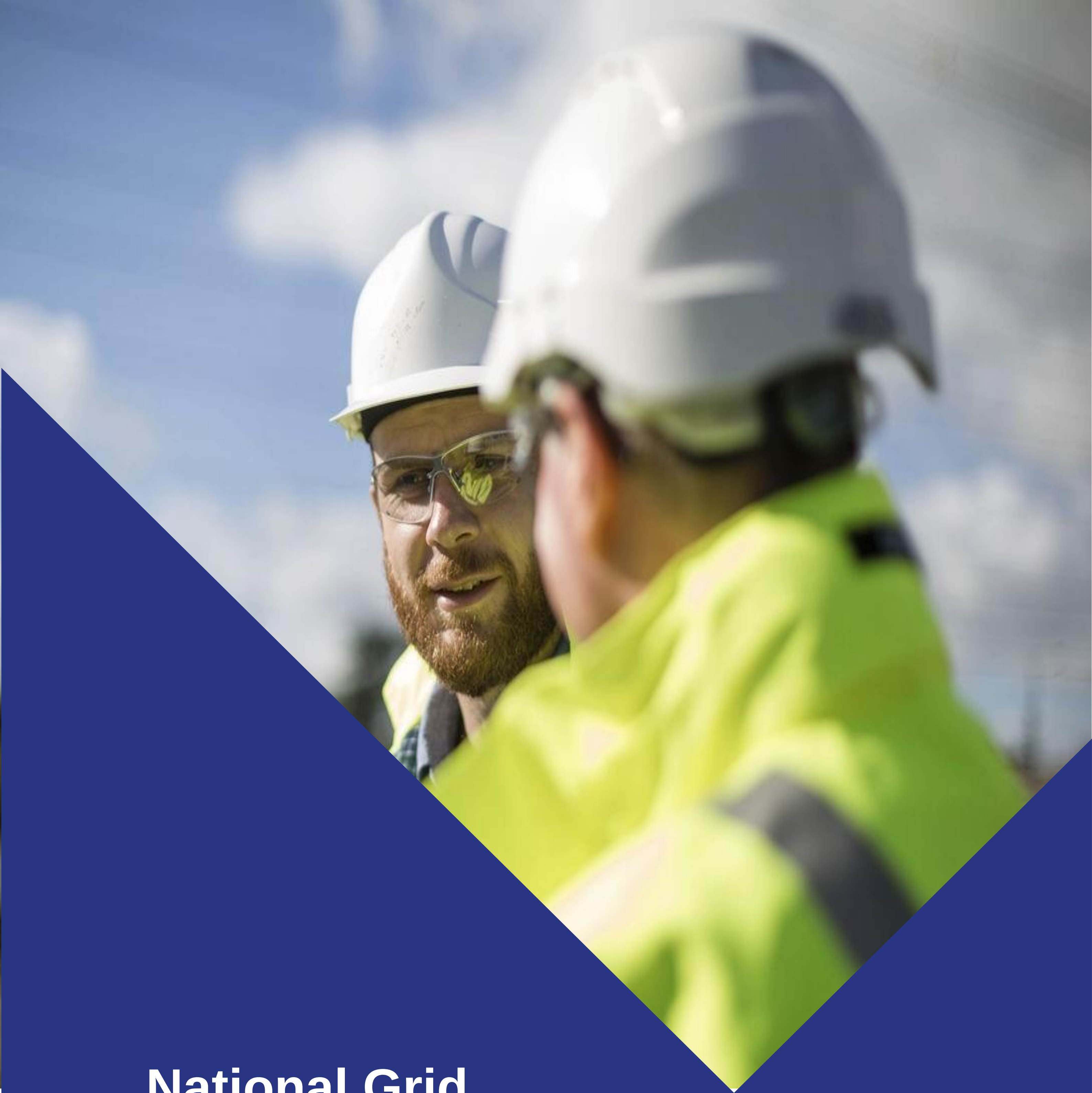


National Grid Electricity Transmission

Regulatory Financial Performance Report Narrative

August 2022

Contents

Executive Summary ... 3

Key Financial Performance Measures ... 5

Key Operational Performance Measures ... 5

Overview of Regulatory Performance ... 6

- **RoRE** ... 6
- **Reconciliation to Revenue and Profit** ... 7
- **Totex – Reconciliation** ... 8
  - **Totex performance** ... 8
  - **Reconciliation to Totex** ... 9
- **Incentives and Other Revenue** ... 10
  - **Incentives** ... 10
  - **Energy Not Supplied ODI** ... 10
  - **Insulation and Interruption Gas Emissions ODI** ... 11
  - **Timely Connections ODI** ... 11
  - **Quality of Connections Satisfaction Survey ODI** ... 11
  - **SO-TO Optimisation ODI** ... 12
  - **Environmental Scorecard ODI** ... 12
  - **RIIO-2 Network Innovation Allowance** ... 12
  - **Carry Over Network Innovation Allowance** ... 13
  - **Strategic Innovation Fund** ... 13
- **Financing and Net Debt position** ... 14
- **RAV** ... 15
- **Taxation and Tax Reconciliation** ... 15
- **Corporate Governance** ... 16
  - **Corporate Ownership and Governance Framework** ... 16
  - **Board of directors** ... 16
  - **Board committees** ... 16
  - **Executive Remuneration Policies** ... 18
  - **2021/2022 Executive Remuneration** ... 20
  - **CEO Pay Ratios** ... 20
- **Pensions and Other Activities** ... 21

Data Assurance Statement ... 21

- **Basis of any estimates and allocations** ... 21

Appendices ... 23

- **Appendix 1 - Enduring Value Adjustments** ... 23
- **Appendix 2 - Corporate Ownership Structure** ... 25

National Grid Electricity Transmission Regulatory Financial Performance Reporting narrative 2021/22

Executive Summary

This narrative supports the submission of our 2021/22 Regulatory Financial Performance Report (RFPR22) which is the first RFPR submission of the RIIO-2 price control period. RFPR22 sets out the regulatory information to meet the requirements of Standard Condition B15 of the National Grid Electricity Transmission licence.

RFPR22 summarises National Grid Electricity Transmission's (NGET's) operational and financial performance components of Return on Regulated Equity (RoRE) across the RIIO-2 period. RoRE is Ofgem's measure of the financial return achieved by shareholders in a licensee during a price control period. This narrative covers NGET's RORE performance across the price control period with focus on the 2021/22 performance delivered to date. Whilst RoRE reflects the financial performance achieved by shareholders, it does not reflect the consumer aspects of performance. Delivery of financial performance will also result in a financial benefit to consumers. Non-financial benefits to consumers such as improvements to safety and reliability are also not represented by Ofgem's performance measures.

The forecast and actual cost, volume and output data submitted via the Regulatory Reporting Pack (RRP22) inform the regulatory performance. However, RRP22 is unable to account for a number of adjustments required to give a true view of performance. As a result, there are a number of adjustments that are applied to the RRP22 for the purpose of RFPR22. These are detailed in the Totex – Reconciliation section of this narrative.

Our aim is to present a view of financial performance through the price control period that is consistent with our understanding of business performance. Performance under the RIIO-2 framework is achieved through delivery of outputs prioritised by consumers for lower cost than allowances and by exceeding output delivery incentive targets. This drives financial benefit to our stakeholders – to shareholders through return on investment and to current and future consumers through lower bills. NGET has previously communicated our ambition to the market to achieve 100bps of outperformance for the price control period. This reflects our ambition to perform well for our stakeholders under the RIIO-2 framework. The underlying forecasts for this ambition are aligned to the RRP submission. The difference between the 100bps communicated to investors and the 74bps shown in RoRE for the five years of the RIIO-2 period can be explained by the differences in the calculation of RoE and RoRE:

- -30bps totex performance – an element of allowance from RIIO-1 is deferred to RIIO-2 to align to delivery of the output. The RIIO-1 sharing factor has been applied to the related underspend in the derivation of RoE. We have not taken this approach for the calculation of RoRE as the RFPR input template does not have the functionality to apply a sharing factor which differs from that set under the RIIO-2 framework.
- -10bps unlicenced income – unlicenced income is excluded from RoRE in RIIO-2 by definition, however is included in our definition of RoE which is used for investor reporting.

- -5bps incentive performance - we have taken a prudent approach to forecasting incentive performance included in RoRE compared with the forecast used to derive RoE.
- +20bps legacy adjustment – within RoE an adjustment was applied in prior year performance which was not included in RRP21 due to the functionality of the tables. This performance flows through in FY23 RoRE instead.

It should be noted that, the overall performance and the forecasts in RRP22 are based on our forecast view as at 31st March 2022 and are subject to a number of uncertainties that could influence our performance over the remaining years of the RIIO-2 period.

RoRE is calculated using two methodologies; RoRE based using the notional gearing assumption of 55% and RoRE based on actual gearing.

Based on our cost and outputs forecasts, RoRE (including operational and financing performance) based on notional gearing is forecast at 7.1% for the 5 years of the RIIO-2 period, 2.8% above average Allowed Return on Equity. This performance stems from:

- 0.1% totex performance as the -0.4% RRP22 totex performance is increased by 0.5% as a result of our ongoing efficiency ambition.
- +0.8% as a result of Enduring Value Adjustments to show the impact on performance of projects crossing price control periods. These adjustments ensure that performance is only recognised when outputs are delivered.
- +2.1% of financing performance largely as a result of NGET's financing strategy, including choosing not to index a higher proportion of the debt book, and higher than expected inflation rates. This is partially offset by negative performance on RPI linked debt due to an increase in the RPI-CPIH wedge.
- -0.2% Business Plan Incentive.

The 2021/22 RoRE shows higher performance than the five-year average with 8.5% achieved in the first year of RIIO-2, 4.3% above average Allowed Return on Equity. RoRE in 2021/22 is in excess of the RIIO-2 average due to:

- + 1.2% of totex outperformance; largely driven by T1+2 allowances being recognised in 2021/22 as well as re-phasing of RIIO-1 non load allowances for projects that cross-price controls. This is higher than the RIIO-2 average as a result of T1+2 deferrals only being present in the first two years of RIIO-2.
- + 3.1% of financing performance for reasons noted above. This is higher than the RIIO-2 average as a result of inflationary impacts being at the highest in early years of RIIO-2.

RoRE performance based on actual gearing is broadly aligned to its notional comparator. Actual gearing has decreased slightly below notional at an average of 53.8% for the price control period and 53.4% for 2021/22. Gearing has fallen because we have maintained the level of dividend paid in line with previous years. The reduction in gearing will help provide capacity to finance high levels of capex investment in future years to achieve Net Zero. The level of dividend paid also anticipates a reducing notional gearing level for the purposes of the tax clawback mechanism in the outer years of RIIO-2. The difference between actual and notional gearing creates minimal variance between notional and actual performance; average actual performance for the period is slightly lower at 6.9% and 8.2% for 2021/22

This year's submission is the first year of the RIIO-2 price control and therefore there will be no comparison of 2021/22 RoRE and its component values to previous years.[1]

[1] RIIO-2 Regulatory Financial Performance Reporting – Regulatory Instructions and Guidance Version 1.0, Ofgem, 1st June 2022, para 1.16

Key Financial Performance Measures

The key financial performance measure within the RFPR22 submission is RoRE financial performance. The values quoted in this section focus on RoRE based on notional gearing of 55% unless otherwise stated.

NGET's RoRE financial performance across the period is forecast to outperform against regulatory cost of debt and tax allowances across the period by 2.1%, comprising 2.5% debt performance offset by -0.4% underperformance of actual vs regulatory tax. A major driver underpinning debt performance is the actual and forecast increase in inflation set against our strategic decision not to rely on high levels of index linked debt. This is partially offset by negative performance on RPI linked debt due to an increase in the RPI-CPIH wedge.

The main driver underpinning tax performance is largely as a result of lower actual debt costs resulting in a lower tax shield.

Financial performance in 2021/22 is 3.1%, comprising 3.7% debt performance offset by -0.6% tax underperformance. Performance in the early years of RIIO-2 is forecast to be higher than that in later years as a result of inflationary impacts being at the highest in early years of RIIO-2.

The financial RoRE values based on actual gearing are aligned to their notional equivalents. Actual gearing is slightly below the notional level of 55% at 53.8% for the period average and 53.4% for 2021/22.

Key Operational Performance Measures

(Financial values in 2018/2019 price base unless otherwise stated)

The key operational performance measure within the RFPR22 submission is RoRE operational performance. The values quoted in this section focus on RoRE based on notional gearing of 55% unless otherwise stated.

RoRE operational performance is based on actual data for 2021/22 (with the potential exception of totex allowances which may be phased over a period of years) and forecasts for 2022/23 onwards. Forecast data is based on our view as at 31 March 2022 and is subject to a number of uncertainties that could influence our performance over the remaining years of the RIIO-2 period.

RoRE operational performance is forecast at 5.0% for the RIIO-2 period, 0.7% above average Allowed Return on Equity comprising:

- 0.9% totex outperformance; and
- -0.2% under performance arising from the Business Plan Incentive adjustment of -£65m.

Totex outperformance of +0.9% for the RIIO-2 period is driven from:

- 0.1% totex performance as the -0.4% RRP22 totex performance - largely as a result of inflationary cost pressures and spend on delivery of outputs outside of the RIIO-2 price control, for example projects initiated in RIIO-1. This is increased by cost-saving initiatives and +0.5% as a result of our ongoing efficiency ambition. NGET has stated its ambition to continue to seek additional efficiency through improving and innovating its approach to operating, maintaining, replacing and extending its transmission network. There are a number of initiatives currently being developed and implemented. £500m has been included at a high level in our financial forecasts and is included in the Price Control Financial Model to ensure the benefit is passed to consumers in a timely manner.

- +0.8% as a result of Enduring Value Adjustments to show the impact on performance of projects crossing price control periods. These adjustments ensure that performance is only recognised when outputs are delivered. +0.3% as a result of deferral of allowances relating to load related projects initiated in RIIO-1 but completing in the first two years of RIIO-2. Associated allowances have been re-profiled for financial reporting purposes to recognise the performance when the output is delivered. +0.5% as a result of rephasing of allowances for non-load projects that cross price control periods. Allowances are rephased to ensure performance is recognised when the output is delivered.

The 2021/22 performance shows an operational performance of 1.1%, comprising:

- 1.2% totex outperformance; largely driven by T1+2 allowances being recognised in 2021/22 as well as re-phasing of RIIO-1 non load allowances for projects that cross-price controls.
- 0.1% non-totex incentive performance; and
- -0.2% under performance arising from the Business Plan Incentive adjustment of -£65m.

Operational performance in 2021/22 exceeds the RIIO-2 average due to higher totex outperformance. Increased spend forecast in the later years of RIIO-2 as projects are mobilised is expected to reduce our totex outperformance over the RIIO-2 period.

The operational RoRE values based on actual gearing are aligned to their notional equivalents. Actual gearing is slightly below the notional level of 55% at 53.8% for the period average and 53.4% for 2021/22.

Licence condition 2.3 sets out a Return Adjustment Mechanism based on operational performance which is triggers a revenue adjustment when operational performance falls outside of a +/-300 basis points threshold. Based on our forecasts, we do not anticipate that NGET will meet these thresholds and therefore do not expect any associated adjustment to RIIO-2 revenues.

Overview of Regulatory Performance

RoRE

RoRE is Ofgem's measure of the financial return achieved by shareholders in a licensee during a price control period from actual performance under the price control. The measure is further broken down into operational and financing components. Operational RoRE encompasses costs and allowances associated with a RIIO-2 regulated business, including Totex, incentive performance and company funded innovation costs. Financing and tax performance are included within the financial component.

RoRE aims to show the full value earned by the regulated company during the price control period. This is based on the enduring value, being the true value of the regulated business over the course of the price control. The enduring value of the business factors in the financial impact of any decisions or future events, which have yet to be reflected in Revenue and RAV but are known at the time of estimation. Where possible forecasting is utilised to give a view of the true value of the regulated business, however RRP22 does not accommodate all required adjustments. Therefore, several adjustments are applied after the completion of RRP22. These adjustments either re-phase allowances in line with spend or release deferred allowances from RIIO-1 to ensure performance is recognised when outputs are delivered. The enduring value adjustments impact on the network's return and RAV and ultimately RoRE. All values quoted in this document are post application of enduring value adjustments unless otherwise stated. Further detail on enduring value adjustments is included at Appendix 1.

RoRE for 2021/22 and the RIIO-2 period comprise the following components:

	2021/22	RIIO-2 average
Allowed Return	4.2%	4.3%
Totex performance	1.2%	0.9%
Business plan incentive	(0.2%)	(0.2%)
Non-totex incentives and innovation	0.1%	0.0%
RoRE – operational performance	**5.4%**	**5.0%**
Financing	3.7%	2.5%

Tax	(0.6%)	(0.4%)
RoRE including financing	**8.5%**	**7.1%**

The subsequent sections of this narrative cover performance against each of the individual components.

This year's submission is the first year of the RIIO-2 price control and therefore there will be no comparison of 2021/22 RoRE and its component values to previous years.[1]

Reconciliation to Revenue and Profit

(Financial values in 2021/22 price base unless otherwise stated)

The purpose of Table R2 is to report Allowed and Collected Regulated Network Revenue ("collected revenue") and to reconcile collected revenue to the turnover reported within the statutory accounts. Table R2 also provides a reconciliation for regulated network profit to profit as per the statutory accounts. These reconciliations are only performed for those years for which statutory accounts have been published. Therefore, for this submission the reconciliation is performed for 2021/22 only.

The collected revenue value is the actual year end value and therefore is an update from the collected revenue stated in the previously published PCFM. As required by the RIGs, the allowed revenue is stated as per the previous PCFM published in November 2021[2].

Collected revenue for 2021/22 of £1787.5m is collected via Transmission Network Use of System (TNUoS) charges set by the Electricity System Operator and based on Allowed Revenue for 2021/22 within the PCFM provided by Ofgem on 15 January 2021. Turnover within the statutory accounts includes TNUoS related revenue and revenues received both outside of the TNUoS and the RIIO-2 revenue frameworks. Turnover as per the 2021/22 statutory accounts is £2036.5m, a difference to collected revenue of +£249.0m. The key reconciling items between collected revenue and turnover are:

- Directly Remunerated Services revenue of +£188.9m.

  Directly Remunerated Services are those which are not already remunerated through TNUoS charges or Network Innovation Competition funding. Collected revenue specifically excludes Directly Remunerated Services as per SpC 2.1.7 whereas turnover includes all sources of revenue.

- De Minimis Business of the licensee and Other consented activities of +£34.8m.

  De minimis activities are business activities carried out by NGET outside of the transmission business below a defined threshold and are therefore not included in collected revenue. Similarly, consented activities which are those outside of the transmission business for which the Authority has given its consent in writing are not included within collected revenue. Statutory turnover includes all sources of revenue including deminimis and consented revenues.

- Other Adjustments of +£25.2m.

  The main elements of the remaining £25.2m variance between turnover and collected revenue are funding for two Network Innovation Competition Projects (+£10.9m) and adjustments for capital contributions (+£10.1m).

The second purpose of R2 is to perform a reconciliation of our regulated network profit to our statutory accounts. Net profit as per the regulated business is £330.7m compared to the statutory accounts of £289.1m giving a difference of -£41.5m. This reconciliation comprises:

[2] RIIO-2 Annual Iteration Process 2021 for Transmission, Gas Distribution and the Electricity System Operator | Ofgem

- +£265.7m for operating profit before interest and taxes. This comprises +£248.9m difference in revenues (explained above) and +£16.8m difference in operating costs which is explained in the Reconciliation to Totex section;
- +£90.9m for net interest which is explained in the financing section; and
- -£398.2m for tax which is the difference between our tax related to regulated business +£115.8m and the tax as per our statutory accounts +£514.0m which is explained in the Taxation and Tax Reconciliation section.

Totex – Reconciliation

Table R3 Totex – Reconciliation includes two elements, calculation of totex performance and reconciliation of regulatory totex to the actual opex and capex costs incurred per NGET's statutory accounts with actual reported totex.

The average totex outperformance impact on RoRE is forecast to be +0.9% for the RIIO-2 period.

Totex performance

(Financial values in 2018/19 price base unless otherwise stated)

RIIO-2 totex performance

The totex outperformance of +0.9% forecast for the RIIO-2 period is driven by the following factors:

RIIO-2 Performance	RoRE impact
Performance per RRP22	-0.4%
Efficiency ambition	+0.5%
T1+2 allowances	+0.3%
T1 Non-load allowances	+0.5%
Total	**+0.9%**

<u>Performance per RRP22</u>
Underperformance of -0.4% is primarily driven by inflationary cost pressures and spend on delivery of outputs outside of the RIIO-2 price control, this is partially offset by cost-saving initiatives.

<u>Efficiency ambition</u>
An adjustment of £0.5bn is applied to our performance position. This reflects NGET's ongoing efficiency ambition, which is not yet embedded at project level within RRP22. We continue to seek additional efficiency through improving and innovating our approach to operating, maintaining, replacing, and extending the transmission network. We therefore include £0.5bn performance ambition at a high level in our financial forecasts and the Price Control Financial Model to ensure the benefit is passed to consumers in a timely manner.

<u>T1+2 allowance</u>
There is £0.3bn performance which relates to allowances for load related projects that were initiated in RIIO-1 but are due to complete in the first two years of RIIO-2. The allowances have been reprofiled through enduring value adjustments to ensure that performance is recognised when the output is delivered. Appendix 1 includes additional detail.

<u>T1 non-load</u>
This adjustment rephases allowances for non-load projects that cross price control periods. These are rephased to ensure performance is recognised when the output is delivered. These adjustments relate to T1 non-load and ISS projects. Appendix 1 includes additional detail.

2021/22 totex performance

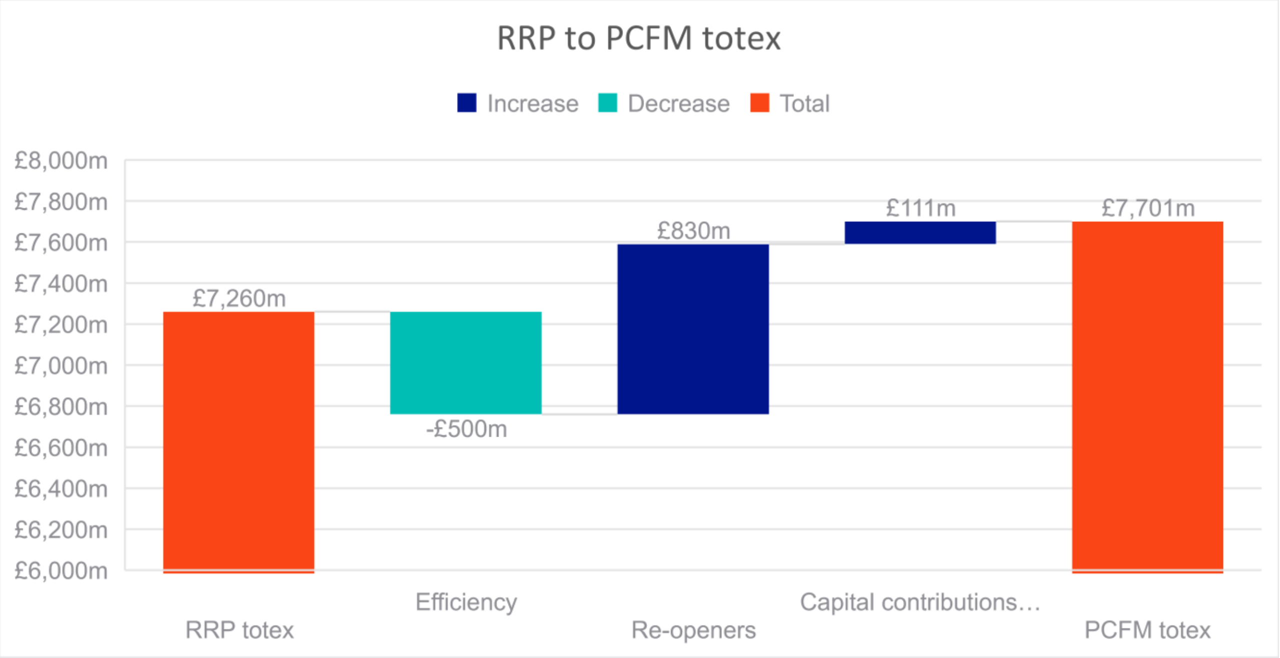
The totex outperformance of +1.2% for 2021/22 is largely driven by T1+2 allowances being recognised in 2021/22 as well as re-phasing of RIIO-1 non load allowances for projects that cross-price controls.

Reconciliation to Totex

(Financial values in 2021/22 price base unless otherwise stated)

The totex reconciliation is only applicable for years for which statutory accounts have been published. Therefore, for this submission the reconciliation is performed for 2021/22 only.

For the purposes of the reconciliation, the regulatory totex costs are as per the cost matrix in RRP22. There are a number of known and deliberate differences between the regulatory totex costs as per the cost matrix in RRP22 and the totex costs reported in the PCFM. The following waterfall details these differences for the RIIO-2 period:



Our efficiency ambition of £0.5bn is included at a high level in our financial forecasts and the Price Control Financial Model to ensure the benefit is passed to consumers in a timely manner. This reflects NGET's ongoing efficiency ambition, which is not yet embedded at project level within RRP22.

Re-opener spend of £0.8bn is included within the Price Control Financial Model as this provides our best forecast of revenues. RRP22 only captures directed and submitted re-openers within the cost matrix, any unsubmitted re-openers are captured within the re-opener pipeline log. In order to generate cost reflective revenues, re-openers that are subject to competition have not been included in the PCFM. This is because there is a level of uncertainty as to whether NGET will carry out the works.

Capital contributions of £0.1m are included within RRP22 cost matrix table totex however, these are excluded from PCFM totex as the net of spend and capital contributions received is included in the PCFM as an allowance as per Special Condition 3.37 of NGET's licence.

NGET's total reported expenditure incurred in 2021/22 is £2,094.4m; comprising opex of £989.9m and capex of £1,104.4m. This compares with regulatory totex as stated in Table R3 of £1,379.6m, a difference of -£714.8m.

The reconciling items fall into two categories, items that meet the definition of statutory opex and capex but are not included in total regulatory costs and vice versa, and regulatory costs which fall outside of the definition of Totex.

The key items which are defined differently for statutory and regulatory purposes are:

- Statutory depreciation and amortisation of £514.3m which is included in statutory opex but does not form part regulatory totex;
- Excluded, Consented and De Minimis Services costs of £25.3m which are included in opex but does not form part for regulatory totex; and
- NGET pipeline log assurance costs of £21.8m which are included in capex but not in regulatory totex. This is reflective of the FY22 value included within the RRP22 re-opener pipeline log.

The costs which fall outside of the totex definition are:

- Directly Remunerated Services of £24.1m;
- Pass-through costs of £157.2m, predominantly business rates; and
- Innovation costs of £3.3m.

Incentives and Other Revenue

Incentive and Other Revenue RoRE performance is -0.09% in 2021/22 based on actual values per RRP22. The RIIO-2 average incentive and other revenue performance is forecast to be -0.17%. The general principle underpinning NGET's forecasting policy is to set incentives equal to 2021/22 actuals plus the application of business intelligence, for example, the Insulation and Interruption Gas Emissions incentive forecast has been aligned to the flightpath to achieve a 50% emission reduction by 2030. The adverse incentive and other revenue performance are primarily driven by the business plan incentive which reduces RoRE by 0.2% each year.

The maximum non-totex incentive value recoverable over the full RIIO-2 period is £147.7m due to the various caps applied to the individual incentives and excluding the Business Plan Incentive Maximum performance would result in RoRE averaging 0.4% over RIIO-2. Inclusion of the Business Plan Incentive of -0.2%, giving an overall RoRE associate with non-totex incentives of 0.2%. The performance available to NGET under the non-totex incentive framework is extremely limited and does not seem in proportion with the level of investment required to achieve net zero ambitions.

Incentives

(Financial values in nominal price base unless otherwise stated)

NGET has continued to focus on delivery against the RIIO-2 output areas: Safety, Meeting the needs of Consumers and Network Users, Customer Connections and the Environment. Incentive performance is based on the six output delivery incentives which support these output areas as well as the Business Plan Incentive, which is set at the start of the price control as detailed below. Further detail for each output incentive is detailed below.

Energy Not Supplied ODI

The purpose of the Energy Not Supplied (ENS) incentive is designed to encourage NGET to improve network reliability by efficiently managing short-term operational risk to minimise disruption to the network. This incentive will either reward or penalise NGET's performance in relation to loss of supply events.

The incentivised loss of supply events volume target is set at 147 MWh. NGET's total incentivised energy not supplied in 2021/22 was 26.7 MWh, outperforming the volume target by 120 MWh. This performance has been achieved through effective management of the network and a strong approach to asset management. This gives rise to earned revenue of £0.8m for 2021/22, which will be recovered through allowed revenue in 2023/24.

The incentivised loss of supply events in 2021/22 were:

Location	ENS (MWh)
Elstree 275/132kV substation	25.7
Imperial Park 400/25kV substation	0.7
Ryhall 400/25kV substation	0.3
Total	26.7

Factors driving the initiation, duration and magnitude of incentivised energy not supplied events are highly varied, therefore this incentive is forecast to align to 2021/22 actuals across the remainder of the RIIO-2 period. The RoRE impact of ENS is +0.01% for 2021/22 and the remaining years of RIIO-2.

Insulation and Interruption Gas Emissions ODI

The purpose of the Insulation and Interruption Gas (IIG) Emissions incentive is to incentivise a reduction in leakage of SF_6 and other IIGs from assets on the transmission network, and to support the transition to low greenhouse gas alternative IIGs. The effect of this incentive is to reward or penalise NGET's performance in relation to CO_2 targets.

Actual IIG emissions in 2021/22 were 229,528 tCO_2e, 20,877 tCO_2e below our incentive neutral target emissions. This gives rise to earned revenue of £1.7m and RoRE impact of +0.03% for 2021/22. This performance is driven by our targeted planning and prioritised intervention approach for repair and replacement activities.

Forecasts are based on historical SF_6 inventory changes through the RIIO-T1 period and future annual IIG emissions aligned to the figures required to maintain the flightpath to achieve a 50% emissions reduction by 2030. The impact of the IIG incentive on average RoRE for the RIIO-2 period is forecast to be +0.01%. There are also a number of initiatives that we expect to undertake over the forthcoming years in order to improve our incentive performance, including SF_6 leak abatement projects which have been funded and those submitted in the SF_6 reopener.

Timely Connections ODI

The purpose of this incentive is to penalise the licensee for failing to deliver timely offers for connection to the licensee's Transmission System.

In 2021/22, NGET delivered 395 out of 408 Transmission Owner Connection Offers (96.81%) to the Electricity System Operator within mandated timescales, leaving 13 'untimely' offers. This reduces revenue by £0.3m and RoRE by <0.01% in 2021/22.

This incentive is forecast to equal 2021/22 actuals.

Quality of Connections Satisfaction Survey ODI

The purpose of this incentive is to incentivise NGET to improve the quality of service delivered to connection customers. The effect of this incentive is to reward or penalise NGET's performance in relation to customer connections.

In 2021/22 NGET achieved a mean performance score for quality of connections satisfaction survey of 7.8, slightly above the performance neutral target of 7.7. This gives rise to earned revenue of £0.2m and a minor impact on RoRE (<0.01%). NGET has worked hard to deliver this outcome, with customers recognising we understand and resolve their issues. However, this is against a backdrop of a significant increase in customer applications. We have thoroughly reviewed the feedback received and are taking steps to increase satisfaction over the remainder of RIIO-2.

NGET has forecast this incentive to be performance neutral for the remaining years of RIIO-2 as this is an Ofgem directed incentive, however, we aim, through a targeted improvement approach that the outturn position, to exceed a flat forecast.

SO-TO Optimisation ODI

SO-TO Optimisation is a new, trial incentive designed to encourage collaboration with the Electricity System Operator (ESO) to identify and provide additional solutions beyond business-as-usual activities to help reduce constraint costs.

In 2021/22 NGET delivered six enhanced services solutions successfully with the ESO, which is estimated to have resulted in over £37.4m in actual constraints savings. This success over the trial period demonstrates the effectiveness of the incentive in delivering benefit to consumers and the value of extending the incentive to cover the remainder of the RIIO-2 period rewarding NGET in continuing to seek innovative ways to provide enhanced services to the ESO to deliver constraint cost savings. These constraint savings achieved incentive revenue of £4.95m out of a maximum £5m, giving rise to a RoRE impact of +0.08%.

This incentive is determined through a direction from Ofgem and is therefore a nil forecast for 2022/23 as no direction has yet been published. As the incentive is currently only in place for the first two years of the price control period, the forecasts for the remainder of the RIIO-2 period are also nil.

Environmental Scorecard ODI

The effect of this incentive is to reward or penalise NGET's performance in relation to six environmental targets compared to annual thresholds. These six environmental targets are:

- Business travel
- Operational and office recycling
- Office waste reduction
- Office water
- Environmental value of non-operational land
- Net gain on construction projects

NGET has outperformed in all six elements of the scorecard this year, with the maximum reward threshold being reached on four of the elements. The revenue earned from this incentive in 2021/22 is £0.5m and the RoRE impact is +0.01%. This is mainly driven by the achievement of the maximum threshold for value of non-operational land. This was achieved through partnering with organisations, such as Langdyke Countryside Trust, which will enable at least 2,200 people per year to access nature via our sites through conservation days and environmental education visits. We also introduced a 10-year habitat management plan to protect and enhance woodland at our Bramley substation site.

The average RoRE impact of the environmental scorecard incentive is forecast to be +0.02% over the RIIO-2 period based on targets and performance consistent with 2021/22 values.

RIIO-2 Network Innovation Allowance

(Financial values in 2018/2019 price base unless otherwise stated)

The purpose of the RIIO-2 Network Innovation Allowance (NIA) is to incentivise networks to take forward innovation projects that have the potential to address consumer vulnerability and/or deliver longer–term financial and environmental benefits for consumers, which may not have been undertaken within the price control.

The NIA allows NGET to recover 90% of total NIA expenditure capped at a maximum allowance of £49.3m over RIIO-2. Therefore, at least 10% of NIA expenditure will impact operational RoRE.

In 2021/22 NGET spent £2.4m with the 90% allowance recovering £2.2m against this expenditure RoRE operational performance for 2021/22 is therefore not significantly impacted (<0.1%) by the net cost of NIA projects.

Expenditure in 2021/22 reflects definition and refinement of strategies for RIIO-2 along with the establishment of processes and stage gates as per RIIO-2 governance. A total of thirteen NIA projects have been registered by NGET and we have made financial contributions through collaboration on three NIA projects led by other network licensees, bringing the total to sixteen. Nine out of the sixteen NIA projects have incurred costs in 2021/22.

NGET forecast that maximum TNIA value will be utilised across the price control period given the focus of the innovation strategy for RIIO-2 and the need to work differently to meet Net Zero targets with the spend trajectory increasing over RIIO-2. In order to meet the increasing trajectory NGET expect to have a fully resourced team to deliver more of the projects in the latter years of RIIO-2. This level of expenditure would result in a net cost to NGET of £4.9m which has a limited impact on RoRE for the RIIO-2 period (<0.1% impact).

Further information can be obtained from NIA annual summaries are published on the National Grid Electricity Transmission website[3].

Carry Over Network Innovation Allowance

(Financial values in 2018/2019 price base unless otherwise stated)

The purpose of the Carry Over Network Innovation Allowance is to extend RIIO-1 Network Innovation funding. This allowance ensures any unspent 2020-2021 RIIO-1 NIA allowance is carried over into the first year of RIIO-2 in 2021/2022, to spend on projects that had already been started by 31 March 2021.

In 2021/22 NGET spent £0.7m (ECNIAt) against the maximum CNIA qualifying for allowance of£0.9m.

Previously, NGET forecast that £0.9m would be spent. However, the forecast amount was not spent in full as:

- Some of the scope elements in NIA_SHET0032 were shifted out of the current project and the remaining scope was created under RIIO-2 funding; and
- an element of scope in NIA_NGTO043 was shifted out of the current project and not included in RIIO-2 funding.

Strategic Innovation Fund

(Financial values in 2018/2019 price base unless otherwise stated)

The Strategic Innovation Fund aims to determine and fund innovative projects with the potential to accelerate the transition to Net Zero whilst succeeding commercially where possible to ensure consumer affordability.

In March 2022, NGET secured funding through the SIF mechanism for three projects across the round one discovery phase. The projects progressed according to the plan described in the funding applications. As projects started in March 2022 only internal labour costs are recorded, as per our view as at 31 March 2022, with remaining costs to be recorded when the project results are delivered in April/May 2022. The summary of the costs and forecast is presented in the table below:

Project Name	2022 (£k)	2023 (£k)	Total (£k)
SCADENT	2	134	136
SEGIL	2	121	123
Eye in the Sky	5	105	110

Financing and Net Debt position

Financing

(Financial values in 18/19 price base unless otherwise stated)

The purpose of Table R5 is to report annual actual and forecast Net Interest as per the Regulatory (RIIO-2) definition. This is then adjusted to remove inflation and include early redemption costs and amortisation of discount/premia on issue and compared against the cost of debt allowances published in the latest PCFM. This table also reconciles actual Net Interest with the interest charge included in the statutory accounts.

The Net Interest Per Regulatory (RIIO-2) Definition will continue to be used as an input to calculate the tax clawback adjustment in the PCFM through the TNDI variable value.

Table R5 further analyses the performance of a notional and actual company. A notional company in this context is a hypothetical, but typical and efficient network company whereas the actual company is the actual performance during the price control. This can be demonstrated in gearing where notional gearing is 55% in RIIO-2 whereas actual gearing in RIIO-2 is on average 53.8%.

Overall assumed regulatory finance cost at notional and actual gearing for RIIO-2 is not a true reflection of our regulatory finance cost. The Ofgem calculation included in the RFPR deducts inflation in the interest charge based on the assumption that all debt is inflation linked but not all debt is index linked. We consider that the non-cash principal inflation accretion on bonds and loans (R5, row 36) is more representative of inflation within the interest charge. Adjusting the regulatory finance cost for this value results in costs in excess of allowances of £156m.

<u>Net Interest Reconciliation</u>

Table R5 also requires a reconciliation between actual Net Interest with the interest charge included in the statutory accounts.

Actual Net Interest for 2021/22 is £334.2m. Net interest as per the 2021/22 statutory accounts is £243.4m, giving a difference of +£90.9m. The key reconciling items between collected revenue and turnover are capitalised interest back of +£55.5m and fair value adjustments including derivatives of +£37.0m. The remaining items including swap termination costs, movements relating to pension fund, commitment fees, provision unwind and right of use liability reconcile the remaining -£1.7m. These items are excluded from Net Interest as per the regulatory definition detailed in the RIIO-2 RFPR - Regulatory_instructions_and_guidance_version_1.0 glossary.

Net debt

(Financial values in nominal price base unless otherwise stated)

The purpose of Table R6 is to report annual actual and forecast Net Debt as per the Regulatory (RIIO-2) definition. The worksheet also reconciles the actual Net Debt with statutory accounts. The Net Debt Per Regulatory (RIIO-2) Definition will continue to be used as an input to calculate any tax clawback.

Total Debt closing average per Statutory Accounts for 2021/22 is £8584.2m and Total Net Debt closing average per Regulatory (RIIO-2) definition for 2021/22 is £8330.8m, a difference to Statutory Accounts of -£253.4m. The key reconciling items between statutory accounts and the RIIO-2 definition are Fair Value Adjustments +£78.1m, Accrued Interest -£69.5m, Derivatives -£197.0m and IFRS 16 Right of Use Liability -£65.0m. These items are excluded from Net Debt as per the regulatory definition detailed in the RIIO-2 RFPR - Regulatory_instructions_and_guidance_version_1.0 glossary.

RAV

(Financial values in 2018/19 price base unless otherwise stated)

The R7 – RAV table details the annual Regulatory Asset Value (RAV) position based on the actual and forecast RAV per the ET2 PCFM for the August 2022 submission. The closing RAV balance is used in deriving actual gearing and the NPV neutral equity element of RAV is then used to calculate RoRE.

The Closing RAV values in row 12, Opening RAV in cell E15, Net additions in row 18 and Depreciation in row 21 are those per the latest PCFM submitted in August 2022. The PCFM is then adapted to include the impact of enduring value adjustments (EVAs) to give the adjusted closing RAV. It is the closing RAV from the PCFM adjusted for EVAs that is used in the calculation of actual gearing and RoRE as the enduring value adjustments applied provide a more representative view of in year performance. Details of the enduring value adjustments are reported in Appendix 1.

The following table shows the difference between the adjusted closing RAV calculated in the R7 – RAV table and the closing RAV per the latest PCFM. The enduring value adjustments that have been applied either re-phase performance in line with spend or release deferred performance from RIIO-1 to ensure performance is recognised when outputs are delivered:

	2022	2023	2024	2025	2026
Closing RAV per latest PCFM (£m)	14,162	14,581	14,983	15,305	15,725
In year enduring value adjustments (£m)	-4	100	44	28	28
Cumulative enduring value adjustments (£m)	-4	96	139	167	195
Adjusted Closing RAV (£m)	14,158	14,677	15,122	15,472	15,920

The adjusted closing RAV is forecast to increase by an average of c.£440m year-on-year, reflecting an increase in the level of outputs NGET expects to deliver in response to Net Zero targets.

Taxation and Tax Reconciliation

(Financial values in 2018/19 price base unless otherwise stated)

The purpose of the taxation worksheet is to calculate the tax out or underperformance against the tax allowance at actual and notional levels of gearing.

Forecast Regulated Tax Liability in 2021/22 is £115.9m, the Adjusted regulated Tax liability is £115.8m. The difference between these values is through the tax on innovation and incentives of £0.1m.

The forecast tax allowance for 2021/22 is £106.9m and forecast tax outperformance is £0.1m at actual gearing and £0.3m at notional gearing levels. The difference between actual and notional is caused by an adjustment to regulatory tax cost relating to variance from notional gearing of -£0.2m.

The primary objective of the R8a- Tax Reconciliation worksheet is to highlight differences between a licensee's CT600 actual corporation tax liability and the calculated tax allowance in the 'Finance & Tax' sheet of the Latest PCFM. Due to the timing of the CT600 submissions to HMRC, this sheet is to be reported with a one-year lag (i.e. inputs will relate to the previous reporting period). Therefore the tax reconciliation worksheet 8a remains blank and will commence in next year's submission in August 2023.

Corporate Governance

(Financial values in nominal price base unless otherwise stated)

The purpose of this worksheet is to report the executive directors' remuneration. Additionally, this worksheet is to report actual dividends paid that relates to the regulated business. The worksheet then reconciles with information in the statutory accounts.

Corporate Ownership and Governance Framework

The corporate governance structure for NGET can be found in Appendix 2, including ownership stakes in the licensee expressed as a percentage and the names (both registered and trading) of all companies in the ownership structure between the NGET and National Grid plc.

Board of directors

Reinforcing its commitment to sound corporate governance the Board has continued to strengthen and develop both its composition and governance framework, implementing, as applicable, many of the best practice governance principles in operation at the National Grid plc level.

At the year end, the Board consisted of three executive directors, two National Grid Group-appointed non-executive directors and two Sufficiently Independent Directors (SIDs). Between them, they provide a broad and diverse range of experience and technical skills from both within and external to the organisation, from the energy sector, other regulated industries and external bodies.

Directors who were in office during the financial year ending 31 March 2022 and up to the date of this report:

Name	Director Type	Appointment Date	Resignation Date
Bennett, Christopher Paul	Executive	25/06/2016	
Childs, Dawn Elizabeth	Shareholder-appointed non-executive	10/12/2019	31/05/2021
Delahunty, Alice Kyne	Executive	14/12/2020	
Elphick, Clive Harry	Sufficiently Independent	01/04/2014	17/03/2022
Lewis, Alexandra Morton	Shareholder-appointed non-executive	13/04/2018	
Long, Jeremy Paul Warwick	Sufficiently Independent	17/03/2022	
Pettifer, Darren	Executive	01/08/2021	01/08/2022
Ross, Cathryn	Sufficiently Independent	21/06/2019	
Shaw, Lucy Nicola	Shareholder-appointed non-executive	27/07/2016	22/11/2021
Sheppard, Philip Graham	Non-executive	01/08/2021	
Todd, Alistair Mark	Shareholder-appointed non-executive	30/04/2020	01/08/2021
Wilson, Benjamin Hollis	Shareholder-appointed non-executive	22/11/2021	

Board committees

There are several committees within NGET, including:

Audit Committee

The Audit Committee's role is to keep under review the Company's financial reporting and internal controls and their effectiveness, together with reviewing the Company's risk management processes. It also reviews the external audit plan and reviews the external auditors' findings. Membership of the Committee comprises:

- Jeremy Long (Sufficiently Independent Director)
- Alexandra Lewis (Shareholder-appointed non-executive Director)

- Cathryn Ross (Sufficiently Independent Director)

Business Separation Compliance Committee (BSCC)

The BSCC is responsible for overseeing the duties and tasks of the Business Separation Compliance Officer and for overseeing compliance with the business separation licence conditions.

Membership of the Committee is by appointment of the Board and comprises all directors of the Company. The Committee is chaired by Cathryn Ross (Sufficiently Independent Director).

Finance Committee

The Finance Committee is responsible for setting policy and grants authority for financing decisions, credit exposure, hedging and foreign exchange transactions, guarantees and indemnities, all subject to the risk appetite of the Board. It also approves other treasury, taxation and pension funding matters, as well as having responsibility for the governance of the Company's pensions schemes and the Company's insurance strategies, and if appropriate, recommends these to the Board. Membership of the Committee comprises:

- Andrew Agg (Executive Director of National Grid plc)
- Alexandra Lewis (Shareholder-appointed non-executive Director)

Electricity Transmission Executive Committee (ETEC)

ETEC directs the affairs of the Electricity Transmission business on behalf of the Board, to perform an assurance role within the context of the overall RIIO networks governance framework. Its remit extends to approving the Electricity Transmission strategies and business objectives for managing the RIIO contract and for approving opportunities to deliver value within that contract in accordance with Delegation of Authority limits. The directors of ETEC are:

- Alice Delahunty (Executive Director)
- Chris Bennett (Executive Director)
- Darren Pettifer (Executive Director until 1 August 2022)

The following Committee members form part of the Company's senior management team and are not statutory directors.

- Derek Goodban (UK General Counsel)
- Sarah Milton-Hunt (Chief Information Officer)
- Claudia Nicoll (Chief People Officer)
- Lydia Ogilvie (Director of Network Strategy & Operations)
- Roisin Quinn (Head of Customer Connections)
- Aled Rowlands (Interim Director of Corporate Affairs)
- Zac Richardson (Head of New Infrastructure)
- Julie Speirs (Director of ET Transformation)
- Matt Staley (Head of Asset Operations)
- Noha Wagdy (Director of Safety, Risk and Compliance)

Decision Making

The following table explains the decision-making responsibilities that are reserved to a parent/group company:

Purpose, values and strategy	Purpose, values and strategy are matters reserved to the ultimate shareholder, National Grid plc. The Company works within the purpose, values and strategy of National Grid and the Company's Board is responsible for the oversight of the Company's purpose, values and strategy. Further details can be found on pages 8 – 13 of the Company's ARA.[4]
Board nominations	Changes to the structure, size and composition of the Board and Board Committees are matters reserved to the Company's Board. In accordance with the Company's Articles of Association, the Company's shareholder (being National Grid Holdings Limited) may appoint and remove directors by ordinary resolution.
Board evaluation	The Board evaluation process is a matter reserved for the Company's Board. Separately to the Company, the Board of National Grid plc complies with the provisions of the UK Corporate Governance Code in relation to its own evaluation.
Executive remuneration	Executive remuneration is a matter reserved to the Board of National Grid plc. Further information on this is available within the Remuneration Report of National Grid plc's Annual Report and Accounts on pages 108 to 131.[5]
Dividend policy	Dividend policy is a matter reserved to the Company's Board. The Company will consult with the Board of National Grid plc to determine dividends, with final approval from the Company's Board.

Executive Remuneration Policies

Executive remuneration is controlled by the ultimate parent company, National Grid plc. The National Grid plc Remuneration Committee is responsible for recommending the remuneration policy for the National Grid plc executive directors, Group Executive Committee members and the Chair, and for implementing this policy. Further information on this is available within the Remuneration Report of National Grid plc's Annual Report and Accounts on pages 108 to 131[6].The aim of NGET's renumeration policy is to ensure that how we structure remuneration and how we make decisions on annual and long-term reward plans are compatible with and fully support:

- attracting, motivating, and retaining employees while not over-paying; the key elements of remuneration are targeted broadly at mid-market of our peer group of general industry and energy services organisations.
- ensuring we pay our employees in a way that incentivises stretching financial and operational performance, within the risk appetite set by the NGGT leadership team.
- being fully aligned to the fact that we are a Regulated company and our impact we have on the cost to the consumer; and
- actively supporting our strategy, ethics, values, and contribution to society in the areas where we operate.

[4] https://www.nationalgrid.com/document/147366/download
[5] https://www.nationalgrid.com/document/147366/download
[6] https://www.nationalgrid.com/document/146731/download

NGET's remuneration policies are designed to ensure alignment with customer and stakeholder interests; our purpose, culture and values; and long-term delivery of our strategy. Our management is incentivised through our target setting and remuneration policy to deliver the actions necessary to achieve our net zero objectives. Alignment of the Annual Performance Plan (APP) and the Long Term Performance Plan (LTPP) to core financial Key Performance Indicators (KPIs) incentivise operational excellence and long-term value creation to ensure we deliver for our customers efficiently.

Remuneration Framework

Our remuneration policy weights executive and senior leadership compensation more heavily towards performance related pay, especially long-term share-based reward. The portion of reward at risk (linked to performance-based elements) accounts for more than half the total remuneration opportunity; and is linked to both business performance measures and individual performance. This typically comprises an annual element (APP) and a longer-term element (LTPP):

Band	Target APP (% of salary)	LTPP Maximum Award	Pension DC contribution*	Car Allowance	PMI	Holiday	Flexible Benefits
President NGET	45.00%	Up to 225% of annual base salary	20%	£12,000	Uncapped	28 days annually (plus public holidays)	We offer a range of benefits including a Sharesave scheme, Share incentive plan, employee assistance programme and flex benefits scheme
NGET Leadership Team	17.5 - 32.5%	Up to 80 - 120% base salary	15%	£8,500	Family		

**Externally hired employees will participate in a Defined Contribution (DC) arrangement with a maximum of 12% employer contributions; and receive Employee only private medical insurance (PMI) cover.*

Annual Remuneration Increases

Base salary increases are generally reviewed annually and are targeted broadly at mid-market of our peer group. In addition, a number of other factors are taken into account:

- business performance and individual contribution;
- the individual's skills and experience;
- scope of the role, including any changes in responsibility; and
- market data, including base pay and total remuneration opportunity in the relevant comparator group.

The remuneration of the President NGET and other senior leaders are reviewed and approved annually at National Grid Group Executive Committee level. The budget for annual salary increases for Senior Managers and Managers is also set by the NG Executive Committee and allocated to individuals with reference to factors outlined above.

Performance Related Remuneration

Short term incentives

The Annual Performance Plan (APP) comprise reward for achievement against NGET scorecard measures and achievement against individual objectives. Performance measures and targets are normally agreed at the start of each financial year and are aligned with NGET strategic business priorities. Targets are set with reference to the budget, which is reviewed and approved annually by the National Grid Executive Committee.

Individual performance will be determined by an assessment of the achievement of objectives set at the start of the financial year and their demonstration of leadership behaviours and National Grid values.

Operational performance of NGET during the year will be assessed against metrics and targets set at the start of the financial year.

The achievement of stretch performance across all measures will result in the maximum APP award of 200% of target at managerial levels. APP awards are paid in June and subject to malus and clawback provisions.

Long term incentives

NGET operates a share based Long Term incentive plan (LTPP) under which awards may be granted to senior managers each year, with the intention to provide an appropriate incentive to NGET employees and to encourage outstanding long-term performance. Awards are in the form of either Performance Shares or Restricted Shares.

Vesting occurs at the third anniversary of the award with the vesting value flexing with the value of the National Grid business during the vesting period. The Committee reserves the right to apply discretion on overall vesting outcome taking into consideration the underlying business, financial and operational performance. LTPP awards are subject to malus and clawback provisions.

2021/2022 Executive Remuneration

As at March 2022, NGET has three executive directors, Alice Delahunty (President of Electricity Transmission), Christopher Bennett (Regulation Director Electricity Transmission & Programme Director FSO) and Darren Pettifer (CFO), whose corresponding remuneration has been declared in Table R9. Darren Pettifer served as an executive director from 1 August 2021 and therefore his renumeration has been pro-rated accordingly.

All executive directors oversee the running of NGET. This has been reflected by allocating 100% of their total remuneration to the regulated businesses

National Grid's group structure means that Directors do not hold shares at a Licensee level. For this reason, NGET has agreed with Ofgem that we will not declare any shares/options as part of the remunerations package as information around Shares/Options and dividends paid becomes inapplicable. Any shares owned would be in National Grid plc and would not be allocated to the individual businesses. Shares owned would not be awarded by the rewards team and do not form part of the remuneration package**.**

CEO Pay Ratios

When making remuneration decisions for NGET senior leaders, account is taken of the remuneration arrangements and outcomes for the wider workforce and statistical information, such as the pay ratio between senior management and the wider workforce. This compares the Director of NGET's remuneration to the equivalent pay for the lower quartile, median and upper quartile UK employees (calculated on a full-time equivalent basis) in accordance with the Companies (Miscellaneous Reporting) Regulations 2018 (as amended).

The 2021/2022 CEO Pay Ratio reports the 25th, 50th and 75th percentiles as 11, 8.8 and 6.9 respectively. The median pay ratio reported this year is consistent with our wider pay, reward and progression policies. For reference, the National Grid plc Group-wide pay ratio and National Grid UK ratio are disclosed in the NG plc Group Annual report.[7]

Dividend policy

NGET's approach to dividend policy is to make distributions which align with regulatory target capital structures taking into consideration credit metrics and medium-term cash requirements. NGET's dividend policy is to anticipate the reducing nominal gearing level in the final year of RIIO-2. Based on current high-level capital expenditure and cash flow projections, assuming a conservative inflation and no further dividend through RIIO-2. The current dividend of £300m would lead to approximately 54% gearing in 2025/26 which closely aligns to the notional gearing.

The Board approved a final dividend of £300.0m paid in July 2022.

Pensions and Other Activities

(Financial values in 2018/19 price base unless otherwise stated)

The purpose of the Pensions and Other Activities worksheet is to report a summarised position of NGET's pensions deficit for defined benefit schemes, and to capture any Ofgem related fines and penalties. The latter feeds into the calculation of RoRE.

The established deficit allowance less Pension Payment History (PPH) is £37.1m. As the pension scheme valuation is performed tri-annually, the valuation presented in the 2021/22 RFPR is the 2018/19 valuation.

There have been no Ofgem related fines or penalties in the year 2021/22.

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.

In summary, the following assurances were completed:

1. Assurance Template completed by Data Provider
2. First Level Reviewer
3. Second Level Reviewer
4. Independent Expert Reviewer/ Internal Data Audit
5. Manager & Senior Manager
6. Director Sign Off

Basis of any estimates and allocations

Forecasts are based on the key principle that variable values remain unchanged from the PCFM published on 30 November 2021 unless:

- Actual data is available;
- there is a clear external signal indicating change to values published through the November 2021 Annual Iteration Process (AIP); and
- there is an increase in the assurance of project costs compared with those published through November 2021 AIP.

[7] https://www.nationalgrid.com/document/146731/download

Where there is neither an external signal nor increased cost assurance, variable values remain unchanged from the November 2021 AIP.

These forecasting principles are specifically interpreted and applied to each category of variable values. On an annual basis the policies within this document are reviewed and signed off by NGET's Chief Financial Officer.

Appendices

Appendix 1 - Enduring Value Adjustments

To provide a true view of RoRE, several enduring value adjustments have been applied to totex. The enduring value is the true value of the regulated business over the course of the price control and factors in the financial impact of any decisions or events which are yet to be reflected in revenue and RAV but are known at the time of estimation. Where possible forecasting is utilised to give a view of the true value of the regulated business, however the RRP does not accommodate all required adjustments. Therefore, several adjustments are required to be overlaid after the completion of the RRP. These adjustments either re-phase performance in line with spend or release deferred performance from RIIO-1 to ensure performance is recognised when outputs are delivered. A summary of the RoRE impact for both categories of adjustment can be seen below:

EV RoRE impact	2022	2023	2024	2025	2026	T2 Ave.
T1 deferral adjustments	1.67%	1.25%	0.29%	0.36%	0.43%	0.78%
Re-phasing adjustments	-1.76%	0.73%	0.58%	0.21%	0.13%	0.00%
Total EV impact	-0.09%	1.99%	0.88%	0.57%	0.57%	0.78%

The following table details the individual enduring value adjustments applied and the reasoning behind the application. The adjustments that have been applied are also used to derive NGET's Return on Equity (RoE) for internal business planning purposes. These items reconcile to worksheet R3 – Totex Reconciliation:

Enduring Value Adjustment	2021/22 Adjustment (2018/19 prices)	Total T2 Adjustment (2018/19 prices)	Total T1 Adjustment (2018/19 prices)	Explanation
T1+2 Deferral	£169m	£332m	-£332m	£332m of allowances deferred in T1 relating to crossover schemes. Performance to be released in line with output delivery dates (£169m in 2021/22 and £163m in 2022/23).
T1 Non Load	£120m	£404m	-£404m	Outstanding projects from T1 where work is expected to complete in T2 without further funding. Deferral of allowances released in line with spend to ensure performance is recognised when outputs are delivered.
ISS Deferral	£25m	£46m	-£46m	Agreement with Ofgem for the late delivery of ISS sites, with no change to T1 allowances.
Pre-con rephasing	-£12m	-£0m	n/a	Re-phasing of performance in line with spend.
Hinkley T1 Deferral	-£14m	£0m	n/a	Delivery of Hinkley works deferred from T1 to T2. Deferral of allowances released in line with spend to ensure performance is recognised when outputs are delivered. Outputs expected to be delivered in FY24.

Hinkley T2 Deferral	-£33m	£0m	n/a	Deferral released in line with spend. Outputs expected to be delivered in FY24.
Phasing adjustment	-£272m	£0m	n/a	Re-phasing of allowances compared to those in the PCFM. This re-phases allowances to match the spend profile to provide a more accurate view of in year performance. .
Total	**-£16m**	**£782m**	**-£782m**	

Appendix 2 - Corporate Ownership Structure