWh in 2023 to below 50gCO2e/kWh by 2030.[27] When monetised using The Green Book valuations of avoided carbon[28] and CP2030 estimates of 287TWh annual electricity demand by 2030, this results in at least £4bn of carbon savings.

A1.69 However, it is difficult to assign a particular portion of this benefit to the APM and so we have chosen not to include a monetised value of avoided carbon

[27] assets.publishing.service.gov.uk/media/677bc80399c93b7286a396d6/clean-power-2030-action-plan-main-report.pdf
[28] The Green Book

emissions in our Impact Assessment. However, we expect that this would be an additional benefit of the APM.

Price impacts

A1.70 One concern raised in relation to the APM is that TOs could be procuring equipment in bulk when prices are at their peak, or that the APM may increase prices as a result of increasing demand.

A1.71 We acknowledge that prices for some key materials have increased as a result of increasing supply chain constraints, and that encouraging bulk purchases in the very near future means that the TOs may be procuring at a higher price than if they waited to procure on a project-by-project basis as need becomes more certain.

A1.72 However, there are several potential reasons why the APM could help to support lower prices than might exist in the counterfactual:

- Prices may continue to rise. Prices have been rising for several years prior to our proposal to introduce the APM. It might be equally or even more likely that prices could continue to rise if we do not take this action, given that global demand for materials (and services) required for ET is only set to rise as nations continue their drive for electrification and decarbonisation. On this basis, we do not consider it credible to suggest that the APM alone will increase prices.
- Bulk procurement. The APM will allow bulk procurement rather than waiting for projects to receive funding approval at different times. Bulk procurement often results in economies of scale as well as cost certainty for the TOs and therefore for bill impacts for consumers.
- Stimulating the supply chain. The volume of spend in the APM, and demonstration of commitment to delivering ET network expansion. This could encourage the supply chain to expand its capacity, including potentially within GB, and thus help to lower prices.
- Reduced administrative/regulatory burden. The volume of work that the TOs will be required to complete over the coming decade is unprecedented. To some extent, there will be efficiency savings for both the TOs and Ofgem in terms of administrative cost and regulatory burden in undertaking procurement in bulk rather than project-by-project.

A1.73 On balance, we consider that it is likely that the cost of equipment – for the TOs and consequently for consumer bills – will be lower with APM than without, but

choose to not make a monetised assumption either way in our Impact Assessment.

Stronger supply chain relationships

A1.74 Procuring in bulk through a mechanism such as the APM, rather than trying to contract with suppliers on a project-by-project basis, means that the TOs are presenting themselves as more attractive clients to their potential suppliers, than if procuring project-by-project. We are hopeful that this should put the TOs in a strong position to achieve commitments from their supply chain, as well as potentially being able to secure potential cost savings from procuring in bulk.

A1.75 This is especially important when considering that the relevant supply chains are typically in a global market, with the GB TOs competing with transmission developers internationally and especially from elsewhere in Europe. For example TenneT, a TO in the Netherlands and Germany, has secured large contracts with the same supply chain that the GB TOs are using, affecting available capacity.[29] The global demand for the same equipment is still increasing, meaning that this impact is likely to worsen.

A1.76 Furthermore, if we continue BAU, in some cases, TOs will have to use 'just-in-time' procurement to secure equipment to deliver projects on time. Not only would this risk delays if supply was not available at short notice, but it would also be more expensive, with higher upfront payments required to secure an order. Furthermore, just-in-time procurement forgoes the benefits of lower prices and supplier certainty from bulk procurement.

Non-monetised costs of the APM

Double funding

A1.77 As with all cases where we have overlapping regulatory funding mechanisms, there is the potential that the TOs receive double funding – that is, receiving funding through the APM that is in part or in whole also funded through another part of the price control. It is therefore important that we put in place measures to avoid this.

A1.78 For this reason "transparency" has been included in our evaluation of each area of scope, ensuring that when setting the scope of the APM we are repeatedly considering if and how we will track APM expenditure to ensure that we are able

[29] Eg a 2023 contract for supply and installation of cables, estimated at £1.5bn TenneT awards mega contract for high-voltage AC cables in the Netherlands and Germany

to account for these allowances in later assessments – such as when determining the full project cost allowance.

A1.79 To facilitate the avoidance of double funding resulting from the APM, we will be placing reporting requirements on the TOs. While some information around the APM will be held in new sections of existing documents (eg the Regulatory Reporting Packs), we will create a centralised log of APM spending, the APM Register. The APM Register will be used to track and monitor spend. The APM register is a confidential register which Ofgem will maintain to track and monitor APM spend for each TO.

A1.80 There are three sections to the APM register, which will occur in sequence:

- APM allowance. This would be populated using information provided by the TOs, giving a high level indication of how the TO expects its spend to be split across the APM expenditure categories. It would also highlight if any allowances are ringfenced due to that procurement being bespoke in the context of the APM.
- TOs report on procurement. The TOs will then be required to provide us with updated information when they commit to spending under the APM through supplier contracts, and would also be required to provide updates once allocating APM-procured equipment/services to specific projects.
- TOs report on allocation to projects. When allocating APM-procured equipment/services to projects, the TO must inform us of which project the equipment/services have been allocated to how many units have been allocated, and the final total equipment cost for these units. Once we have accounted for the APM expenditure in its cost assessment, we will indicate that in the APM register to demonstrate that it is now accounted for within the relevant project rather than under the APM.

A1.81 As such we do not consider that there are likely to be material monetisable costs in this area, and so have not considered it for the purposes of our Impact Assessment.

3. Wider impacts

Effect on competition

A1.82 We received responses to our consultation suggesting that an unintended consequence of the APM might be an adverse effect on competition (market distortion), driving up prices and reducing availability for other market

participants such as Distribution Network Operators (DNOs), offshore wind developers, CATOs and interconnector developers.

A1.83 However, we are confident that it is the correct decision to proceed with the APM, despite the perceived risks to other market participants, for the reasons set out in the sub-sections below.

Prioritising transmission infrastructure

A1.84 To meet decarbonisation targets, including those in CP2030, the whole electricity network will need rapid build out, not just 'onshore' transmission infrastructure. However, it is essential that we have the necessary onshore ET infrastructure in place first, to connect sources of electricity generation to the network, and then to transport electricity from where it is generated to where it is used in homes and businesses. Without this the constraint and carbon emission costs discussed in section 2 could be exacerbated, as new generation and/or interconnection will be built but be largely unable to export onto the still constrained grid. Similarly, electricity distribution (ED) networks may not be able to meet increasing electricity demand for electric vehicles and heat pumps if the ET network cannot transport power from where it is generated to where it is needed.

A1.85 Overall the GB consumer benefits of enabling the build-out of the GB onshore transmission network should outweigh any costs for other GB energy market participants, which we explore in the two sections below.

Impacts on other transmission companies

Summary

A1.86 We have considered the feedback from various stakeholders that the APM may detrimentally impact the market competitiveness of offshore wind developers, CATOs and interconnectors, unless these participants are given a similar mechanism.

A1.87 We accept that there could be some impact of the APM on such developers. However, the extent of that impact is uncertain because it will depend on factors such as the timing of their procurement, growth in supply chain capacity and how they engage with all supply chain participants in the global market. Even where there are impacts, we consider these to be necessary given the importance of prioritising the build-out of the GB onshore ET network, as described at paragraphs A1.84-A1.85 above.

A1.88 We set out our views on this in further detail below.

Supply chain challenges caused by the APM

A1.89 GB TOs and CATO, offshore wind and interconnector developers operate in the same global market for equipment. There are sizeable supply chain participants that these organisations work with that are based across Europe, Asia and America. As such, we agree with the consultation responses which identified that these developers operate in the same supply chain environment as the TOs, and that they are likely to be experiencing similar challenges to the TOs in that environment.

A1.90 Because of this, we also accept that the TOs being encouraged through the APM to procure earlier than they did previously could have an impact on these market participants (ie CATO, offshore wind and interconnector developers), if those participants do not engage the market in a similar manner and TOs book up large portions of supply chain capacity of the providers that those market participants most commonly work with. Equally, we note that 'supply chain capacity' is not a fixed concept, and will vary depending on factors such as the time horizon in which a company is seeking procure, or whether there is enough demand that the supply chain responds to increase its manufacturing capability. If realised, this impact would likely come in the form other transmission developers receiving later manufacturing slots than they otherwise may have done, or those developers needing to engage different supply chain participants.

A1.91 However, it is key to note that the GB TOs make up a small portion of worldwide demand for ET equipment, with markets such as the European Union, United States, China and Japan outstripping GB demand for ET equipment due to their relative sizes. For example, TenneT in Germany and the Netherlands committed €30bn[30] of transmission related investment in 2023 and the Chinese State Grid committed $40bn in 2024.[31] So whilst the APM will improve TO competitiveness in this market, the direct impact of the APM on other market participants, in a global market, should be limited.

A1.92 Given the nature of the global market for ET equipment, it would also not be reasonable to assume that without the APM those supply chain slots would necessarily be available for any one market participant, such as CATOs, offshore wind developers or interconnectors. Those slots could easily be booked up by

[30] Around €30 billion: Europe's largest-ever contracting pack-age for security of supply, the energy transition and climate protection launched
[31] See page 16 of the Building the Future Transmission Grid report, and Chapter 1 of that report is generally helpful for setting out the scale of global demand.

transmission companies in other countries if they were not booked by the GB TOs courtesy of the APM.

A1.93 Similarly, and as described at paragraphs A1.72-A1.73, we do not expect that the APM will materially increase the prices of electrical equipment, and we hope that in the medium-term it could help to bring these prices down if supply chain capacity in the UK increased as a result of the APM.

A1.94 Overall, we agree that the APM may make it more difficult to some CATO, offshore wind and interconnector developers to engage with the parts of the supply chain that the GB TOs are also engaged with, as some supply chain capacity will be booked up as a result of the APM. However, we consider that this impact should be relatively limited in the context of the GB TO share of global demand for ET equipment and the ability for developers to engage with a variety of supply chain participants.

Changed perceptions as a result of the APM

A1.95 We do not consider that the APM is creating a new problem or impact in encouraging the supply chain to work with TOs ahead of CATO, offshore wind and interconnector developers, as suggested by some consultation responses. TO have always had significantly larger market share than these other industry participants given the size of their networks, regardless of the APM. As such, the APM should have only a limited impact the way in which these developers are perceived by the supply chain.

A1.96 In general, CATO, offshore wind and interconnector developers will always engage the market on a project-by-project basis, in a similar manner to how TOs currently work. The APM might move the TOs to a more proactive 'bulk' approach to procurement, which as discussed throughout section 2 should carry significant consumer benefits and may be attractive to the supply chain. However, the project-specific financing and regulatory approach of CATO, offshore wind and interconnector developers means that it would be very unlikely that such a 'bulk' approach to procurement in these sectors would be viable.

Transferability of the APM to other regulatory regimes

A1.97 CATOs, when the regime is operational, would be the TOs' closest equivalents in the wider market for electrical equipment. Given the focus on the development of an early model of competition under the onshore CATO regime, successful CATOs should be able to engage with the supply chain sufficiently early to avoid

project delays. We have sought to design the APM in a manner that avoids distortion of competitive tenders, by ensuring that activity relating to projects that are to be competitively tendered under the CATO regime are not eligible for funding through the APM. Nonetheless, as we establish the CATO model, we will consider whether there are elements of the APM that should be extended to it.

A1.98 We are working with current and potential interconnector developers, and government, on whether a funding approach that achieves similar outcomes to the APM could be introduced in that sector. These conversations are at a very early stage.

A1.99 The regulatory regime for funding and developing offshore wind projects currently sits with government's Contracts for Difference regime, and as such it would not be our role to introduce a regulatory equivalent to the APM in that regime. We are currently developing an Offshore Transmission Owner (OFTO) build model to facilitate additional offshore network co-ordination. While developing this we will consider whether there are elements of the APM that should be extended to that model.

A1.100 Though we see challenges of implementing an APM-like mechanism for offshore wind, we do see opportunities for developers to be more strategic with their procurement activities at group level, where appropriate. We will continue to consider other methods for supporting offshore wind procurement and welcome industry engagement on this matter.

A1.101 We will continue to consider whether there are elements of the APM that it would be in the GB consumers' interest to extend to other regulatory regimes that we operate.

Impacts on DNOs and Independent Distribution Network Operators (IDNOS)

Summary

A1.102 We currently consider that the APM is not necessary or appropriate for implementation in the RIIO price control for ED. While there is some limited overlap in the equipment used by ED and ET, the RIIO-ED2 price control already allows the DNOs to engage with the supply chain similar to how the TOs will be able to engage through the APM.

A1.103 The APM should not have any tangible impact on IDNOs, given the very limited overlaps in the equipment used between them and TOs.

A1.104 We set out our views on this in further detail below.

Similarity of experiences of supply chain constraints

A1.105 We recognise that the ED sector is also facing supply chain constraints,[32] although these constraints appear less acute than in ET.

A1.106 The constraints experienced by TOs will also not necessarily be for the same pieces of equipment as DNOs and IDNOs, given that TOs procure equipment of a higher voltage. There is some risk of overlap in demand for 132kV equipment, which TOs, primarily in Scotland, will now be able to more proactively procure. However, for the reasons set out in the sub-section below, we do not consider this to be a material concern.

A1.107 Given the limited overlap between the sectors we do not expect the APM to increase the price of electrical equipment in the ED sector. Where there are overlaps, as described at paragraphs A1.72-A1.73, we do not expect that the APM will materially increase the prices of electrical equipment, and we hope that in the medium-term it could help to bring prices down if supply chain capacity increased.

Differences between transmission and distribution

A1.108 Our principal rationale for not rolling out the APM in RIIO-ED2 is that the design of RIIO-ED2, which is far less reliant on project-by-project assessments than ET, already allow DNOs to engage the supply chain in advance in advance and in bulk. If anything, the APM allows TOs to procure in a similar manner to DNOs, rather than giving them an unfair advantage over DNOs.

A1.109 A 2024 report on supply chain readiness commissioned by DESNZ highlighted that:[33]

> "Distribution network operators (DNOs) can ensure a consistent and secure pipeline of transformers and switchgear because they share forward-looking plans with approved suppliers."

A1.110 These forward-looking plans are enabled by the top-down approach to setting DNO totex allowances in RIIO-ED, which is different to RIIO-ET, where funding is often granted on a more project-by-project basis.

[32] Eg as highlighted in an April 2024 report commissioned by DESNZ: UK renewables deployment supply chain readiness study - Executive summary for industry and policymakers

[33] UK renewables deployment supply chain readiness study - Executive summary for industry and policymakers

A1.111 We have however received feedback from the supply chain that DNOs are not proactively engaging the supply chain in the manner expected when RIIO-ED2 was set, which is concerning to us. We intend to pick up this issue with DNOs through our work designing ED3.

4. Monitoring and evaluation

Monitoring and evaluating delivery of APM objectives

A1.112 Our APM monitoring and evaluation will attempt to determine learnings about what worked, for whom and whether the intervention delivered the intended outcomes. As described in the main decision document, our overarching objective is to reduce the risk of delayed project delivery. In implementing the APM, we can avoid potential constraint costs and detriment to consumers. The key evaluation question is:

> Have TOs engaged the supply chain earlier than they traditionally have done (ie in advance of regulatory approval for a project) and has this earlier engagement avoided delays to the delivery of transmission projects, avoiding constraint costs and constraints in the supply chain for equipment (and related services)?

A1.113 To evaluate this question, we will monitor the delivery and installation of equipment procured under the APM begins, which will be compared with current and historic procurement and installation timings of equipment. As procurement and installation under APM may not occur until late 2026, 2027 or 2028, we will undertake a preliminary assessment of the APM in 2028, potentially as part of discussions that will be happening around that time regarding RIIO-ET4.

A1.114 We assume that stranded procurement should be minimal and assume up to 10% as a high-end estimate in this Impact Assessment, and so stranded procurement is not expected to contribute to materially increasing costs for consumers. Therefore, this will be a metric to be monitored to achieve the policy objective. We will attempt to measure levels of stranded procurement of equipment under APM and compare it to previous assumed levels of stranded procurement.

Monitoring and evaluating wider impacts of the APM

A1.115 The evaluation will look at wider impacts of the APM to generate additional learnings from the evaluation, to help improve upon the policy in the future. We will monitor and evaluate some additional questions which explore the wider impacts of the APM.

Price Impacts

A1.116 A potential non-monetised benefit is the ability for TOs to bulk buy due to earlier engagement in the supply chain. This can lower prices compared to historical. We will require the TOs to report annually on how the APM allowances are spent and which projects the equipment purchased is used on. This information should provide us with insights within the one or two years. We will factor in our initial views regarding this when considering applications under the APM Re-opener during 2026 and 2027.

Effect on competition

A1.117 As set out in section 3 of this Impact Assessment, we are already actively considering the merits of applying some of the principles or mechanics of the APM into other regimes that we operate, such as the ED price controls, the interconnector regime and potential CATO models.

A1.118 However, we are not yet in a position where we are able to confirm the extent to which these principles or mechanics will be applied in these areas, either through our regulatory regimes or through other means.

A1.119 Regardless of the outcome of that ongoing discussion, we intend to monitor the impact of the APM on market distortion on an enduring basis. We will do this by:

- Receiving regular feedback from potentially affected parties through our business-as-usual engagement, or ad hoc sessions for those that we meet less regularly. This will allow those parties to provide evidence to us of the APM distorting the market when operational, eg impacting their ability to operate in the supply chain market.
- Including a dedicated assessment of the actual market distortion impact of the APM as part of the APM review that we intend to undertake in 2028, as referenced at paragraph **Error! Reference source not found.**.

Impact on supply chain capacity, including growth in GB supply chain

A1.120 One potential benefit of the APM that we have not sought to include in this Impact Assessment, either quantitatively or qualitatively, is the potential for the APM to trigger a growth in supply chain capacity, particularly supply chain capacity that is UK-based. We intend to monitor the impact of the APM on this by:

- Requiring that the TOs report to us on the volumes of APM spend that are allocated to UK-based supply chain parties.

- Engaging with BEAMA, the UK trade association for manufacturers and providers of energy infrastructure technologies and systems, and its member on plans to increase supply chain capacity on the back of the APM (and GB demand generally) through its Supply Chain Council.

5. Proportionality of analytical approach

A1.121 We consider that our analysis is proportional for the following reasons.

- We have provided greater insight into the long list of options and the reasons why we have selected our preferred option. Also following our initial consultation, we have extended our analysis to consider the points made in response to our consultation.
- It is not possible to reliably undertake a full quantitative analysis of the risks and benefits of the APM to support a typical cost-benefit analysis. This is due to APM expenditure not being allocated to specific projects; therefore, we cannot link APM spend to potential specific constraint costs, decarbonisation benefits or delay impacts.
- Likewise, we are unable to reliably quantify the increased risk of stranding for each type of equipment. Therefore, this IA has largely qualitatively assessed the impact of the APM, whilst including a high-level break-even calculation. The latter uses the only available data and is simple to interpret.

6. Summary and preferred option with description of implementation plan

Summary

A1.122 In summary, our proposed solution to the supply chain constraints faced by the TOs is to implement the APM. The design of the allowance, alongside the APM register with a pre-agreed list of eligible equipment to procure, will remove regulatory barriers which would otherwise slow down procurement, and jeopardise project delivery. Furthermore, the flexible/fungible/bespoke framework protects consumers from the risk of stranded procurement, by ensuring that procured equipment can fit a variety of project needs

A1.123 We believe that implementing the APM, with the scope focused on constrained equipment, is the right course of action to mitigate supply chain constraints and minimise risk of delayed project delivery.

Implementation

A1.124 The APM will be operated through the TO licence conditions and supported by a governance document.

Governance document

A1.125 The governance document will provide clear guidance on what the TOs must include in their applications for the APM, reporting requirements, how the APM re-opener will operate, and how the APM allowances and register will be updated.

Licence changes

A1.126 The APM will be introduced through a statutory modification to the RIIO-ET2 licences in early 2025, to allow the TOs to begin using the APM as soon as possible.

A1.127 In-period licence changes will be enabled by the APM re-opener, which will make adjustments to the APM register to reflect real world market conditions. The re-opener will be open for one week in April every year, and Ofgem holds the ability to trigger the re-opener if new supply constraints emerge, or market conditions improve. Any adjustment to APM allowances will be publicly consulted on.