

# **Northern Ireland Electricity Transmission and distribution price controls 2012-17**

**Final determination**

23 October 2012

**Executive summary**

## 1 ABOUT THIS DOCUMENT

- 1.1 This document outlines our final determination for the fifth price control for Northern Ireland Electricity Ltd. This control will apply from 1 January 2013 to 30 September 2017. It is referred to as RP5.
- 1.2 This document contains a summary of the analyses we have undertaken to reach our final position for RP5.
- 1.3 We have also prepared a more detailed paper that includes further information about our analyses and the final determination. The paper can be accessed by clicking [here](#).
- 1.4 This price control will affect the network tariffs that are paid by all those who consumes electricity in Northern Ireland, or who generates electricity in Northern Ireland or Ireland and participates in the Single Electricity Market.
- 1.5 We published our draft determination, which set out our initial proposals, on 19 April 2012. The consultation closed on 19 July. We received 32 responses to the consultation and have published these on our website alongside this document<sup>1</sup>. We would like to thank all respondents and attendees at the stakeholder events for the time and effort they contributed to this process.
- 1.6 We have also published a separate document that outlines the key points made in each of the consultation responses, along with our comments on these. This responses document is also available on our website<sup>2</sup>.
- 1.7 We assessed the consultation responses in the light of our statutory duties. In coming to our final decisions we fully and carefully considered each of the responses. We also carefully considered any new information that NIE T&D submitted.
- 1.8 The outcomes that we expect to be delivered during the RP5 period (2013-17) are summarised in Table 1.1.
- 1.9 This price control will be implemented through modifications to NIE T&D's licence. These modifications are published for consultation in a separate document<sup>3</sup>. NIE T&D and other interested parties have four weeks to respond to the consultation on these.

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<sup>1</sup> [http://www.uregni.gov.uk/electricity/price\\_control/](http://www.uregni.gov.uk/electricity/price_control/)

<sup>2</sup> [http://www.uregni.gov.uk/electricity/price\\_control/](http://www.uregni.gov.uk/electricity/price_control/)

<sup>3</sup> [http://www.uregni.gov.uk/electricity/price\\_control/](http://www.uregni.gov.uk/electricity/price_control/)

**Table 1.1:** Expected outcomes for RP5

<b>Strategic theme</b>	<b>Expected outcomes (to be delivered within the revenues we set)</b>
<b>Security of supply</b>	<p>Maintain and develop an economic, safe, stable and reliable network.</p> <p>Ensure a timely and effective response to all new demands on the network (new connections, load growth &amp; renewables).</p>
<b>Sustainability</b>	<p>Facilitate delivery of the renewable target in the Department of Enterprise, Trade and Investment's (DETI) Strategic Energy Framework.</p>
<b>Customer service</b>	<p>Maintain continuous good customer service (as measured by 'customer minutes lost' and Guaranteed Standards of Service' metrics).</p>
<b>Other</b>	<p>Have effective business processes and information and reporting systems in place to ensure that regulatory reporting is transparent.</p> <p>Design and implement a programme to achieve best practice in asset management. This should include measuring asset condition and serviceability effectively (using, for example, load and asset health indices) in order to ensure that plans for the next price control period (RP6) are fully justified in terms of need, optimum intervention strategies, efficient costs and appropriate risk sharing.</p>

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## 2 INTRODUCTION

- 2.1 Our principal statutory objective is to protect the interests of customers of electricity services<sup>4</sup>. In Northern Ireland, the assets required to transmit and distribute electricity are owned by Northern Ireland Electricity Ltd.
- 2.2 Transmitting and distributing electricity is generally accepted as being a monopoly activity. This is because the high cost of duplicating the necessary assets would result in unnecessary high costs. This company is also responsible for planning, developing and maintaining the networks. They are also responsible for operating the distribution network.<sup>5</sup>
- 2.3 Northern Ireland Electricity Ltd (which is referred to as NIE T&D throughout this paper) has been owned by ESB since December 2010.
- 2.4 We make sure that customers' interests are protected by setting price controls. The objective of a price control is to ensure that NIE T&D, as a monopoly provider, does not set prices too high. At the same time we make sure that NIE T&D can finance its licensed activities to provide an adequate service.
- 2.5 To date we have set four price controls (RP1 to RP4), covering the period from 1992 to 2012. This fifth price control (RP5) covers the period 2013-17.
- 2.6 We have already consulted on the strategy<sup>6</sup> to be adopted for RP5. We also held three stakeholder events on this strategy, in conjunction with the Consumer Council for Northern Ireland (CCNI).
- 2.7 In April 2012, we published our draft determination for the RP5 price control. This covered all aspects of NIE T&D's revenue from the charges it makes for customers to use the transmission and distribution systems. In coming to our decisions, we must allow the company sufficient revenue to cover its:
- operating costs;
  - capital investments (through associated depreciation & return);
  - pensions; and
  - connections to the system.
- 2.8 Following publication of our RP5 draft determination we held three further stakeholder events, one of which was in conjunction with CCNI.

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<sup>4</sup> See Appendix C of RP5 Final Determination main paper: Statutory duties

<sup>5</sup> SONI is responsible for operating the transmission network.

<sup>6</sup>[http://www.uregni.gov.uk/uploads/publications/RP5\\_NIE\\_TD\\_Fifth\\_Price\\_Control\\_Strategy\\_Paper\\_FINAL.pdf](http://www.uregni.gov.uk/uploads/publications/RP5_NIE_TD_Fifth_Price_Control_Strategy_Paper_FINAL.pdf)

- 2.9 We received 32 responses to our draft determination, 31 of which are published on our website. We were asked to keep one response confidential. Of the 31 responses published, 16 were from consumer groups and 16 were from industry groups.
- 2.10 In August 2012 we also published two further draft determinations. These covered: changes to NIE T&D's capitalisation practice; and the mechanism we are putting in place to enable NIE T&D to claim capital expenditure for the integration of renewable generation and interconnection.
- 2.11 The price control defines separate limits for revenue from charges for the transmission and distribution systems. It does not include any revenue that NIE T&D collects under the PSO Levy.<sup>7</sup>
- 2.12 This document is our final determination on the revenue that NIE T&D will be allowed to claim from consumers to cover services provided between 1 January 2013 and 30 September 2017.
- 2.13 All costs in this document are in 2009-10 prices unless stated otherwise.
- 2.14 This document covers each of the aspects of NIE T&D's revenue in turn. It provides a short summary of the responses received to our draft determination and details any changes we have made as a result of either consideration of these responses or of new evidence that NIE T&D has provided.

### **3 APPROACH TO RP5**

- 3.1 RP4 was a five-year price control that began on 1 April 2007 and was due to end on 31 March 2012.
- 3.2 We will implement RP5 from 1 January 2013, which means that RP4 has been extended from 1 April 2012 to 31 December 2012. This has been necessary because of delays in receiving NIE T&D's full RP5 submission. As a result we needed more time to complete a robust assessment of the submission itself and to deal with the significant issues that were subsequently identified.

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<sup>7</sup> The PSO levy is a separate tariff that covers a number of cost items that are not related to the use of the electricity network.

- 3.3 For RP5 we will implement an RPI-X type price control, designed to incentivise NIE T&D to manage its operating and capital costs efficiently.

### **Using a Reporter**

- 3.4 A Reporter is an independent professional who audits, certifies and comments on submissions that are made by regulated companies to their regulators over a price control period.
- 3.5 In our draft determination we stated that we were minded to introduce a Reporter for RP5. Eight respondents commented on the advantages and disadvantages of this. Having carefully considered respondents' comments we are still of the view that the benefits from introducing a Reporter outweigh the costs. The main benefits include the fact that the Reporter will independently verify performance and will ensure that information is of a high quality and is provided in a complete form. This will improve the efficiency of the approvals processes.
- 3.6 The Reporter's role and scope are set out in detail in the Terms of Reference in appendix L of the main document. This is deliberately flexible so that the scale of the work can vary as required. The Terms of Reference will be issued to NIE T&D. The regulated company will then tender and recommend a shortlist of suitable Reporters. We will then appoint the Reporter from this shortlist.
- 3.7 It is anticipated that the Reporter will be in place from 31 August 2013 and we have included a proposed licence modification to reflect the role of the reporter in RP5.

### **Transmission system operator (TSO) certification**

- 3.8 NIE T&D has applied for TSO certification under EC Directive 2009/72/EC (IME3), on the basis that the current transmission ownership, planning, development, maintenance and operating arrangements remain unchanged. This certification decision has not yet been made..
- 3.9 This final determination has been written on the basis that NIE T&D's current arrangements will stay in place. However, changes to this final determination

may be required pending this decision<sup>8</sup>. NIE T&D's licence would be amended to allow any such changes to be made. This would require further consultation.

#### **4 CHANGE TO CAPITALISATION PRACTICE DURING RP3 AND RP4**

4.1 In our RP5 draft determination we explained that we had initiated an investigation into NIE T&D's accounts. The purpose of the investigation was to determine whether or not any outperformance had resulted from a change in NIE T&D's capitalisation practice.

4.2 For the RP4 price control, NIE T&D was given an operating expenditure (opex) allowance. Under the principles and rules, if NIE T&D actually incurred less operating costs, it was entitled to keep the difference in full. This is known as outperformance. NIE T&D was also allowed full recovery of its actual capital expenditure (capex).

4.3 This largely reflected proposals that NIE T&D had made for RP4 (referred to as the 'composite proposals') and which were accepted in the final RP4 determination. This proposal contained the statement that:

*"The use of actual expenditure to determine future revenue entitlement removes ambiguity around the allocation of costs as between opex and capex. For regulatory purposes actual expenditure is recovered either via the RAB over 40 years or via the opex allowance but not through both."*

4.4 During the last two years of RP3, and after we had indicated our acceptance of NIE T&D's proposals for RP4, the company changed its capitalisation practice with regards to a number of cost items.

4.5 The change in practice meant that some cost items or their apportionment that were treated as opex could now be treated as capex. We became aware of this during our review of the RP4 opex outperformance.

4.6 The nature of the RP4 mechanism meant that consumers would pay twice for certain services that NIE T&D provided if this adjustment were not corrected. It

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<sup>8</sup> [http://www.allislandproject.org/en/transmission\\_current\\_consultations.aspx?article=ee4464ea-1c6a-423c-a3dc-1f07c9561290&mode=author](http://www.allislandproject.org/en/transmission_current_consultations.aspx?article=ee4464ea-1c6a-423c-a3dc-1f07c9561290&mode=author).



should be noted that this is the opposite of what NIE T&D said in making its proposals in relation to the RP4 price control.

- 4.7 We undertook an investigation into this change, including commissioning consultant auditors to examine NIE T&D's regulatory accounts over this period. On 30 August 2012, we published the findings of this investigation, along with our draft determination<sup>9</sup> on how to adjust the company's income to ensure that customers would not pay twice for services provided by NIE T&D. We proposed a revenue adjustment of £2.7 million and a reduction of £31.7 million to the regulated asset base (RAB). We also considered NIE T&D's policy on asset disposals.
- 4.8 We received two responses to this draft determination, one of which was NIE T&D. These are published on our website. NIE T&D commissioned KPMG to undertake a review of its accounting practices and provided a copy of its report along with the company's response. NIE T&D rejected the proposals in the draft determination.
- 4.9 The other respondent raised concerns about the fact that we had not detected the change in practice for a period of seven years. The respondent asked us to consider imposing further sanctions on NIE T&D, under article 45 of the Energy Order 2003. They added that if no further sanctions were considered appropriate then an explanation should be given as to why this was the case.

### **Final determination for capitalisation practice change**

- 4.10 We have never claimed that NIE T&D has changed its accounting policy in relation to the capitalisation of costs over the period under review. However, our analysis does demonstrate that there were changes in accounting estimates that have had a material impact on the allocation of costs between opex and capex. NIE T&D stated in its response that it had made these changes. To clarify we do not believe, nor have we ever asserted, that any accounting rules have been broken.
- 4.11 In conjunction with our consultants we have considered each of the points raised by NIE T&D and KPMG. Our draft determination proposed an adjustment of £2.7 million to revenue allowance within RP4, based on using a pre-tax WACC. In its response, NIE T&D stated that the adjustment had been

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<sup>9</sup> [http://www.uregni.gov.uk/publications/draft\\_determination\\_consultants\\_report](http://www.uregni.gov.uk/publications/draft_determination_consultants_report)

overstated and that a vanilla WACC approach should be used, along with the addition of a separate allowance for tax. By adopting this approach, no revenue adjustment would be made.

- 4.12 We have accepted that using a vanilla WACC and tax allowance is in keeping with the formula defined in NIE T&D's licence for the period when this money was recovered from customers. We therefore propose that no adjustment is to be made with respect to revenue adjustment.
- 4.13 The draft determination proposed a RAB adjustment of £31.7 million to correct for the change in capitalisation practice adjustments. We do not consider that any adjustment is required to the original capitalisation figure and so we are not persuaded to change our original position.
- 4.14 We accept the company's interpretation of the rules around asset disposal and will not be making any adjustment..
- 4.15 As the RP4 opex allowance was based on RP3 actual opex there is a requirement to ensure that the cost basis remains constant to avoid any double counting. We have decided that NIE T&D should be able to keep the opex allowance in RP4 and that an adjustment of the RAB of £31.7 million should be carried out at the start of RP5.

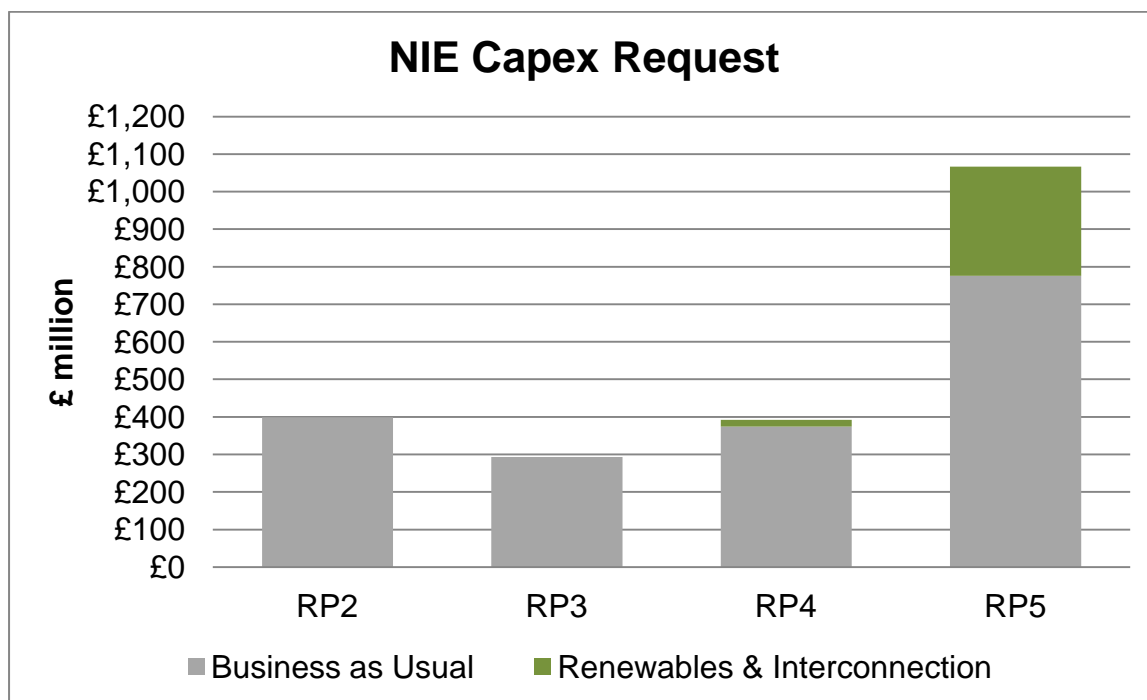
## 5 RP5 CAPEX

- 5.1 NIE T&D has requested a significant increase in its capital spend for RP5. It published a paper<sup>10</sup> detailing an increase in 'business as usual' capital investment from £374 million in RP4 to £606 million in RP5. In a subsequent submission<sup>11</sup> this was increased again to £776 million (107% higher than RP4). When it made its submission, NIE T&D also expected to invest an additional £291 million in infrastructure to support the development of renewable generation and further interconnection. These increases are shown in Figure 5.1.

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<sup>10</sup> [http://www.uregni.gov.uk/uploads/publications/Capital\\_Investment\\_Requirements\\_for\\_RP5\\_NIE\\_Paper.pdf](http://www.uregni.gov.uk/uploads/publications/Capital_Investment_Requirements_for_RP5_NIE_Paper.pdf)

<sup>11</sup> NIE T&D's response to the Utility Regulator dated 27/01/2012

**Figure 5.1: NIE T&D's request for capital expenditure for RP5****Draft determination for RP5 capex**

5.2 The company submitted proposals for mitigating uncertainty during RP5. We reviewed these and also considered mechanisms that would satisfy our statutory duties to protect consumers and ensure that NIE T&D can fund its activities. Based on this, we separated the capex projects into three funds depending on the type of activity:

- **Fund 1:** Asset replacement and refurbishment (both planned and unplanned)
- **Fund 2:** load related investment, metering (excluding smart meters), connections and less predictable investment
- **Fund 3:** Large projects for renewable generation or interconnection, where there is material uncertainty over the timing and level of expenditure.

5.3 For each fund, the reporter will need to verify delivery and substitution between asset types.

5.4 Based on the information provided by the company before we published our draft determination, we were minded to allow £314.7 million for business as

usual capex during RP5 within Funds 1 & 2. All capex investment will be verified by the Reporter.

- 5.5 In addition, we were minded to assess Fund 3 projects for developing the network for renewable generation and interconnection on an individual basis as the need and actual cost is determined by NIE T&D during the RP5 period.

### **Final determination for RP5 capex**

- 5.6 During the consultation period, NIE T&D provided additional information about its capex investment plans. The company also provided significant data during our discussions once the consultation period closed.
- 5.7 We employed [consultants] SKM to reassess all of the information that NIE T&D provided. They also undertook modelling of NIE T&D's asset replacement proposals, to ensure that the volumes of work funded during RP5 are comparable with the amounts that similar companies in GB would spend.
- 5.8 We have reviewed the projects to be included in Fund 3. We have reallocated two further projects into this fund (from fund 1 and fund 2) as their scope is currently uncertain because of ongoing assessments of the impact that non-synchronous generation has on system stability. In its response to our questions, NIE T&D has revised its estimate of the amount of investment in interconnection and renewables down to £223 million during RP5.
- 5.9 On 31 July 2012, after the consultation period for our draft determination had closed, DETI announced<sup>12</sup> that it intended that smart meters should be rolled out to electricity consumers in Northern Ireland. Any costs associated with this roll out will be assessed and recovered under Fund 3. We will be consulting on the implementation of this policy, including the roles and responsibilities of each party involved in the process. This will reduce expenditure under Fund 2.
- 5.10 We accept that NIE T&D will need to undertake trials and investment related to smart grids during RP5. However, the proposals included in the company's submission require further development. These trials and any subsequent investments will be included in Fund 3.
- 5.11 Our final determination for RP5 capex is detailed in Table 5.1. It should be noted that these figures show a five year view to allow comparison with NIE T&D's submission.

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<sup>12</sup> <http://www.northernireland.gov.uk/news-deti-310712-northern-ireland-to>

- 5.12 In order to allow NIE T&D to continue with its capital investment programme, the our board has approved a further capex budget for the period of 1 October 2012 until the beginning of RP5.
- 5.13 The amount of capital investment specified in this final determination covers the five years from 1 October 2012 to 30 September 2017. In the licence modifications, the amount that is subject to the RP5 price control is defined as the amount approved minus the actual spend over the three months between 1 October 2012 and 31 December 2012.
- 5.14 The actual investment over those three months will be added to the RAB in line with the RP4 mechanism.

**Table 5.1: Final determination capital expenditure allowance for RP5**

Fund	Spend area (£m)	NIE T&D submission		Our final determination	
		Transmission	Distribution	Transmission	Distribution
1	Asset replacement	£119.0	£357.3	£92.4	£202.4
2	Load related capex Network IT; network performance; changes to legislation; non-network IT; new technology trials	£60.1	£142.8	£11.6	£31.3
R	Ring-fenced for metering	£0.0	£37.5	0	£20.5
	Ring-fenced for connections and alterations	£0.0	£59.3	0	£37.3
<b>Subtotal</b>		<b>£179.1</b>	<b>£596.9</b>	<b>£104.00</b>	<b>£291.50</b>
		<b>£776.0</b>		<b>£395.50</b>	
3	Medium-term plan	£70.3	£0.0	TBD	TBD
	Wind farm clusters	£17.6	£0.0	TBD	TBD
	RIDP	£127.2	£0.0	TBD	TBD
	Tyrone - Cavan Interconnector	£76.0	£0.0	TBD	TBD
<b>Subtotal</b>		<b>£291.1</b>	<b>£0.0</b>	<b>TBD</b>	<b>TBD</b>
<b>Total</b>		<b>£470.2</b>	<b>£596.9</b>	<b>TBD</b>	<b>TBD</b>
		<b>£1,067.1</b>		<b>TBD<sup>13</sup></b>	

5.15 We have compared the capex amounts from our draft determination in table 5.2.

<sup>13</sup> NIE T&D's latest best estimate is £223 million for the transmission projects.

**Table 5.2: Comparison with RP5 draft determination**

Fund	Spend area (£m)	NIE T&D submission		Our final determination	
		Transmission	Distribution	Transmission	Distribution
1	Asset replacement	£74.7	£118.8	£92.4	£202.4
2	Load related capex Network IT; network performance; changes to legislation; non-network IT; new technology trials	£34.7	£41.0	£11.6	£31.3
R	Ring-fenced for metering	£0.0	£18.6	£0.0	£20.5
	Ring-fenced for connections and alterations	£0.0	£26.9	£0.0	£37.3
<b>Subtotal</b>		<b>£109.4</b>	<b>£205.3</b>	<b>£104.0</b>	<b>£291.5</b>
		<b>£314.7</b>		<b>£395.5</b>	

## 6 RP5 OPEX

- 6.1 NIE T&D proposed a total opex of £345 million for RP5. This comprised controllable, uncontrollable and 'new' opex. The RP5 submission is 22% higher than the total actual opex of £283.5 million that was incurred during RP4.
- 6.2 Controllable opex includes: payroll; repairs and maintenance; IT & Telecoms; NIE Powerteam Ltd costs; corporate costs; insurance; property costs; professional services; meter reading; and other general controllable opex.
- 6.3 Uncontrollable opex refers to operating expenditure on which NIE T&D is deemed to have little or no impact. This category has historically included rates, wayleaves and licence fees. For RP5, NIE T&D has also included injurious affection costs. In total, the company has identified uncontrollable opex during RP5 of £107 million.

## Draft determination for opex

- 6.4 Before assessing NIE T&D's RP5 submission for 'new' opex, we established a 'base year' as a starting point for analysing controllable and uncontrollable opex. We focused on actual expenditure, reconciled to the latest audited accounts (2009-10<sup>14</sup>).
- 6.5 We undertook a bottom-up analysis of actual costs in 2009-10, then adjusted for 'one-off' costs and non-recurring costs. In parallel with this we also commissioned economic consultants Cambridge Economic Policy Associates (CEPA) to complete a benchmarking exercise of NIE T&D's opex in order to gauge whether efficiencies could be achieved.
- 6.6 We applied two efficiency adjustments: an initial adjustment of 9% to reflect existing inefficiencies identified through our benchmarking of RP4 performance; and a 1% annual reduction to reflect ongoing efficiency.
- 6.7 In our draft determination, we said that we were minded to allow £168.2 million for controllable opex during RP5.
- 6.8 In the draft determination we allowed for uncontrollable elements of opex was £88.8 million. We proposed to introduce a Reporter for RP5 and an indicative value of £300,000 a year (or £1.5 million in total) is proposed in the uncontrollable opex category for this. The Reporter will be appointed by us and the scope of work will be determined by the need to protect consumers. Therefore we consider this to be an uncontrollable cost as NIE T&D will not be able to influence it.
- 6.9 To incentivise NIE T&D to minimise uncontrollable costs, we proposed a risk sharing mechanism for any changes in these costs.
- 6.10 The total opex in the draft determination was £257 million.

## Final determination

- 6.11 Following publication of our draft determination, we received detailed comments from NIE T&D and other stakeholders in response to our RP5 opex proposals. We considered all views and have updated our position based on additional or new information provided.

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<sup>14</sup> 2009/10 annual accounts were the latest available accounts at the time of NIE T&D's price control submission.



6.12 Since the draft determination was published we have reassessed a number of cost items. After analysis of new evidence the following changes have been made to the opex allowance:

- The base year amount used in our decision has increased due to a modelling issue.
- The efficiency factor applied to controllable opex has reduced from 9% to 7%.
- Meter reading and 'Enduring Solution' allowances have increased based on new information submitted by NIE T&D.
- The renewables baseline allowance has decreased to ensure that there is no double counting with a previously approved allowance.
- Other controllable opex has increased slightly.
- Real price effects (RPEs) have decreased.

6.13 The total change in RP5 controllable opex since the draft determination is an increase of £14 million, from £257 million to £271 million for a five year period. No changes have been made to the uncontrollable opex amount. The uncontrollable opex allowance is £88.8 million.

6.14 We have adjusted our allowances to reflect the fact that RP5 will last for four years and nine months.

**Table 6.1: Final determination operating expenditure allowance for RP5**

<b>£m</b>	<b>NIE T&amp;D submission</b>	<b>Draft determination</b>	<b>Final determination (5 years)</b>	<b>Final determination (4 yrs 9 mth)</b>
<b>Controllable opex</b>	237.5	168.2	182.2	173.6
<b>Uncontrollable opex</b>	107.3	88.8	88.8	84.3
<b>Total opex</b>	<b>344.8</b>	<b>257.0</b>	<b>271.0</b>	<b>257.9</b>

## 7 PENSIONS COSTS IN RP5

7.1 NIE T&D submitted total pension costs of £77.2 million (in 2009-10 prices) for RP5. This consisted of:

- £10.5 million of ongoing pension costs (to cover both defined benefit and defined contribution members); and
- £66.7 million of deficit repair costs associated with the defined benefit plan.

7.2 NIE T&D's submission was based on an actuarial assessment of the contributions required to fund ongoing costs and a total pension scheme deficit of £150 million which took account of changes in funding position since the last formal valuation date (31 March 2011). The company proposed that the deficit should be recovered over 11 years. NIE T&D assumed that consumers would fund the entire pension scheme deficit.

7.3 We commissioned both actuarial and regulatory expertise to aid our analysis of NIE T&D's pension costs during RP5. We reviewed recent regulatory precedent and adopted a set of pension principles.

### **Draft determination – pensions**

7.4 In our draft determination, we proposed that consumers should fund the unavoidable and efficiently incurred costs of the pension scheme that related to the regulated company, NIE T&D, only. Our proposals allowed for £10.5 million of ongoing costs, which aligned with NIE T&D's submission.

7.5 We reviewed the most recent actuarial valuation report, dated 31 March 2011 for the NIE Pension Scheme (NIEPS) which reported a total deficit of £87.6 million. We undertook a detailed analysis to investigate how much of that deficit could have been avoided.

7.6 Our analysis concluded that the NIEPS deficit amount of £87.6 million at 31 March 2011 is £33.4 million higher than it would have been had the net effect of actions that we classed as legally avoidable or inefficient had not occurred. We proposed therefore that this amount be recovered from consumers over a period of 15 years of which £12.5 million should be recovered during the five years of RP5.

## Responses to draft determination

7.7 Of the 32 responses that we received, eight commented on the proposed pension allowance. A number of stakeholders also discussed pension issues at the workshops that we held during the consultation period.

## Final determination

7.8 Due to the nature of pension deficit recovery costs and the dependency on triennial formal actuarial valuations, we have decided to treat these costs differently from other opex. Consistent with our pension principles, we will re-determine deficit recovery costs on the basis of the deficit at each triennial formal valuation. We expect the next formal valuation to be on 31 March 2014. However, given the recent volatility in valuations, if we consider it appropriate and with adequate notice, we may ask NIE T&D to bring this valuation forward by 12 months. Any actuarial information that we receive from NIE T&D will be subject to robust review.

7.9 This means that the pension revenue to be collected via the annual tariff process will be adjusted<sup>15</sup> from October 2015 onwards (at the latest) to reflect the level of pension deficit stated in the next formal valuation. This approach further reduces the cash flow risk to NIE T&D, and maintains consumer tariffs more in line with current costs.

7.10 Although one of our pension principles is that deficits will be based on the most recent formal actuarial valuation, we have decided to take into account changes in the deficit position as the deficit since 31 March 2011 has increased. This is a one-off action in order to reduce the potential tariff volatility in October 2015 and to take account of NIE T&D's current funding agreement with the pension trustees.

7.11 For the RP5 final determination we will base allowances on the deficit amount quoted at 31 March 2012. This amount is £156.4 million<sup>16</sup>.

7.12 In our draft determination, we attributed 79% of the deficit to the regulated company. Following consideration of stakeholder responses and a further

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<sup>15</sup> Any adjustments made, or truing-up/-down of figures, will be done on an NPV-neutral basis.

<sup>16</sup> We commissioned the Government Actuary's Department (GAD) to review the reasonableness of the assumptions used for the 31 March 2012 update. The GAD concluded that the changes in financial assumptions between 31 March 2011 (the results used in our draft determination) and 31 March 2012 are reasonable overall, reflecting the pension scheme's statement of funding principles and material reductions in gilt yields (which are used to derive the discount rates used to value the liabilities).

consideration of the regulatory treatment of similar circumstances, we have decided to apply a different treatment in our final determination. We will attribute 99.26% of the pension scheme deficit to NIE T&D<sup>17</sup>. This new option is chosen on the basis that NIE Powerteam Ltd provides services exclusively for the T&D business and ultimately charges its pension costs through to NIE T&D via its charge-out rates. Ofgem used this approach for United Utilities, an associated service company, because 100% of the service company's activities were carried out for the regulated business. We regard this as a strong regulatory precedent. On the basis of this regulatory fraction, and the informal valuation as at 31 March 2012, the amount of scheme deficit that is applicable to NIE T&D is £155.1 million.

7.13 Having considered the responses received, for our final determination we will ignore the effect of any historical legally avoidable actions apart from costs arising from early retirements. We will also ignore the effect of special or extra contributions that the company had paid.

7.14 A number of respondents commented on our approach to historical adjustments to the deficit related to the avoidable deficit costs. We have reviewed our approach to this. To be consistent with RP4 and with GB regulatory precedent, we have decided to only make an adjustment associated with early retirement deficiency contributions. When combined with the change to the deficit attributable to NIE T&D, the amount to be recovered during RP5 is £43.7 million. This will be updated based on the results of the next formal valuation.

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<sup>17</sup> A small proportion of the overall pension scheme deficit is attributable to other unregulated participating employers. Their proportion has therefore been excluded from the fraction.

**Table 7.1 : Final determination for pensions compared with NIE T&D's submission**

<i>2009-10 prices</i>	NIE T&D submission	Draft determination	Final determination (5 years)	Final determination (4 yrs 9 mths)
Total scheme deficit	£150m	£87.6m	£156.4m	£156.4m
Regulated fraction	100%	79%	99.26%	99.26%
Deficit recovery period	11 years	15 years	15 years	15 years
Deficit considered for NIE T&D	£150m	£69.2m	£155.2m	£155.2m
<b>Deficit recovery in RP5</b>	<b>£66.7m</b>	<b>£24.3m</b>	<b>£63.1m</b>	<b>£58.4m</b>
<b>Adjustments:</b>				
Actuals vs allowance (incl. effect of contribution holiday in RP2)	0	+£26m	No adjustment	No adjustment
Special contributions made by the company	0	+£65m	No adjustment	No adjustment
Benefit improvements	0	-£72m	No adjustment	No adjustment
Early retirements	0	-£53m	-£42.3m <u>+£1.1m</u> -£41.2m	-£42.3m <u>+£1.1m</u> -£41.2m
<b>Adjustment in RP5</b>	<b>£0m</b>	<b>-£12.5m</b>	<b>-£15.2m</b>	<b>-£14.7m</b>
<b>NET DEFICIT RECOVERY IN RP5</b>	<b>£66.7m</b>	<b>£11.8m</b>	<b>£47.9m</b>	<b>£43.7m</b>
<b>Ongoing costs</b>	<b>£10.5m</b>	<b>£10.5m</b>	<b>£10.5m</b>	<b>£10.0m</b>

## 8 TREATMENT OF CONNECTIONS

- 8.1 As part of the RP5 process, we consulted<sup>18</sup> on the distribution connection policy and audited NIE T&D's approach to pricing connection offers. As a result, we have instructed NIE T&D to remove the 40% subsidy for domestic connections from the statement of charges for connection to the Northern Ireland distribution system<sup>19</sup>. Any connection applications received in full after 1 October 2012 will be processed under the new rules.
- 8.2 We have worked with NIE T&D to ensure that its connection charging statement for distribution provides an appropriate level of information. The updated statement of charges was published in September 2012.

## 9 INCENTIVES

- 9.1 The overall purpose of incentives is to encourage NIE T&D to maintain and develop the network efficiently whilst delivering the outputs identified earlier. The RPI-X framework by itself incentivises NIE T&D to deliver efficiencies.
- 9.2 Of the 32 responses we received to our draft determination, seven made specific references to incentives. All respondents supported the principle of incentives, although many suggested alternatives to the proposed incentive structure. Many respondents said that they preferred a greater focus on outputs rather than inputs; these respondents considered the role of incentives to be limited.
- 9.3 Having considered NIE T&D's submission, we will exclude planned outages and transmission outages from the network performance incentives for customer interruptions and customer minutes lost during RP5. As stated in Chapter 5, we intend to consult on the criteria for "exceptional weather events". Any supply interruptions that meet these criteria will also be excluded from the network performance incentives. We intend to consider the inclusion of planned outages in the future, particularly for RP6.

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[http://www.uregni.gov.uk/uploads/publications/Consultation\\_on\\_Electricity\\_Connections\\_to\\_the\\_NI\\_Dist\\_System\\_Vfinal.pdf](http://www.uregni.gov.uk/uploads/publications/Consultation_on_Electricity_Connections_to_the_NI_Dist_System_Vfinal.pdf)

<sup>19</sup> [http://www.uregni.gov.uk/publications/decision\\_paper\\_on\\_electricity\\_connection\\_policy\\_april\\_2012](http://www.uregni.gov.uk/publications/decision_paper_on_electricity_connection_policy_april_2012)

- 9.4 Other more specific network performance incentives will be structured as a symmetrical incentive. This will feature a range within which the customer minutes lost (CML) may fluctuate without penalty or reward. This range, or 'dead band', will provide flexibility for NIE T&D, permitting the company to achieve targets while allowing for any 'natural fluctuations' that may occur. We will use a development of our draft determination proposal to apply an incentive to variances that are greater than 10% from the target CML.
- 9.5 In the event that CML goes beyond the specified range we will use the same rate as agreed by Ofgem for SSE Hydro rate, as it is the most comparable company. As outlined in our draft determination, this incentive penalty/reward is £0.18 million per CML outside of the +/- 10% threshold.
- 9.6 We will use a similar approach as the CML incentive for the incentive for customer interruptions (CI). A specified target number of CI will have a dead band range of +/- 10%. For each CI above or below the upper or lower limits, a penalty or reward of £0.03 million will apply, as we proposed in our draft determination.
- 9.7 In the draft determination we proposed introducing new standards in relation to connections, worst served customers and queries. After considering further evidence on the time required and cost to introduce the standards we proposed in the draft determination, they will not be introduced at present. We will consider their development further during the RP5 period.
- 9.8 Our draft determination noted that the revenue protection unit service has provided a net benefit for consumers during RP4. We believe that this work should be resourced to ensure that illegal extraction is kept to a minimum. We have decided that it should continue in RP5 on the same basis as it did in RP4, that is, any recovered amount will be shared 50:50 between NIE T&D and consumers. We will require regular reporting of this area during RP5.
- 9.9 We are keen to introduce new incentives, such as a distribution loss incentive and health and load indices. However to do so we need detailed measurements and base line information. We encourage NIE T&D to develop these areas during the RP5 period so that we are in a position to consider additional incentives later in RP5 or in RP6.
- 9.10 In relation to these new incentives we will consider an incentive of up to £1 million over the final two years of RP5 in relation to distribution losses. We will identify the incentive formula once we have reliable baseline data. This will

require consultation prior to implementation. A licence modification will be required to implement this incentive.

## 10 INNOVATION

10.1 Three formal innovation schemes were put in place during RP4. These were:

- the Sustainable Management of Assets and Renewable Technologies (SMART) Programme,
- the Vulnerable Customer Programme, and
- the Sustainable Networks Programme.

10.2 NIE T&D reported annually to us on each of these. We assessed the schemes operating in RP4 and have determined that they should not be continued into RP5.

10.3 In RP5, NIE T&D is seeking £14.9 million to fund smart technology:

- £2.5 million for the Research and Development Programme,
- £6.0 million for trialling smart technology projects,
- £3.3 million for applying advanced condition monitoring to network assets, and
- £3.1 million for upgrading the distribution network management system to facilitate smart grids.

10.4 Of the 32 responses received, six included specific references to our innovation proposals.

10.5 In our final determination, we have assessed NIE T&D's request for innovation capex to the same standards as business as usual capex. We have allowed funding for online monitoring for transmission transformers under Fund 1.

10.6 We recognise the need for further investment in these areas, particularly with the synergy between control systems for smart grids and smart meters. However, we do not consider NIE T&D's plans to be sufficiently developed at this stage to allow funding. We have therefore moved this to capex Fund 3, to provide NIE T&D with opportunity to develop this further.



10.7 We have not introduced a scheme similar to the Low Carbon Network Fund (LCNF) that Ofgem uses. We expect NIE T&D to be fast followers. We believe that our approach to considering innovation under capex Fund 3 allows NIE T&D to consider innovative solutions and to use third party expertise where appropriate.

## **11 ENVIRONMENT AND SAFETY**

11.1 As part of the review of NIE T&D for RP5, we have assessed the standards of performance and reporting associated with environmental and safety issues. Based on this assessment, we will require more reporting on these issues in RP5. We will develop the requirements and templates as part of the overall annual reporting requirements.

## **12 THE WEIGHTED AVERAGE COST OF CAPITAL**

12.1 In its submission, NIE T&D proposed a framework for calculating the WACC. NIE T&D's report concludes that it would be appropriate to use a vanilla WACC (real) of 5.34%, made up of:

- a post-tax cost of equity of 7.7% real (in line with the average which Ofgem allowed at DPCR5);
- a pre-tax cost of debt of 3.6% real; and
- an adjusted level of gearing for NIE T&D of 57.5%.

12.2 We commissioned First Economics to recommend an appropriate WACC for RP5. First Economics deliberately sought to estimate the cost of capital independently from NIE T&D's current ownership arrangements. The reason for doing so was to ensure that the return on offer through the price control would be capable of supporting any efficient investor.

- 12.3 We asked First Economics to assess the cost of capital for the separate transmission and distribution elements of the business. It concluded that the same range of values could be applied to both.
- 12.4 In our draft determination, we proposed a WACC of 4.45% for conventional capex and 4.0% for Fund 3, as these investments are exposed to lower systematic risks.
- 12.5 Of the 32 responses that we received, seven commented on the WACC.
- 12.6 We have reviewed our bottom-up assessment of the WACC that we proposed in the draft determination and taken account of stakeholder responses. The cost of debt, gearing and cost of equity have been updated since our draft determination.

### **Cost of debt**

- 12.7 We do not see any reason to move from the approach detailed in the draft determination for the cost of debt, and intend to follow the Competition Commission's approach for the final determination.
- 12.8 The nominal cost of debt within our WACC lies above current secondary yields for both A and BBB rated debt. The Iboxx corporate non-financial 10-year maturity series for A and BBB rated bonds shows that the yield on utility bonds has fallen steadily since the end of 2009. We therefore expect that NIE T&D should be able to raise any new debt required in RP5 at or below its embedded cost of debt.
- 12.9 We have updated the cost of debt to take account of updated inflation figures based on HM Treasury's latest forecast.
- 12.10 The real cost of debt that we are using in the WACC calculation is 3.39%. This has been converted from a nominal weighted average cost of debt of 6.65%<sup>20</sup> using the formula:  $(1 + \text{real cost of debt}) = (1 + \text{nominal cost of debt}) / (1 + \text{forecast inflation})$ <sup>21</sup>.

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<sup>20</sup> See RP5 Draft Determination, April 2012 (page 168).

<sup>21</sup>  $(1+6.65\%)/(1+3.15\%) = 3.39\%$

## Gearing

- 12.11 In our draft determination we stated that we considered that a 60% gearing level for both the transmission and distribution networks should apply. However, there was an internal inconsistency in our WACC calculation.
- 12.12 The assumed gearing figure in the WACC should be in line with the equivalent figure in the modelling of NIE T&D's financeability, at least at the start of the control period. If this is not the case there is the risk of a logical inconsistency between the financeability assessment and the setting of charges in the price control.
- 12.13 In developing an assumption for gearing to use in our modelling we have adopted a figure that is closer to NIE T&D's actual gearing figure at the start of RP5. We also consider that a lower level of gearing is more appropriate during a growth phase and when there is some investment uncertainty (timing and quantum) associated with funds 2 and 3. We consider that this level of should allow NIE T&D to maintain a solid investment-grade credit rating.
- 12.14 The gearing level to be applied in the final determination is 50%.

## Cost of equity

- 12.15 NIE T&D has argued that our proposed cost of capital compares unfavourably with the expected return under Ofgem's price controls. One of its contentions is that Ofgem deliberately provides GB network companies with additional return outside of the headline WACC calculation. It would be very difficult for us to explain why we should match revenues that GB companies have earned from good behaviour under a mechanism that is not in place in Northern Ireland. We therefore consider that we should set the right allowed return for NIE T&D based on its risk profile, regardless of whether this turns out to be higher or lower than the WACCs that Ofgem uses.
- 12.16 We have reviewed our equity risk premium and have increased it to 5.0% for this final determination. We do not propose to change the asset beta of 0.42.
- 12.17 Based on these parameters and a gearing of 50%, the cost of equity (post-tax real) is 5.70%.

### Fund 3 WACC

12.18 Our view is that we have structured Fund 3 projects in such a way as to reduce the systematic risk in comparison with Fund 1 or Fund 2 investments. We accept that this is a novel approach and it may be more appropriate to experience the process for Fund 3 in practice before considering a different WACC for these investments. We have therefore decided to allow the same rate of return on renewables-driven investments and NIE T&D's transmission and distribution assets.

### RP5 WACC

12.19 Table 12.1 shows the WACC for RP5. It should be noted that the equity beta and therefore the post-tax cost of equity value are lower than the draft determination figures as a result of the change in gearing.

**Table 12.1: RP5 WACC**

	RP4	NIE T&D's submission	NIE T&D's response to draft determination	Draft determination	Final determination
Gearing (%)	65.0%	57.5%	60.0%	60.0%	50.0%
Pre-tax cost of debt (%)	3.6	3.6	4.3	3.2	3.39
Risk-free rate (%)				2.0	2.0
Equity risk premium				4.8	5.0
Debt beta				0.1	0.1
Asset beta				0.42	0.42
Equity beta				0.90	0.74
Post-tax cost of equity (%)	6.7	7.7	7.7	6.32	5.70
<b>Vanilla WACC (real) (%)</b>	<b>4.69</b>	<b>5.34</b>	<b>5.7</b>	<b>4.45</b>	<b>4.55</b>

12.20 The vanilla WACC (real) to be applied in RP5 is 4.55%.

### **13 DEPRECIATION AND RAB STRUCTURE**

13.1 We have reviewed the depreciation profile and structure of the RAB for RP5. We also completed a review of how NIE T&D treats assets that it has disposed of in its regulatory accounts. In our draft determination we said that we were minded to leave depreciation periods and the depreciation type for RP5 the same as it had been in RP4, with the exception of the market opening RABs. The core RAB will be divided into separate RABs for transmission and distribution.

13.2 We do not propose any change to this as a result of our consultation.

### **14 FINANCEABILITY**

14.1 In our draft determination we summarised our position on NIE T&D's financeability by stating that the company could finance its base case activities without the need for new equity or the need to retain dividends. We also pointed out that the company faced certain challenges. These included the large programme of new investment in relation to renewables and interconnection as well as the potential short-term additions to the pension fund over and above the regulatory allowance. We considered that to meet these challenges the company would inevitably need to retain dividends and/or inject fresh debt and equity.

14.2 We considered all of the responses to our draft determination carefully, and have adjusted our approach in light of this feedback.

14.3 Over the course of the consultation period we met Fitch, Moody's, and Standard and Poor's ratings agencies to discuss our draft proposals and our

financial modelling. In our final decisions we have taken into consideration the approach and views of the ratings agencies.. We have also expanded our analysis to include additional functionality to stress test our assumptions.

- 14.4 Our analyses are based on a target credit rating of BBB+ to A-. In our final determination we have differentiated between cash requirements that result from licence obligations such as development and maintenance of the network and other cash requirements such as those arising from the change in capitalisation practice.
- 14.5 We initially assessed NIE T&D's financeability on a 'base case'. We define the base case as business as usual for the company<sup>22</sup>. Our modelling highlights the financing challenge for the business given its debt obligations and the cost of that debt. We note that Fitch has suggested a PMICR<sup>23</sup> value of 1.4 in relation to NIE T&D. We regard 1.4 as an acceptable level but regard 1.5 to be a more desirable benchmark.
- 14.6 The PMICR for the base case is detailed in Figure 14.1 below.
- 14.7 The graph demonstrates that during the RP5 period NIE T&D is at or above the 1.4 level highlighted by Fitch for most of the RP5 period. We do not consider this level of PMICR coverage to be ideal. However, we note the impact of the 'real/nominal mismatch' which is affecting the ratio that measures real return over the nominal interest costs.
- 14.8 The 'real/nominal mismatch' becomes a bigger issue during periods of higher inflation. Inflation is remunerated to the company by increasing the RAB value each year and hence the effect is spread over a long period of time. The company obtains a real return on the inflated RAB value each year. On the other hand the company must pay for interest costs on a nominal basis. The PMICR ratio is calculated using real income divided by nominal interest costs – hence the mismatch<sup>24</sup>.
- 14.9 We propose to correct for this timing issue by moving revenues from the next price control (RP6) into this price control (RP5) in an NPV neutral manner, such that there is no transfer of value from consumers to the company. Our

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<sup>22</sup> In the base case, we assume that NIE T&D spend their full allowances for Capex (fund 1 and 2), opex and pensions. We do not assume an out performance

<sup>23</sup> Post Maintenance Interest Cover Ratio

<sup>24</sup> Please refer to publications in 2006 and 2010 by First Economics on the real/nominal mismatch.

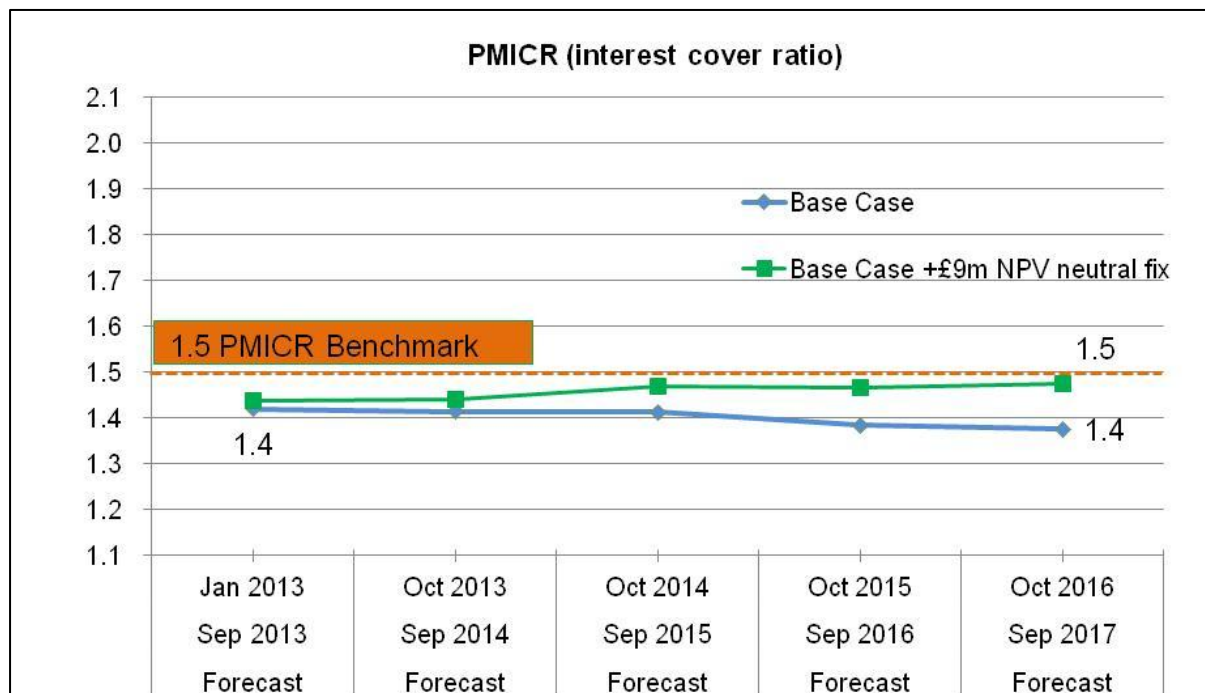
<http://www.first-economics.com/financeability2.pdf>

<http://www.first-economics.com/financeability2010.pdf>

modelling shows that the inclusion of £9 million of ‘financeability revenue’ would sufficiently improve the PMICR.

14.10 The PMICR after this fix is included in the company revenues is detailed in Figure 14.1 below. We refer to this scenario as ‘base case + £9 million NPV neutral fix’.

**Figure 14.1 – PMICR for RP5 base case and with NPV neutral adjustment**



14.11 We have also modelled the impact of the company spending £223 million on Fund 3 during RP5. In these scenarios NIE T&D can provide the necessary equity for Fund 3 from dividend retention.

14.12 Although we consider it to be unlikely, if the scenario arose where the company needs to raise new equity, we would regard it as reasonable to consider the efficient costs<sup>25</sup> of raising equity as a recoverable cost. If this situation were to arise we would expect detailed discussions with NIE T&D and scrutiny before approval of the costs<sup>26</sup>.

14.13 As noted above we considered separately the impact of adjustments which we believe could have been avoided by the company. We consider that any

<sup>25</sup> For example Ofgem and Ofwat allow for transaction costs of 5% on raising new equity.

<sup>26</sup> For example the raising of new equity to support the growth of the company, should be in line with the notional gearing in their WACC, ie 50% equity.

cash requirements resulting from the change in capitalisation practice, and our subsequent RAB correction, are a matter for the company. We do not consider that this will be material however given that the RAB is depreciated over 40 years. We also consider that any remaining mismatch between pension allowances and the funding schedule agreed with the pension trustees is also a matter for the company. However, we expect that this mismatch should now be significantly reduced with our final determination on pension costs.

## 15 REVENUE ENTITLEMENT

15.1 The revenue that NIE T&D would have received based on its submission is £1.11 billion over four years and nine months. For the same period, our final determination allows for £0.92 billion.

15.2 When the estimated expenditure on renewables and interconnection are included (Fund 3 capex), the NIE T&D submission increases to £1.17 billion, The equivalent revenue based on our final determination is £0.96 billion. This is shown in Table 15.1.

15.3 We have used the cost apportionment provided by NIE T&D to split the costs in the categories above across transmission and distribution. As a result the tariffs in RP5 should be fully cost-reflective.

**Table 15.1: Our RP5 revenue decision**

Revenue block\financial year	2012-13 <sup>27</sup>	2013-14	2014-15	2015-16	2016-17
<b>Without interconnection and renewables</b>					
NIE T&D	£164m	£223m	£229m	£240m	£252m
Our proposals	£152m	£200m	£186m	£191m	£191m
<b>With interconnection and renewables</b>					
NIE T&D	£169m	£232m	£240m	£254m	£273m
Our proposals	£153m	£204m	£193m	£202m	£206m

<sup>27</sup> This is for nine months from 1 January 2013 to 30 September 2013.



## 16 IMPACT ON ELECTRICITY TARIFFS

- 16.1 Following publication of our draft determination, NIE T&D reworked our analysis of the impact that our proposals would have on tariffs. The company used its more detailed tariff model and actual metered data for this analysis. It also highlighted an error in our model concerning the amount of revenue that was being collected from customers. The revenue collected through TUoS<sup>28</sup> in tariff year October 2011 – September 2012 was reduced by 7% as SONI had an over-recovery in the previous year.
- 16.2 We have updated our analysis based on the information that NIE T&D provided. In our final determination we are reallocating the costs associated with obsolete retail market IT systems from the PSO into the DUoS tariff and accelerating depreciation. This will reduce the PSO levy in future years. To ensure a like for like comparison between base year tariffs and future tariffs we have added in the portion of the PSO levy that was associated with those systems into our base year costs<sup>29</sup>.
- 16.3 Table 16.1 shows the impact that NIE T&D's proposals would have had on the network charges paid for by a selection of customer types. The average domestic bill would have increased by £106 in total over five years, excluding RPI inflation, and before network expansion for renewables and interconnection.
- 16.4 The impact of our final determination is shown in Table 16.2. This shows that, excluding RPI inflation and before network expansion for renewable generation, network charges should remain relatively flat over RP5<sup>30</sup>.
- 16.5 The current best estimate of investment on renewables and interconnection would result in a further increase of £18 on the average domestic bill over the five years.
- 16.6 For large energy users, the impact is much greater due to the fact that the majority of the investment for renewables and interconnection is on the transmission network. Therefore, customers in the category 'Half hourly

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<sup>28</sup> Transmission Use of System Tariff

<sup>29</sup> See a description of the various tariffs:

[http://www.uregni.gov.uk/uploads/publications/October\\_2012\\_Draft\\_Retail\\_Tariff\\_Background\\_Briefing.pdf](http://www.uregni.gov.uk/uploads/publications/October_2012_Draft_Retail_Tariff_Background_Briefing.pdf)

<sup>30</sup> The domestic customer type is based on 4041 kWh per year) and the Half hourly metered EHV customer is based on 27 GWh per year connected at 33kV. Comparisons of electricity costs across Europe are based on a standard consumption by domestic customers of 3300 kWh per year. The values should therefore be adjusted accordingly if they are to be used in such a comparison.

metered EHV' could see their network charges increase by £55,892 over the RP5 period.

- 16.7 In the case of domestic consumers, the network charges make up in the region of 20% of electricity bills.
- 16.8 In summary, our proposals would result in little change over the five years of RP5 on the network charges paid by consumers. It is important to remember that these figures all exclude RPI inflation, which is applied to NIE T&D's allowed revenue each year.

**Table 16.1: Impact of NIE T&D request on network charges (excluding renewables and interconnection)**

Customer Type	Current Average Cost	Annual Cost for Average Use (TUoS + DUoS)					Total Cost over 5 years
		Dec-13	13/14	14/15	15/16	16/17	
Domestic	132	146	146	152	159	165	106
Small Business (Quarterly Billing)	497	548	549	571	599	619	399
Half hourly Metered MV	1,107	1,220	1,222	1,271	1,333	1,376	889
Half hourly Metered MV	7,652	8,436	8,451	8,791	9,217	9,513	6,149
Halfhourly Metered HV	39,163	42,912	43,127	44,895	47,064	48,804	30,988
Halfhourly Metered EHV	124,927	135,408	136,866	142,668	149,524	156,312	96,142

**Table 16.2: Impact of our proposals on network charges (excluding renewables and interconnection)**

Customer Type	Current Average Cost	Annual Cost for Average Use (TUoS + DUoS)					Total Cost over 5 years	
		Dec-13	13/14	14/15	15/16	16/17		
Domestic	132	141	136	126	129	129	-	1
Small Business	497	529	510	473	485	485	-	5
Half hourly Metered MV <70kVA	1,107	1,179	1,137	1,052	1,080	1,078	-	9
Half hourly Metered MV	7,652	8,157	7,862	7,272	7,465	7,448	-	55
Halfhourly Metered HV	39,163	41,137	39,841	37,248	38,258	38,343	-	987
Halfhourly Metered EHV	124,927	127,808	124,867	118,984	122,322	123,560	-	7,095

**Table 16.3: Potential impact of investment in renewable integration and interconnection**

	Potential additional cost of investment for renewables and interconnection over 5 years <sup>31</sup>
Domestic	£18
Small business (quarterly billing)	£66
Half hourly metered MV <70kVA	£136
Half hourly metered MV	£895
Half hourly metered HV	£9,274
Half hourly metered EHV	£55,892

<sup>31</sup> This is based on NIE T&D's latest estimate for RP5. Please note that the cost of capital investment is recovered over 40 years, therefore the impact of renewables investment will continue to increase during RP6 and the total cost will be considerably higher if all of the expected network capacity is required. Most of the increase is seen in the TUoS tariffs in the final two years of RP5.

## **17 ANNUAL REPORTING**

17.1 As highlighted earlier, we intend to introduce a Reporter for RP5. The aim for RP5 is to standardise the reporting in order to:

- allow NIE T&D to collate and process the required information in an efficient and pro-active manner;
- ensure that we have all of the information required to monitor progress during RP5;
- ensure that the information is provided in the right format in a timely manner; and
- facilitate the Reporter's verification processes.
- Reduce work for future price controls

17.2 The reporting will cover a range of areas. We propose to develop a coherent set of annual report templates for NIE T&D to complete. These will provide us with the level of detail we need to fully discharge our statutory duties while minimising the reporting burden on NIE T&D. We will develop the relevant requirements and templates as part of the company's overall annual reporting requirements.

## **18 LICENCE MODIFICATIONS**

18.1 The proposed modifications to NIE T&D's licence required to implement RP5 are published along with this document. As expected, modifications have centred on Annex 2 with a smaller number of consequential changes to the main body of the licence.

18.2 We have added one new condition in relation to the function of the reporter.

18.3 A formal consultation period is required for the proposed modifications by Article 14 of the Electricity (Northern Ireland) Order 1992. This notice is published on our website. This "Article 14 notice" details the proposed modifications that will put the final determination for the RP5 price control into action. It also gives details of how any interested persons can respond to the consultation, and the deadline for responses to be received.