

SCHEDULE A

DETAILED DRAFTING

2.2.5 Review of the Capital Revenue Requirement - CRR

(a) The Authority shall:

- (i) a request from the Licensee to review the CRR Formula for the purposes referred to in Conditions 2.2.5 (b) and (d) provided that such request is submitted no later than twelve (12) months prior to the relevant Review Date; or
- (ii) otherwise if the Authority considers it appropriate,

conduct a review of the CRR Formula in accordance with this Condition 2.2.5 and each such review shall have effect from the next following Review Date.

(b) In any review under this Condition 2.2.5 the Authority shall be entitled to consider whether there have been any changes since 01 October 2004 to the actual values, including Actual Capital Expenditure, grants and capitalised interest, which are used to calculate the CRR Formula (the "CRR Actuals") or to one or more of the following (the "CRR Variables"):

- (i) tax allowances, laws, statutory rules and regulations applicable to the Licensee's development, construction, operation and maintenance of the Economic Network;
- (ii) the inflation rate indicated by the Consumer Prices Index;
- (iii) tax rates;
- (iv) such other variables as the Authority may determine from time to time after consultation with the Licensee.

(c) The Licensee shall provide such information and explanation, documents and records as the Authority reasonably requires for the purpose of conducting its review in accordance with Condition 2.2.5 (b).

(d) Subject to Condition 2.2.5 (fe), if following a review as referred to in Condition

2.2.5 (b) the Authority reasonably deems it necessary or desirable, the Authority

shall be entitled by notice in writing to the Licensee with effect from the

relevant Review Date to:

- (i) amend, add to and/or delete the CRR Formula, any CRR Actuals or any CRR Variables; and
- (ii) recalculate the CRR Formula, taking into account any changes to the CRR Actuals and the CRR Variables, to produce an amended CRR_m^{fp} for all future months in the Revenue Recovery Period.

such that from the relevant Review Date, the CRR_m^{fp} will be calculated to ensure:

$$\sum_{m=z}^n \frac{CRR_m^{fp}}{(1+r_m)^{m-z}} = \sum_{m=1}^{z-1} \frac{CRR_m^{ap}}{(1+r_m)^{m-1}} + \frac{OAV_{m-1}}{p} + \frac{PVT_{m-1}}{p}$$

where

$m=1$ is the month when the First Operational Commencement Date, for pipeline p, occurs;

z is the month of the Review Date;

n is 300 at the 25th anniversary of the First Operational Commencement Date for pipeline p;

r_m is the nominal weighted average Rate of Return in month m calculated in accordance with paragraph 5 of Annex A;

CRR_m^{fp} is the forecast monthly capital revenue requirement in month m with respect to pipeline p, calculated in accordance with paragraph 2 of Annex A;

CRR_m^{ap} is the actual monthly capital revenue received in month m with respect to pipeline p, calculated in accordance with paragraph 2 of Annex A;

- OAV_m^p is the opening asset value in month m calculated in accordance with paragraph 2 of Annex A;
- $PVT_{m=1}^p$ is the present value of estimated grossed up tax payments in month $m=1$ calculated in accordance with paragraph 2 of Annex A; and
- p is the North-West Pipeline or South-North Pipeline or any Spur along with any associated Postalised Distribution Pipelines as appropriate.

(e) Subject to Condition 2.2.5(f), the Authority shall be entitled by notice in writing to the Licensee with effect from the relevant Review Date determine (in accordance with paragraph 5(a) of Annex A) the nominal post tax rate of return on equity, the level of financial gearing and the cost of debt for the purposes of the r_t , g_t and d_t terms in paragraph 5 of Annex A.

~~(e)(f)~~ Before serving a notice under Condition 2.2.5(d) or (e), making any amendments to the Formula the Authority shall provide details of the amendments and the reasons for them and give the Licensee an appropriate period (not being less than 28 days) to comment on them.

2.2.19 Additional Definitions and interpretation

“Actual Controllable Operating Expenditure” means the “Actual Controllable Operating Expenditure” notified by the Licensee in accordance with Condition 2.2.4 (l);

“Allowed Controllable Operating Expenditure” means “Controllable operating expenditure” less the amount of “Uncontrollable Operating Expenditure approved by the Authority under Condition 2.2.4 (g) or (h).”

“Formula Amendment” has the meaning given to that term in Condition 2.2.22;

2.2.21 Allocation of OS Revenues

2.2.21.1 The Licensee may, in respect of each Gas Year, retain the Licensee's OS Revenues

Share as calculated in accordance with the relevant provisions of the OS Scheme.

2.2.21.2 In respect of each Gas Year for which the Licensee has an obligation pursuant to the OS Scheme to make a payment during the Gas Year, the Licensee shall make such payment at the time prescribed and otherwise in accordance with the OS Scheme.

2.2.22 Disapplication

(a) This Condition 2.2.22 applies in the event that the Authority:

- (i) determines/amends, pursuant to Condition 2.2.4(g) or 2.2.4(h), the Allowed Operating Expenditure for any Gas Year t ;
- (ii) serves a notice under Condition 2.2.5(d)~~determines, pursuant to paragraph 5(a) of Annex A, the value to be given to the term r_t , g_t , or d_t , for the purposes of calculating r_m as set out in that paragraph;~~ or
- (iii) serves a notice under Condition 2.2.5(ed).

(b) For the purposes of this Condition 2.2.22:

- (i) any ~~amendment or~~ determination referred to in Condition 2.2.22(a)(i) ~~and 2.2.22(a)(ii)~~, ~~and~~ any amendment, addition or deletion set out in the notice referred to Condition 2.2.22(a)(iii) and any value set out in the notice referred to in Condition 2.2.22(a)(iii), is a "Formula Amendment"; and
- (ii) each Formula Amendment shall, for the purposes of Condition 2.2.22(~~e~~), constitute and be treated as a separate Formula Amendment (including where it may be made at or around the same time as any other Formula Amendment and where it is included in the same notice).

(c) Where the Authority makes a Formula Amendment:

(i) subject to the remaining provisions of this Condition 2.2.22, the Formula Amendment, and where a notice is served under Condition 2.2.5(d) the recalculation referred to in that notice (the "associated recalculation"), shall have effect for the relevant Gas Year t or on the relevant Review Date (as the case may be);

~~(i)~~(ii)

the Licensee may within 28 days of the date of the Authority's notification to it of the Formula Amendment serve a written notice on the Authority (a "Disapplication Notice") which shall identify the part(s) of the Formula Amendment the Licensee wishes to be disapplied, in which case:

~~(A)~~ those part(s) of the Formula Amendment identified in the Disapplication Notice shall not take effect; and

~~(B)~~(A) where the part(s) of the Formula Amendment identified in the Disapplication Notice relate to a value set out in the notice referred to in Condition 2.2.22(a)(iii) determination made under paragraph 5(a) of Annex A, the Rate of Return that applied on the date immediately prior to the relevant Review Date shall continue to apply on and from the relevant Review Date; and

~~(C)~~(B) where the part(s) of the Formula Amendment identified in the Disapplication Notice relate to a determination of an amendment to the Allowed Operating Expenditure, the Allowed Operating Expenditure which shall apply for each relevant Gas Year t shall be;

$$AOE_t = \left(\underset{t=-5}{\overset{t=-1}{AOE_t}} \right) \times 0.2$$

~~(ii)~~(iii) the Disapplication Notice may be withdrawn by the Licensee at any time within six months of the date of the Disapplication Notice;

~~(iii)~~(iv) if within six months after the date of the Disapplication Notice (provided such Disapplication Notice has not been withdrawn), the Authority publishes a decision under Article 14(8) of the Order to:

- (A) where the Disapplication Notice relates to a Formula Amendment in respect of the CRR Formula, CRR Actuals and CRR Variables, modify this Condition 2.2 in respect of the CRR Formula, CRR Actuals and CRR Variables (or any aspect of part of them);
- (B) where the Disapplication Notice relates to a Formula Amendment in respect of the Allowed Operating Expenditure, modify this Condition 2.2. in respect of the Allowed Operating Expenditure (or any aspect or part relating to it);
- (C) where the Disapplication Notice relates to a Formula Amendment in respect of a value or values set out in the notice referred to in Condition 2.2.22(a)(iii)~~the calculation of $r_{m,m}$ (as set out in paragraph 5(a) of Annex A)~~, modify this Condition 2.2 or Annex A in respect of that value or values ~~the calculation of $r_{m,m}$~~ (or any aspect or part relating to it),

in each case “the Modification Decision”, then Condition 2.2.22(d) shall apply.

- (d) Where this Condition 2.2.22(d) applies and;
 - (i) the Licensee either:
 - (A) does not exercise its right to appeal to the CMA against the Modification Decision in accordance with Article 14B of the Order; or
 - (B) does exercise that right, but the CMA refuses permission for or otherwise does not allow the appeal;
 - then:
 - (C) the part of the Formula Amendment contained within the Modification Decision (and as amended to reflect the Modification Decision), including where applicable any associated recalculation, shall apply in the period from the

~~relevant Review Date date of that notice~~ to the date of modification pursuant to Article 14(9) of the Order; and

(D) such adjustment as the Authority may direct shall be made to the Formula, and where applicable to CRRfpm, in respect of any future months in the Revenue Recovery Period to reflect the retrospective application of the Formula Amendment and, where applicable, any associated recalculation,

but otherwise the Formula Amendments, and where applicable the associated recalculation, referred to in the Disapplication Notice shall not apply;

(ii) the Licensee exercises its right to appeal to the CMA against the Modification Decision in accordance with Article 14B of the Order, and:

(A) the CMA quashes the Modification Decision of the Authority under Article 14E(2)(a) of the Order;~~and~~

~~(B) the CMA neither remits the matter back to the Authority under Article 14E(2)(b) of the Order nor substitutes its own decision for that of the Authority under Article 14E(2)(c) of the Order,~~

then the Formula Amendment, and where applicable the associated recalculation, referred to in the Disapplication Notice shall not apply; or

~~(iii) the Licensee exercises its right to appeal to the CMA against the Modification Decision in accordance with Article 14B of the Order, and the CMA reaches a conclusion other than one of those described in Conditions 2.2.22(d)(i) and (ii), then the Formula Amendment, and where applicable the associated recalculation, shall have effect in accordance with that conclusion or any decisions of the CMA or the Authority made pursuant to it.~~

ANNEX A: ACTUAL REQUIRED REVENUE FORMULA

5. Rate of Return

The applicable Rate of Return is expressed on a vanilla weighted average cost of capital basis and will apply to the North West Pipeline, South North Pipeline, and each of the Spurs and any associated Postalised Distribution Pipelines.

- (a) The nominal weighted average rate of return in month m is calculated according to the following formula:

$$r_{n_m} = [1 + g_t((1 + d_t) \cdot (1 + i_t) - 1) + (1 - g_t) \cdot re_t]^{1/12} - 1$$

where:

r_{n_m} is the nominal weighted average rate of return in month m ;

re_t is the nominal post tax rate of return on equity in Gas Year t and shall be determined by the Authority to apply at and with effect from each

Review Date, as notified to the Licensee by the Authority [and in accordance with Condition 2.2.5\(e\)](#), taking account of (amongst other relevant considerations) the prevailing market rates at the time of the determination;

g_t is the level of financial gearing as determined by the Authority to apply at and with effect from each Review Date; as notified to the Licensee by the Authority [and in accordance with Condition 2.2.5\(e\)](#),

d_t is the cost of debt as determined by the Authority to apply at and with effect from each Review Date, as notified to the Licensee by the Authority [and in accordance with Condition 2.2.5\(e\)](#), taking account of (amongst other relevant considerations) the prevailing market rates at the time of the determination.

(b) The regulatory allowed real weighted average rate of return in month m is calculated according to the following formula:

$$r_t = \frac{(1 + rn_m)}{(1 + i_m)}$$

(c) The regulatory allowed nominal weighted average rate of return in Gas Year t is calculated according to the following formula:

$$rn_t = (1 + rn_m)^{12} - 1$$