31st July 2019

nationalgridESO

National Grid ESO RFPR submission narrative – 2018/19

Introduction

This narrative supports the submission of the Regulatory Financial Performance Reporting (RFPR) pack for the National Grid Electricity System Operator (ESO).

As per the RFPR Regulatory Instructions and Guidance (RIGs)[1], the following sections are not required for input and thus have not been published or commented on within this narrative.

- RORE
- Innovation
- Financing - The SO element is an allocation of TO net debt and financing cost and is reported in the TO RFPR.
- Net Debt - The SO element is an allocation of TO net debt and financing cost and is reported in the TO RFPR.
- Dividends

Revenue

(2018/19 Price base)

Maximum SO internal revenue for 2018/19 has increased by £28.8m to £193.2m compared to 2017/18. With the inclusion of forecast incentives, the Allowed Network Revenue for NGESO is £211.65[2]. This increase in internal revenue is primarily due to increase in SOMOD, comprising key components as follows:

- Increased Legacy Revenue and RAV terms
- Total Impact of Totex
- Mid Period Review (MPR) outcome resulted in increased allowances for ESO to deliver Supplemental Balancing Reserve (SBR) and Demand Side Balancing Reserve (DSBR) balancing products and new Integrated Transmission Planning and Regulation (ITPR) roles.

Totex Performance

(2018/19 Price base)

The below narrative is in line with the ESO Cost & Outputs RRP narrative and is in 2018/19 prices, so values will differ to 09/10 values included within the RFPR tables.

Our overall total expenditure forecast for the RIIO T1 period is £1,408m against forecast allowances of £1,401m. Total spend is £7m higher than our RRP submission last year.

Spend in 2018/19 is £5m below prior forecast, with year on year additional investment of £14m driven by the CNI data centre programme and IT investment associated with European Network

[1] https://www.ofgem.gov.uk/system/files/docs/2019/04/rfpr_guidance-decision_2.pdf

[2] The 2019 incentive value has been input based on average historic performance of BSIS scheme, explained further in Output Incentive Section below.

codes. Opex spend increased compared to 2017/18 by £19m with £12m of this due to work required for legal separation of the ESO. There were also £11m increased costs in 2018/19 associated with a multi-year cost efficiency and restructuring programme covering a range of initiatives to drive further efficiency and lower costs for customers. This has already started delivering Opex efficiencies and an organisation well positioned to take on an expanded role in the future.

Further investment in the remaining years of RIIO T1 of £130m will deliver new CNI data centres, IT systems which are compliant with EU regulations and continue to invest in capabilities to deliver on our forward plan commitments. Our Opex costs are forecast to decrease over the next two years as the legal separation work is completed and we continue to deliver savings following our restructuring programme.

Total expenditure for the full 8-year period is expected to be £7m higher than allowances.

Totex Assumptions and enduring value adjustments

The overarching principle of enduring value adjustments is to recognise performance that relates to the T1 period. For uncertainty mechanism allowances that are volume driven, this means only recognising performance in T1 for outputs that have been delivered in T1.

Totex

1. The following assumptions are made within the Cost and Outputs (C&O) RRP submission and included in the allowances row headed 'Totex allowance including allowed adjustments and uncertainty mechanisms'. These are also included in the November 2018 PCFM:
    a. Re-opener allowances are set as per the May 2018 reopener decisions.
    b. NGET (SO) legal separation allowances are set as per the August 2018 decision.
2. Re-phasing
    a. We re-phase allowances compared to those in the PCFM. This better matches allowances to the level of incurred or forecasted expenditure, providing a more accurate view of in-year performance. We have presented the impact of the re-phasing allowances as a single line on the R4 totex tab. This is appropriate as re-phasing does not affect the overall level of allowances recognised over the RIIO-T1 period, thus does not materially impact the RoRE (R4 totex enduring value adjustment a).
3. Enduring Value
    a. Allowances for additional funding requested on 31st May 2019 for Electricity Market Reform are included per the reopener submission (R4 totex enduring value adjustment b). These were also included within the Cost and Outputs (C&O) RRP submission.

Output incentive Performance

Forecast output incentives are assumed to be an average of the actual earned incentives in T1 to date. In the case of the new ESO incentive that has replaced the previous balancing services (BSIS) incentive, we have applied the historic average BSIS performance to the new incentive for future years as well as 2019 whilst we wait for direction from Ofgem.

RAV

(2018/19 Price base)

The RAV table utilises the PCFM published in November 2018 to calculate the adjusted RAV balances.

The RAV for net additions (after disposals) is based on the November 2018 PCFM. The enduring value adjustment row reflects the additional EMR funding and re-phasing adjustments noted above.

The closing RAV in 2021 has reduced from 227.5m in RFPR18 to 223.5m in RFPR19.

Tax

(2009/10 Price base)

Forecast tax performance for 2019 is £2.8m (£5.3m actual for 2018).

Ignoring the impact of financing performance, residual tax performance continues to be minimal. This is in line with our expectations, and deviations are primarily a result of the 'dead-band' benefit received on lower corporation tax rates, partially offset by forecasting variances, including capital allowance rate changes.

The allocation of the NGET tax attributable to TO and SO is in line with the allocations used within our underlying accounting systems and is reflected in the Statutory Accounts. There are no specific allocations made for the RFPR tables.

The forecast tax allowance is derived from the PCFM post enduring value adjustments.

Pensions

(2009/10 Price base)

Pension deficit payments were broadly in line with the prior years. The only notable change is the adjustment of (£0.2m) for the Pension Payment History Allowance (PPH), which is forecast for the remaining periods of T1. The pension scheme valuation is performed tri-annually, the valuation presented in the 2018/19 RFPR is therefore the same valuation as that presented for 2017/18

Data assurance statement

The RFPR submissions have been completed in line with the Ofgem Data Assurance Guidelines (DAG) process. This mandates a fully documented 2 level review process. The overall submission and regulatory judgments have been signed off at Director level.

Basis of any estimates and allocations

Where allocation between NGET (TO) and NGET (SO) has been required, this has been done on a RAV basis.