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RP7 - NIE Networks Price Control 2025-2031

Final Determination Annex F
Pensions
30 October 2024

About the Utility Regulator

The Utility Regulator is the independent non-ministerial government department responsible for regulating Northern Ireland's electricity, gas, water and sewerage industries, to promote the short and long-term interests of consumers.

We are not a policy-making department of government, but we make sure that the energy and water utility industries in Northern Ireland are regulated and developed within ministerial policy as set out in our statutory duties.

We are governed by a Board of Directors and are accountable to the Northern Ireland Assembly through financial and annual reporting obligations.

We are based at Queens House in the centre of Belfast. The Chief Executive and two Executive Directors lead teams in each of the main functional areas in the organisation: CEO Office; Price Controls; Networks and Energy Futures; and Markets and Consumer Protection. The staff team includes economists, engineers, accountants, utility specialists, legal advisors and administration professionals.

OUR MISSION

To protect the short and long-term interests of consumers of electricity, gas and water.

OUR VISION

To ensure value and sustainability in energy and water.

OUR VALUES

ACCOUNTABLE
We take ownership of our actions.

TRANSPARENT
Ensuring trust through openness and honesty.

COLLABORATIVE
Connecting and working with others for a shared purpose.

DILIGENT
Working with care and rigour.

RESPECTFUL
Treating everyone with dignity and fairness.

Abstract

This Annex provides a detailed outline of analysis of the NIE Networks RP7 submission, concerning the Northern Ireland Electricity Pension Scheme (NIEPS). We review funding of historical Pension Deficit Repair, Investment Strategy, costs, expenses and proposed allowances.

Audience

NIE Networks, consumers, consumer representatives, consumer groups, other regulated companies in the energy industry, government, and other bodies with an interest in the energy industry.

Consumer impact

NIE Networks has a pivotal role in terms of 'keeping the lights on'. Both the effectiveness and efficiency of NIE Networks are key to industry and domestic consumers. The RP7 Price Control aims to set an efficient revenue cap to enable NIE Networks to deliver quality outputs that customers need.

This final determination would result in a £17 reduction in network charges for each domestic consumer when compared to the NIE Networks business plan submission.

Contents

Executive Summary

Background

The NIEPS is a multi-employer scheme. This means that other companies (both regulated and non-regulated) are also members of the scheme. Current employers that participate in the NIEPS are: Northern Ireland Electricity Networks Ltd (referred to as NIE Networks throughout this paper), and Capital Pensions Management Ltd.

Before these companies were divested to the ESB Group in December 2010, the NIEPS was formerly known as the Viridian Group Pension Scheme (VGPS). In addition to the above companies, VGPS also included Viridian P&E, Viridian Group and others, NIE PPB and NIE Energy Supply (now Power NI). As part of the divestment to ESB, 91% of the VGPS deficit was transferred to NIEPS and 9% to the newly created Viridian Pension Scheme.

The pension scheme operates two sections as follows:

- Defined Benefit (DB) section, referred to as the ‘Focus’ plan; and
- Defined Contribution (DC) section, referred to as the ‘Options’ plan.

In March 1998, NIE (now NIE Networks) closed the DB section of the pension scheme to new entrants. Since then, new joiners are instead offered membership in the DC section of the scheme[1] . This is consistent with general trends in United Kingdom (UK) private sector pensions.

NIE Networks makes two types of payment to the scheme:

- Ongoing pension payments which represent the cost of additional benefits being accrued by existing employees who are still members of the scheme and
- Annual deficit repair payments which aim to bring the scheme into surplus over a period of time.

In the DB section of the scheme an employee’s pension is based on the number of years of service and final salary with sponsoring employer(s). The level of future pension benefit an employee will receive is set; the investment risk lies with the employer(s).

Employer contributions to the DB section were just over £26 million in the year to 31 March 2021 and nearly £27 million in the year to 31 March 2022 (contributions in respect of future benefit accrual represented around 25% of total contributions). Employer contributions to the DC section were around £6 million a year over the

[1] See Northern Ireland Electricity Limited: Transmission and Distribution RP5 Price Control, Statement of Case to the Competition Commission, 10 May 2013.

same period.

The Electricity (Protected Persons) Pensions Regulations (Northern Ireland) 1992 protect certain employees' pension benefits in respect of past and future service. This protection restricts the extent to which the NIEPS's benefits and member contribution rates can be changed.

In the DC section of the scheme, an employee's benefits will be dependent on the contributions to, and growth of, the fund and the fund manager's investment and other attributable costs. There is no guarantee on the level of future pension benefit an employee will receive; the investment risk lies with the employee.

DC arrangements typically, but need not, involve lower employer pension contributions than a DB pension. Whether contributions are lower to a DC arrangement than to a DB scheme, depends on the design of the two schemes.

The main difference between DB and DC provision relates to risk: in a DB scheme the employer bears the risk of adverse future experience through the possibility of deficiency contributions being required, whereas in a DC arrangement the risk of adverse future experience rests with the member, through lower than expected benefits. Conversely, members benefit from favourable experience in a DC arrangement, whereas in a DB scheme the employer may benefit (depending on the scheme rules).

The NIEPS is governed by a trust deed and rules and is managed by trustees. Under the scheme rules, each participating employer is required to contribute to the scheme both by way of ongoing contributions and in terms of deficit repair. Trustees take into account the financial position of these companies and the strength of its covenants when forming a view of a deficit recovery plan for the scheme.

Participating employers make ongoing payments to the NIEPS associated with its current employees. With regard to the DB plan, they are also responsible for deficit repair payments associated with the cumulated member liabilities.

For the final determination review we are primarily using pension scheme data from the triennial pension scheme valuation, as at 31 March 2022. This triennial valuation provides a more detailed analysis of pension scheme aspects, assumptions and valuations than the annual or quarterly valuation updates. In addition, we also note that the company relies on the triennial valuations for setting the schedule of company contributions.

Table 1 provides an overview of the number of active members in both the DB and DC sections of NIE Networks' pension scheme as of 31 March 2022.

Scheme Section	Number of Active Members (as of 31 March 2022)
DB (Focus)	213
DC (Options)	1,047

Source: AON, Scheme Funding Report: Actuarial Valuation of the Northern Ireland Pension Scheme at 31 March 2022.

Table 1: Overview of active members for DB and DC section of NIE Networks' pension scheme

These members include current employees (active members), deferred pensioners and pensioners. Table 2 provides further details on membership numbers of the scheme by category as at 31 March 2022. As can be seen, only 4.6% of the total members of the DB section of NIE Networks' pension scheme are active employees.

Table 2 illustrates the membership of NIE Networks' pension scheme as at 31 March 2022:

Scheme Section	Defined Benefit Membership (Focus)	Defined Contribution Membership (Options)
Actives	213	1,047
Deferred pensioners	350	795
Pensioners and dependants	3,978	76
Total	4,541	1,897

Table 2: NIE Networks' pension scheme membership breakdown as at 31 March 2022 – Source: Northern Ireland Electricity Pension Scheme: Annual Report & Accounts, Year Ended 31 March 2023

It should also be noted that the majority of active employees are 'Protected Persons' as outlined in the Electricity (Protected Persons) Pension Regulations (Northern Ireland) 1992. Protected persons are protected by status and their pension benefits cannot be reduced without their consent. This applies to both past and future service. There are only 25 active employees of NIE Networks who are not 'Protected Persons'[2] .

Both the DC and DB sections of the pension scheme have:

- Normal ongoing pension service contributions[3]

[2] Note that NIE Networks states in its 'RP7 Business Plan Pensions Commentary Template: August 2022', that *"As at 31 March 2022 there were 4,541 members in the DB section of the pension scheme. Out of 213 active members, 25 do not have protected persons status. 98% of the deferred and pensioner population have protected persons status."*

[3] Contributions to a pension scheme to cover the normal pension service cost of that scheme, i.e., the actuarially-determined present value of retirement benefits earned by plan participants in the current period, based on the company's existing pension benefit formula.

- Pension scheme administration costs[4] and investment management fees[5]

In addition, there may be a range of other costs specific to the DB section of the scheme, which may include:

- Pension deficit repair payments[6]
- Pension Protection Fund (PPF)[7] Levies[8]
- Pension hedging and contingent asset cost[9]
- Augmentation of benefit cost[10]
- Pension-related severance cost[11]

NIE Networks proposed an allowance of £20.025 million per annum from 1 April 2022 to 30 September 2023, increased on 1 April 2023 by the increase in the Retail Prices Index between 1 September 2021 to 31 August 2022. These deficit contributions are to ensure “the statutory funding objective (i.e. the amount of assets needed by the Scheme to meet its technical provisions) is met.” NIE Networks outlines that under the recovery plan, if the assumptions made are borne out, then the funding shortfall will “be eliminated over a period of 1 year 6 months from the effective date of the valuation, which is by 30 September 2023[12].”

In addition, NIE Networks proposed allowances for ongoing pension costs. These costs have been assessed and benchmarked and our analysis and proposed allowances for RP7 are included in section 6 of this document.

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[4] The administrative cost for the operation of a pension scheme by the scheme trustees (excluding interest and taxation) including salaries and cost of pension scheme administrators and all other associated cost of administering the pension scheme, whether borne by the scheme directly or the employer(s) and not recovered from the scheme.
[5] Any scheme investment management expenses which are charged separately or have not been implicitly allowed for, under change in market value of investments or as a deduction from investment income.
[6] The cash cost paid, directly or indirectly, by the licensee to reduce a shortfall in a pension scheme’s assets compared with its liabilities as set out in the deficit recovery plan agreed between the licensee and the pension scheme trustees, reported to the Pensions Regulator and certified by the pension scheme actuary, in accordance with the pension scheme rules.
[7] Any scheme investment management expenses which are charged separately or have not been implicitly allowed for, under change in market value of investments or as a deduction from investment income.
[8] The cash costs paid, directly or indirectly, by the sponsoring employer(s) or pension scheme (in respect of the transmission/distribution business) to the Pension Protection Fund.
[9] Costs of (a) hedging certain risk in a pension scheme (e.g. longevity, interest and RPI); and (b) a sponsoring employer funding a contingent asset provided to the pension scheme, incurred directly by the employer.
[10] Cost associated with the provision of additional benefits offered to members of a DB scheme (other than enhanced pension benefits granted under severance arrangements), normally where the cost is borne by the scheme and/or the employer.
[11] The cost of providing enhanced pension benefits granted under severance arrangements.
[12] ‘Northern Ireland Electricity Pension Scheme (The Scheme): Recovery Plan.’

This Annex summarises our analysis of pension deficit elements of NIE Networks' pension scheme, with respect to the RP7 Price Control. It also reviews pension costs for RP6 to determine whether any adjustment of allowances is required.

In conducting this analysis, we have considered the findings from the RP5 CC (Competition Commission) (now the CMA)[13] determination on the treatment of pension costs, regulatory precedents and other relevant material.

Document Structure

The structure of this document is set out below:

- Chapter 1 - Pensions Background – background details on RP6 and RP7.
- Chapter 2 - This section discusses the Investment strategy.
- Chapter 3 - Defined Contribution Scheme, analysis on costs relating to the DC section of NIE Networks' pension scheme.
- Chapter 4 - Defined Benefit Scheme, analysis on costs relating to the DB section of NIE Networks' pension scheme.
- Chapter 5 - Pension Scheme Expenses – analysis of pension scheme administration and expenses costs.
- Chapter 6 - Provides details of UR's Final allowances in relation to pensions.

We also provide, in addition to the information contained in this document, a summary of the findings of our pension analysis in the RP7 Final Determination main document.

[13] Competition Commission: Northern Ireland Electricity Limited price determination, Final Determination, 26 March 2014.

1. RP6 Pensions and NIE Networks' RP7 business plan

Pension principles

1.1 In this price control, we are applying principles to pension deficits and ongoing contributions. Below is a summary of the development of these principles:

1.2 In our RP5 Draft Determination, we proposed a number of principles for the consideration of pension costs[14]:

"The principles that we will adopt going forward are as follows:

NIE Transmission and Distribution (T&D) should be allowed to recover the efficient ongoing pension costs for employees who are members of either the DB pension scheme or the DC scheme.

NIE T&D should be allowed to recover any deficit repair costs, associated with the DB pension scheme for both NIE T&D and NIE Powerteam Ltd, which it cannot legally avoid.

Customers will achieve the benefit of any surplus which may exist during future price controls.

Pension scheme trustees have a legal obligation to manage the pension fund prudently and in accordance with good investment principles and actuarial practice. Assuming that these legal obligations are complied with, there is little opportunity for NIE T&D to achieve efficiencies in the way it manages the DB scheme, other than by closing the scheme to new members.

Pension deficits that occur in any price control period may have been influenced by avoidable or inefficient actions taken in previous price control periods. We will adjust for the impact of unfunded ERDCs.

Pension deficits will be based on the most recent formal actuarial valuation."[15]

1.3 On 30 April 2013 the RP5 Price Control Determination was referred to the CC). The CC ruled that the treatment of pension deficits as part of the RP5 Price Control should be consistent with Ofgem's treatment of pension deficits

[14] See Utility Regulator: Northern Ireland Electricity Transmission and Distribution Price Controls 2012-2017, Draft Determination, 19 April 2012, Paragraph 11.8.
[15] Utility Regulator: Northern Ireland Electricity Transmission and Distribution Price Controls 2012-2017, Final Determination, 23 October 2012, Paragraph 7.56.

of distribution businesses in Great Britain (GB)[16] .

1.4 Following-on from the CC Determination, we published, in December 2014, a regulatory decision paper on pension deficit recovery, in which we stated that it was correct to ensure each price control followed the same core principles[17].

1.5 We stated in our final approach for the RP6 Price Control, published in December 2015, the following: '[... we] consider that the pension principles we apply in setting pension-related price control allowances should be consistent across all NI regulated energy businesses with DB schemes as well as, in so far as reasonable and practical, also with the pension principles used by Ofgem. [...] For RP6, we therefore proposed to build on the pension principles used as part of RP5. We may consider reviewing our pension principles in the future as part of a roll-out and alignment of pension principles across all NI regulated energy businesses with DB schemes[18]. This was restated in the RP6 Final Determination.

1.6 In our 'NIE Networks RP7 Price Control: Our Approach' document, we commented that, "For RP7, we intend to continue to apply the principles developed for RP6 to pension deficits and ongoing contributions:

- costs of the DC pension scheme will be covered by benchmarking.

- we will take account of the current scheme funding, based on the latest actuarial valuation of the scheme, using the Technical Approach method and take into consideration the current treatment by Ofgem on this area, including deficits and the funding implications that will result from this. In particular, we will continue to apply the principle that the "established deficit" which represents the difference between assets and liabilities attributable to pensionable service up to 31 March 2012 will be 100% funded by consumers, subject to an Early Retirement Deficit Contributions (ERDC) liability factor which reflects historical decisions by NIE Networks on enhancement to pension benefits with no additional funding when the scheme was in surplus[19]."

1.7 In setting allowances for RP7, we will consider our precedents, the CC determination for RP5, the RP6 determination and other relevant regulatory

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[16] See Competition Commission: Northern Ireland Electricity Limited price determination, Final Determination, 26 March 2014, Paragraph 12.80.
[17] See Utility Regulator: Pension Deficit Recovery – A Utility Regulator Position Paper, December 2014, p. 4.
[18] Utility Regulator: Northern Ireland Electricity Networks Ltd Transmission & Distribution 6th Price Control (RP6), Final Overall Approach, December 2015, Paragraphs 128 and 129.
[19] Utility Regulator, 'NIE Networks RP7 Price Control: Our Approach: July 2022'.

precedents.

Consideration of pension cost elements

1.8 As part of setting total revenues, we consider the treatment of pension costs and the elements of costs therein.

1.9 Both the DC and DB sections of the pension scheme have:

- Normal ongoing pension service contributions; and
- Pension scheme administration cost and investment management fees.

1.10 In addition, there may be a range of other costs specific to the DB section of the scheme, including:

- Pension deficit repair payments.
- Pension Protection Fund (PPF) Levies.
- Pension hedging and contingent asset cost.
- Augmentation of benefit cost.
- Pension-related severance cost.

1.11 NIE Networks calculated the total pension deficit contributions expected to be payable during RP6 as £114.5million, ignoring the ERDC adjustment of £30.5million. NIE Networks requested a net allowance for pensions of £84million for RP6. In its response to a UR query NIE Networks stated that it considered that current contributions would be insufficient to reduce the deficit at September 2016 (of £262.8million) by 2022, and that it considered that the recovery plan would continue beyond 2022, but at higher levels.

1.12 Employer contributions for the Focus section of the NIEPS are higher than those for the Options Section. Total employer contributions to the Focus section were just over £26 million in 2021 and nearly £27 million in 2022. Employer contributions were just over £6 million in 2021 and 2022 for the Options section. The ongoing costs of the Focus section was 43% of pensionable salary - for 1 April 2022 to 31 March 2023, “plus additional amounts of £87,500 each month to cover the costs of meeting Scheme expenses.” From 1 April 2023, this would be 52.1% of Pensionable Salary, “plus additional amounts of £100,000 each month to cover the costs of meeting Scheme expenses.” By comparison, for the Options section, employers would pay “contributions matching the members’ normal contributions (as described above) plus 6.4% of Pensionable Salaries,” from

1 April 2022 to 31 March 2023. From 1 April 2023, this would be 6.6% of Pensionable salary[20].

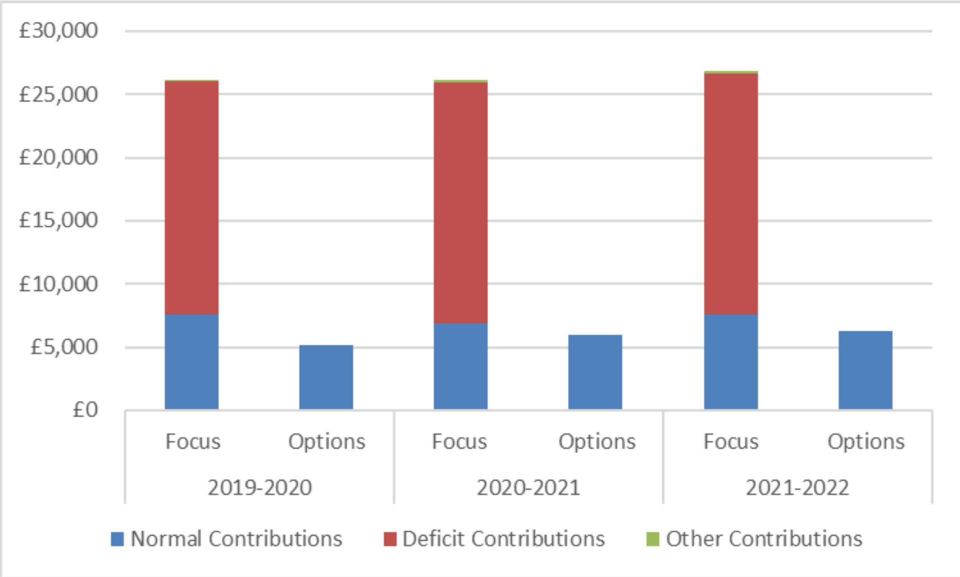


Figure 1.1: Employer contributions in the NIEPS From 31 March 2019 to 31 March 2022[21]

1.13 Ongoing pension costs are treated differently to the pension deficit recovery allowances. UR's consideration of deficit recovery allowances is included in this Annex.

Pension cost review

1.14 We recognise that the treatment of pension costs is an important area, with implications for energy consumers and a number of stakeholder groups.

1.15 A pension deficit typically arises from the DB section of the pension scheme. A deficit is the amount by which the present value of the pension fund liabilities exceeds the value of the assets. Deficits can generally arise from lower-than-expected investment returns and people living longer.

1.16 The Electricity (Protected Persons) Pensions Regulations (Northern Ireland) 1992 protect employees' pension benefits in respect of past and future service (the protection applying to members who joined the NIEPS pre-1992). As benefit protections apply to over 98% of deferred and pensioner members, the scope to vary the NIEPS's benefits, and member contribution rates is limited.

1.17 Deficit repair payments are cash amounts, agreed with the pension scheme

[20] 'Northern Ireland Electricity Pension Scheme (The Scheme): Schedule of Contributions, Actuarial Valuation as at 31 March 2022.'
[21] GAD Review.

trustees, paid by the company to reduce a pension fund deficit.

1.18 In analysing pensions, we reviewed recent regulatory precedent, and also commissioned the Government Actuary's Department (GAD) to provide specialist expertise.

1.19 In determining price control allowances, we will consider:

- Deficit treatment, including:
    - ♦ the appropriate deficit amount to be considered;
    - ♦ a deficit recovery period;
    - ♦ a regulatory fraction which can be applied to NIE Networks to ensure that consumers only fund the element of pension costs which apply to the regulated entity; and
    - ♦ any disallowance to be attributed to the employers' contribution in respect of the ERDC.
- The treatment of ongoing contributions.

NIE Networks' business plan submission for deficit recovery payments

1.20 NIE Networks requested allowances in relation to pension deficit recovery payments in the Business Plan submitted to UR, that have then been updated based on the Pensions BPT and latest inflation indices. The requests are shown in Table 6.1 below.

1.21 The pension deficit recovery allowance was reduced for RP6 due to the Employer Recovery Deficit Contribution. This is the amount of deficit recovery assumed to be attributed to the Employer. The CC, when looking at the allowance for RP5, had specified that 30% of the ERDC should be disallowed (based on a possible range of 23-45%).

1.22 NIE Networks noted in its RP7 submission to us that "Pension Deficit Repair costs are £19.3m in excess of allowances. This is mainly due to the ERDC disallowance included as part of RP6." ERDC disallowance was average £4.3 million per annum during RP6 and is forecast to be average £1.4 million per annum during RP7 (Distribution), and average £1.3 million (RP6) and £0.4 million (RP7) for Transmission.

1.23 In assessing RP7 allowances we will consider whether the previous approach to ERDC disallowance is still relevant, and whether it should be retained.

1.24 In analysing the amounts requested, we must determine the appropriate split of the requested allowances between the transmission and distribution sections of the Business.

1.25 In the Business Plan, NIE Networks requested amounts for the Transmission and Distribution sections of the business as shown in Table 6.3 and Table 6.4 below. The splits used by NIE Networks for cost allocation between the Transmission and Distribution businesses is shown in Table 6.2 below.

1.26 Deficit contributions of c.£19-20 million a year were paid over the period 31 March 2020 to 30 September 2023. No further deficit contributions are due to be paid to the scheme; however, it is possible that further contributions may need to be paid in the future – this will depend on scheme experience. We note that the only request for Pension Deficit Repair Payments is concentrated in the first year of the RP7 period (2025/26, -£15.8 million Distribution and -£4.7 million Transmission).

1.27 NIE Networks has requested that a re-opener be included as part of RP7 should any deficit contributions arise beyond 30 June 2026 (when the results of the next funding valuation are due). Under the RP6 framework, the Company can request engagement with us if an increase in the deficit leads to a funding ratio below a certain threshold. The threshold funding ratio set at RP6 was 75%, and NIE Networks has proposed that there is no funding ratio threshold in any future re-opener and allowances for pensions are reviewed in line with each Triennial Valuation.

1.28 At this point we do not consider this approach is necessary, but we will seek further views from stakeholders on this question.

1.29 The deficit is forecasted to be cleared by September 2023, with the allowances forecasted to be fully settled by 2026/27. NIE Networks' tables in its submitted Business Plan make a revenue request of -£15.8 million (Distribution) and -£4.7 million (Transmission) for 2025/26 for pension deficit repair payments (£20.5 million in total). No further request is made for the remaining period of RP7. This request amounts to a split of 22.9%/77.1% (Transmission/Distribution)[22].

1.30 Note that for RP6, as is noted in NIE Networks' Business Plan submission, it is stated that Pension Deficit Repair costs are £19.6 million in excess of allowances – "mainly due to the ERDC disallowance included as part of RP6." (The actual value from October 2017 – March 2022 being £77.4 million)[23]. We note that for RP7, there is no amount requested for ERDC

[22] rp7-business-plan-full-report-april-2023.aspx (nienetworks.co.uk)
[23] NIE Networks, 'NIE Networks Limited Business Plan: 1 April 2025 to 31 March 2031: All Submission Pdf Files, P.4522.'

disallowance (compared to a £30 million request for RP6), and the pension deficit contribution total is significantly lower than that requested for RP6, meaning the utility of detailed comparison to RP6 figures is limited.

1.31 In determining pension costs, we have analysed a range of material: Scheme Actuary actuarial valuation reports and funding updates, trustees' annual report and accounts, Focus and Options members' booklets, statement of investment principles, statement of funding principles, NIE Networks' business plan submissions, other publicly available pension information, and approaches taken by other regulators including Ofgem.

1.32 It is a legal requirement that triennial actuarial valuations are carried out by occupational pension schemes. Since price controls last over three years, this causes issues in implementing the price control using up-to-date actuarial results. During a price control period, a more up-to-date actuarial valuation will be completed, which may report differing results from the previous valuation.

1.33 Accordingly, it can be expected that actual pension costs incurred by NIE Networks will vary from those anticipated at the beginning of a price control review, following the completion of funding valuations during the price control review period. The effect can work in either direction; actual (deficit) funding costs may reduce if scheme experience is more favourable than expected, or costs can increase if scheme experience is poor.

1.34 Due to fluctuations, including deficits over time, we will consider triennial valuation reports from 2017, 2020 and 2022 while also considering updated valuation reports. We will also consider the latest valuation reports available.

1.35 Actuarial valuations represent a snapshot of the NIEPS's funding position at a point in time. Changes in market conditions, actuarial assumptions and other factors affect the funding position over time. We have also considered the implications of events since March 2022 on the future pension contributions of NIE Networks.

1.36 We will monitor pension costs as part of the ongoing price control monitoring processes, and we expect to receive triennial pension valuations from the company. We will also be vigilant to other relevant factors in the pension environment (e.g. legislation changes or relevant changes) that may occur during a price control.

1.37 In general, the main financial and demographic assumptions adopted for the 2020 and 2022 funding valuations of the NIEPS are within a broadly reasonable range and we do not consider the margins for prudence reflected in the discount rate assumptions to be overly excessive (recognising the scheme's circumstances).

Methodology

1.38 During RP5, one of the decisions involved basing price control allowances on a similar approach to that used by Ofgem, by adopting its Pension Deficit Allocation Methodology (PDAM) framework. This approach was retained for RP6 and is also maintained for RP7.

1.39 NIE Networks completed the PDAM with its business plan submission. The PDAM approach involves the creation of two subfunds; one in respect of benefit accrual up to 31 March 2012 (the "cut-off date") and one for benefit accrual after the cut-off date. Shareholders are fully responsible for any deficits emerging in the post cut-off date subfund (referred to as the "incremental deficit"), whilst consumers effectively guarantee any deficits emerging in the pre-cut-off date subfund (referred to as the "established deficit").

1.40 NIE Networks has commented in its submission to us that "the current Triennial Valuation agreed between the Trustees and the Company proposes that the historic deficit will be fully addressed before the start of RP7. Accordingly, the ex-ante allowance we are currently seeking through the RP7 Price Control is zero. However, the deficit can move significantly due to factors outside the control of the Trustees, and it may be required that a deficit can move significantly due to factors outside the control of the Trustees, and it may be required that a deficit will arise in the future that will need to be funded by the Company."

1.41 NIE Networks has proposed that a re-opener is included during RP7, and that there be no funding ratio threshold in any future re-opener. NIE Networks has proposed allowances for Pensions are reviewed in line with each Triennial Valuation.

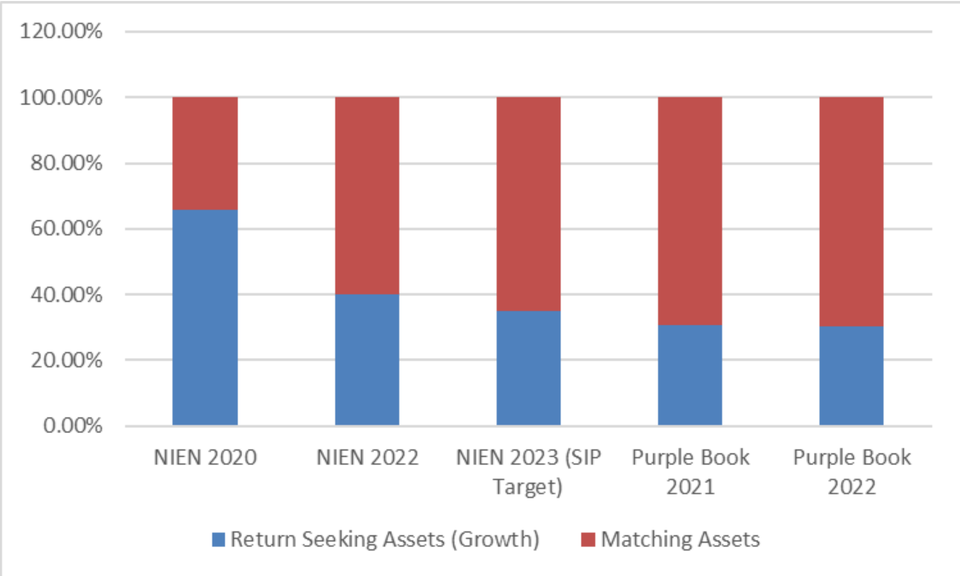
1.42 At this point we do not consider either of these proposed measures is necessary.

1.43 Our review indicates that contributions during RP6 (and RP5) have been payable as expected, in line with the schedule of contributions and therefore we do not believe that any adjustments are required in respect of contributions for service accrual or deficit recovery, which account for the majority of NIE Networks' RP6 contributions. Therefore, we have decided not to make any adjustment in respect of RP6 (or RP5).

2. Investment Strategy

2.1 The current benchmark investment strategy (effective July 2023) is as follows:

- Invest 35% of the scheme's assets in return-seeking funds such as equity (10%), absolute return funds (5%) and private assets (20%);
- Invest 25% in corporate bonds, and 40% in a Liability Driven Investment (LDI) portfolio (i.e., 65% in matching assets).



Source GAD Interim Report Sent to UR (2023).

Figure 2.1: NIEPS' investments (from valuation reports and funding updates, at market value) and average allocation for UK private sector DB schemes (from the Purple Book) – percentage of assets

2.2 Figure 2.1 shows investments in assets designed to match liabilities for the NIEPS. We understand there is an objective to "de-risk" the scheme over the longer term by reducing the allocation to return-seeking assets and increasing the level of matching assets. This approach is typical of recent developments seen more generally for DB UK pension schemes.

2.3 The Purple Book reports that around 30% of UK private sector DB schemes' assets by market value was invested in return-seeking assets (including equities, property and hedge funds), on average, in 2021 and 2022. The NIEPS is targeting full funding on a more prudent measure of liabilities over an agreed period of time, with the intention of reducing investment risk as the return required to reach this objective falls i.e. over time we would expect to see the proportion of return-seeking assets reduce and the proportion of matching assets increase.

2.4 Figure 2.1 suggests that the average UK scheme with a similar membership profile would have about 30% of its assets invested in return-seeking assets. Therefore, the NIEPS's allocation of 35% (updated 2023 figure, from its current benchmark investment strategy, effective July 2023) to return-seeking assets is slightly higher than average after allowing for scheme maturity.

2.5 Overall, the current NIEPS asset allocation – recognising that the NIEPS is a mature scheme with a strong employer covenant – does not appear unreasonable when compared to data covering other UK schemes.

2.6 NIE Networks confirmed that since the 2022 valuation, the Trustee has slightly reduced the amount of return-seeking assets and increased the level of matching assets. This would typically have the overall impact of reducing the overall return on the pension scheme's assets and therefore more money is required upfront to meet the funding targets; however, NIE Networks has confirmed that the overall return was not materially lower following the change in asset allocation.

2.7 If the scheme has a large enough surplus, then no additional deficit contributions would be required. It is expected to be another 3 years until the next valuation, and all else being equal, it could be expected that the funding level will improve over time. It is expected to be another 3 years until the next valuation.

2.8 The changes in asset allocation could reduce the risk of large deficits emerging in future, which could be in the interest of the consumer. This reflects the behaviour of most private sector DB pension schemes over time.

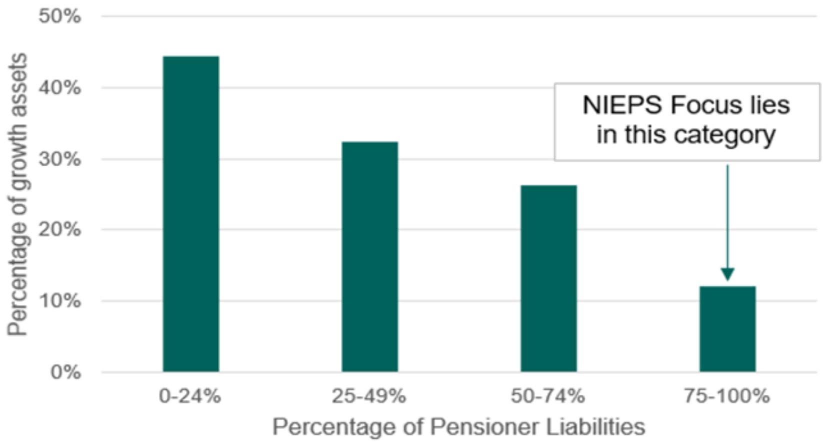
2.9 We also note NIE Networks' comments in response to a query from us concerning the rationale for updating the funding principles and level of prudence. NIE Networks said that the Trustees' initial proposals for the assumptions were intended to be a best estimate, other than for the discount rate. At the March 2022 valuation, the assumptions were updated where there was supporting evidence, such as for post-retirement mortality. The structure of the CPI/RPI differential was updated to reflect the change in Aon's best estimate view of long-term inflation. The derivation of the pre-retirement and post-retirement discount rate assumptions were updated from the levels agreed for the 2017 and 2020 valuation. It had been assessed that the assumptions in previous valuations were high compared to other schemes.

2.10 In response to a query from us concerning the valuation assumption reports during the 2020 and 2022 valuations, and the level of prudence included in the individual assumptions, NIE Networks responded that these reports were prepared by the Scheme Actuary, and the Company did not have access to these reports. The Trustees have confirmed to the Company that all assumptions are set out as best estimates other than the discount rate and understand that the post-retirement mortality best estimate base table assumptions were derived using Aon's 'Demographic Horizons' scheme specific postcode and experience analysis model.

2.11 We also asked NIE Networks if the Company had explored alternative methods to limit the future service cost impact (cost of accrual and the employer's contribution rate). The Company had concluded the approach was reasonable.

2.12 The updated investment strategy, with the reduction in the proportion of LDI and Corporate Bonds, was described by NIE Networks as a decision to reduce risk within the Scheme's investments, involving a reduction in the Scheme's target absolute return allocation and a re-organisation of the Scheme's 'matching' assets. The 2023 SIP shows what NIE Networks calls a "subtle difference between the strategic allocation in RP7 submission and the 2023 SIP, with the latter showing a 5% bias toward LDI and away from corporate bonds."

2.13 The 2022 Purple Book illustrates the relationship between investment strategy and scheme maturity, using the percentage of a scheme's liabilities attributable to current pensioners as a proxy for scheme maturity. Figure 2.2 shows approximate figures, based on the 2022 Purple Book:



*This increase is due to one large scheme which has shifted a lot of its assets into annuities.

Figure 2.2: UK private sector DB pension scheme average investment in return-seeking assets – by percentage of liabilities attributable to current pensioners – percentage of assets

Pension scheme funding

2.14 We note funding updates are not used to set contributory requirements and do not fully reflect all the considerations of a formal actuarial valuation.

Using the latest full actuarial valuation represents the most robust assessment of the scheme.

2.15 In response to a query from UR, asking if NIE Networks expected to have an approximate funding position available at 31 December 2022 (or 31 March 2023), NIE Networks understood this was expected to be received later in 2023.

	31 March 2014	31 March 2017	31 March 2020	31 March 2022
Funding:				
Assets	997.3	1,122.5	1,050.3	1,196.8
Liabilities	(1,104.4)	(1,259.4)	(1,250.8)	(1,225.8)
Surplus/(Deficit)	(110.7)	(136.9)	(200.5)	(29.0)
Funding Ratio %	90%	89%	84%	98%
Typical GB Funding Ratio %	85%	Unavailable	91.4% (Pensions regulator 2021 report)	88.8%[24]
Typical GB recovery period for schemes in deficit	8.5 Years	Unavailable	5 Years (Pensions Regulator 2021 Report[25])	Unavailable

Table 2.1: NIE Networks' pension scheme data and comparison with GB pension schemes (£m).

2.16 2022 Data from the Pensions Regulator shows the spread of funding ratios for pension schemes.

2.17 Table 2.2 illustrates the membership of NIE Networks' pension scheme as at 31 March 2022:

Scheme Section	Defined Benefit membership (Focus)
Activates	213
Deferred pensioners	350
Pensioners and dependants	3,978
Total	4,541

Note 1. Figures may not sum due to rounding.

Table 2.2: NIE Networks' pension scheme membership breakdown as at 31 March 2022 – Source: Northern Ireland Electricity Pension Scheme: Annual Report & Accounts, Year Ended 31 March 2022

[24] DB defined benefit hybrid scheme funding analysis 2022 | The Pensions Regulator
[25] DB defined benefit hybrid scheme funding analysis 2021 | The Pensions Regulator

2.18 As can be seen from the tables above- at a high level:

- The NIEPS is a large scheme (liabilities exceeding £1billion), which is now relatively mature as the scheme was closed to new members in 1998.

- The reported funding ratio for similarly mature schemes is broadly in line with schemes of similar maturity.

De-risking strategies

2.19 A key feature of the scheme's investment strategy is a long-term objective to de-risk, reducing the allocation to return-seeking assets and increase the level of matching assets. Matching assets are expected to move broadly in line with changes (up or down) in the value of the liabilities. However, as these assets are considered lower risk, the expectation is that returns will be lower – over the long term – than returns earned on higher risk asset classes (for example, equities).

2.20 All schemes have regard to the level of matching assets which their trustees believe is appropriate. The NIEPS makes use of liability-driven investment (LDI) strategies to manage its exposure to risks such as interest rates and inflation. This is consistent with general market practice for larger-sized schemes[26]. We would expect NIE Networks will have fully considered different strategies before setting an approach to its investment strategy.

Other considerations

2.21 The percentage of the NIEPS's assets by market value invested in return-seeking assets partially reflects changes in market conditions over time. It is therefore not appropriate to place undue weight on the investment allocation at any certain date.

2.22 One key consideration for the trustees is the financial strength of the sponsoring employer (the employer's covenant). A stronger employer covenant could support greater investment in return-seeking assets, due to the likelihood of the employer being able to meet any future deficits caused by investment losses. NIE Networks has stated that the NIEPS's trustees' view of its covenant is "tending to strong". The NIEPS's level of investment in return-seeking assets should be viewed in this context. All else being equal, schemes with a strong employer covenant are typically able to accept more risk in its investment strategies, which is ultimately expected to reduce the cost of providing benefits over the long-term. However, higher anticipated

[26] For example, Chart 31 in Aon Hewitt's Global Pension Risk Survey 2021 UK survey findings, shows that less than 8% of schemes had interest rate and inflation hedge ratios lower than 40%.

returns are associated with increased volatility in asset values (and potentially funding outcomes).

3. Defined Contribution Scheme

Overview

3.1 The DB section (Focus) of the scheme closed in 1998 and was replaced with a DC arrangement entitled Options for new entrants. This was consistent with pension progression trends at that time. The DC section of the NIEPS is fairly typical of a DC arrangement.

3.2 DC arrangements typically involve lower employer pension contributions than a DB pension, although this is dependent on the design of the two schemes.

3.3 In a DB scheme the employer bears the risk of adverse future experience through the possibility of deficiency contributions being required, whereas in a DC arrangement the risk of adverse future experience rests with the member through lower-than-expected benefits. These effects will increase over time as more entrants join the DC section rather than the DB section. Conversely, members benefit from favourable experience in a DC arrangement, whereas in a DB scheme the employer may benefit (depending on the scheme rules). DC arrangements are expected to reduce overall pension costs over time as more entrants join.

3.4 The employer contribution rates available in the NIEPS's DC section (Options) is slightly less generous than average, but still within the range of contribution rates typically paid into private sector DC schemes in the UK.

Normal ongoing pension contributions

3.5 Figure 3.1 shows the range of member contribution rates payable by NIE Networks into the DC section, including the minimum rate, the average rate at the time of the 2022 valuation and the maximum rate (for a member who personally contributes each year at least 8% of pay and is eligible for the extra contributions to long service):

3.6 Aon's 2022 DC Pension Scheme survey[27] suggests that the average default pension contribution rates are 6% from employers and 4% from employees and therefore NIE Networks' average default contribution rate, paid by employers and employees are broadly in line with the average default rate.

3.7 The minimum contribution rate for NIE Networks' Options scheme is 4.5% a year for employees and employers will also match the contributions and pay

[27] Better-Outcomes-By-Design-2022-DC-Pension-Scheme-and-Financial-Wellbeing-Survey.pdf.aspx (aon.com)

4.5% a year, a combined total of 9% a year. This is above the statutory minimum auto-enrolment requirement of 8% a year.

3.8 The survey concludes that there is a wide range of minimum and maximum contribution rates made available by employers of private sector schemes. Minimum contribution rates typically fall between 4% to 9% a year. Maximum contribution rates range from 6% to 16% for most schemes. NIE Networks falls towards the lower end of this contribution rate band offered by employers, but still within range of an “average” private sector scheme i.e., between the 10th and 25th percentile of schemes surveyed. As seen in Figure 3.1, NIE Networks’ average contribution rate is slightly below the private sector average.

3.9 NIE Networks’ future contributions to the DC section are expected to be more certain than those to the DB section. In the DC section, the contribution rates (not the level of benefits) are specified in the scheme rules (other than for some death and ill-health benefits). The employer risk of future funding shortfalls applies only to the DB section.

3.10 NIE Networks’ contributions to the DC section, Options, depend on the following factors:

- The contribution rates specified in the scheme rules;
- The rates at which scheme members elect to contribute (because NIE Networks matches member contributions up to 8% of pay);
- The payroll of scheme members; and
- NIE Networks’ contributions for death and ill-health benefits (which are not met entirely by members’ pension accounts), and to meet administration expenses.

3.11 Employees in the DC section of the NIEPS can choose how much to contribute, subject to a minimum contribution of 4.5% of pay. NIE Networks matches the employee's contributions up to 8% of pay and contributes an additional 1% of pay for employees with over ten years’ service, with an extra 1% of pay for employees with over 15 years’ service, a further 1% increase for employees reaching 20 years service, and a further 1% upon employees reaching 25 years of service, introduced from 1 January 2015. NIE Networks pays further contributions in respect of the cost of death in service insurance, ill health benefits and Options expenses (estimated at 6.6% of Pensionable Salaries from 1 April 2023)[28].

[28] Aon, ‘Scheme Funding Report: Actuarial Valuation of the Northern Ireland Electricity Pension Scheme at 31 March 2022’.

3.12 The structure of contributions to the DC section, whereby NIE Networks matches employee contributions on a 1:1 basis up to a limit (8% of pay here), is fairly typical, with NIE Networks falling to the lower contribution rate band, but still within range of an average private sector scheme.

3.13 NIE Networks' average contribution rate to the DC section at time of the 2022 actuarial valuation was 8% of pay in respect of retirement benefits. The valuation report showed further contributions at an average of 6.2% of pay in respect of death and ill health benefits. Contributions were also paid to meet administration expenses (0.4% of pay) giving a total of 14.6% of pay as an average to be paid from 1 April 2023. This is an increase from 9.5% at the 2014 valuation.

3.14 Figure 3.1 shows the range of member contribution rates payable by NIE Networks into the DC section, including the minimum rate, the average rate at the time of the 2022 valuation and the maximum rate.

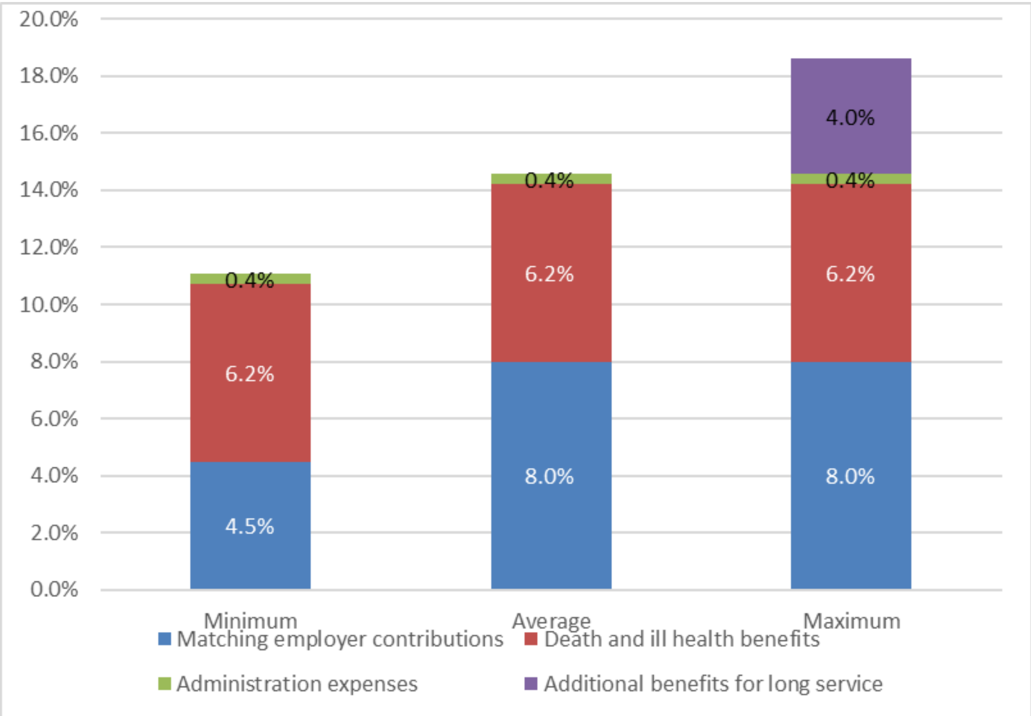


Figure 3.1: Contribution rates payable by NIE Networks in respect of the Options section on the NIEPS.

Comparing DC contribution rates

3.15 ONS survey data from 2019[29], suggests that the average employer contribution rate to private sector DC occupational pension schemes was 7.5%, for schemes of a similar size to NIEPS Options. A 2022 Aon[30] survey

[29]Occupational pension schemes in the UK - Office for National Statistics – note this data is from 2019, after which date this survey ceased to be collected.
[30] Better-Outcomes-By-Design-2022-DC-Pension-Scheme-and-Financial-Wellbeing-Survey.pdf.aspx

reported an average default contribution rate of 6% from employers.

3.16 Overall, the average employer contribution of 8% (with 6.6% for retirement benefits) paid is within the range of an average private sector scheme, but slightly towards the lower end of the band.

Options section – member choices

3.17 We note that it is cited in the Trustees Report and Accounts, that the existing Drawdown, Cash and Annuity Lifestyle strategies were closed and replaced with new versions in April 2021. These strategies employ five building block funds:

- NIEPS Growth Fund
- NIEPS Diversified Fund
- NIEPS Bond Fund
- NIEPS Annuity Tracking Fund
- NIEPS Cash Fund.

3.18 The below table shows where members' assets were invested, at 31 March 2022:

(aon.com)

Lifestyle Strategy Fund	Self-Selection Fund	£'000
NIEPS – Growth		28,603
NIEPS – Diversified		12,635
NIEPS – Bond		1,348
NIEPS – Annuity Tracking		195
NIEPS – Cash including Replacement Aegon BlackRock Cash Property		1,146
	Aegon BlackRock Diversified Growth	1,532
	Aegon BlackRock UK equity optimum	5,488
	Aegon BlackRock property	596
	Aegon BlackRock over 15 years corporate bond index	468
	Aegon BlackRock World ESG Equity Tracker	487
	Aegon BlackRock Index-linked gilt	673
	Aegon BlackRock 50:50 global equity index	5,078
	Aegon BlackRock emerging markets equity index	1,838
	Aegon Standard Life global absolute return strategies	112

Table 3.1: Investment of NIEPS Members' Assets, 31 March 2022[31]

[31] NIE Networks, 'Northern Ireland Electricity Pension Scheme: Annual Report & Accounts, Year Ended 31 March 2022.'

4. Defined Benefit Scheme

Overview

4.1 The principal benefits provided by the Focus section of the NIEPS are summarised in Figure 4.1, with the benefits offered by a 'typical' UK private sector DB scheme for comparison[32].

	NIEPS Focus Section 2022	"Typical" UK Scheme 2014
Age at which unreduced benefits are paid (NRA)	60 or 63[1]	65
Accrual rate	60ths	60ths
Dependants' pension after death of member	50%	50%
Benefits on ill-health	Enhanced pension	Enhanced pension
Lump sum on retirement	By commutation	By commutation
Member contributions (% of pay)	6%	5.2%
Pension increases (in payment)	CPI[2]	RPI/CPI with cap[3]

Source: "Typical" UK scheme: Occupational Pension Schemes Annual Report 2014 (ONS)[33]
Note 1: 63 for post-April 1988 entrants. The cost of unreduced employer-approved early retirement benefits is met by NIE Networks.
Note 2: Future NIEPS pension increases reflect Consumer Prices Index (CPI) increases. Increases above 10% are at NIE Network's discretion.
Note 3: UK private sector DB pension schemes' pension increases typically reflect increases in either the Retail Prices Index (RPI) or CPI, depending on the scheme rules. Increases are often capped at 2½% or 5% pa.

Table 4.1: NIE Networks' pension scheme benefits (Focus section).

Pension contributions and ongoing pension costs

4.2 The ongoing costs of the Focus section reflect both ongoing accrual of future service benefits for existing members and deficit contributions arising from negative scheme experience in respect of past service benefits. NIEPS's DB section's benefits have not changed since the last review, in 2017.

4.3 NIE Networks' employer Standard Contribution Rate (SCR) has significantly increased to 52.1% (from 1 April 2023) of pensionable salaries (equivalent to c.£5-6m in cash contributions).

4.4 Deficit contributions of c.£19-20m a year were paid over the period 31 March 2020 to 30 September 2023. No further deficit contributions are due to be paid into the scheme; however, it is possible that further contributions may

[32] Office for National Statistics (ONS),"Occupational Pension Schemes Survey 2014", Section 10.
[33] Note the 2014 reference has been included for comparative purposes and is still included as such, but due to the low number of DB schemes, it appears it is not possible to obtain more recent figures.

need to be paid in the future – this will depend on scheme experience.

4.5 Employer contributions for the Focus section of the NIEPS are higher than those for the Options Section. Total employer contributions to the Focus section were around £27 million during the year ended 31 March 2022, compared to employer contributions to the Options section in the region of £6 million a year over the same period. This equated to a higher percentage of pensionable salary, 43.0% of pay compared to the average of 6.4% of pay in the Options section from 1 April 2022 to 31 March 2023[34].

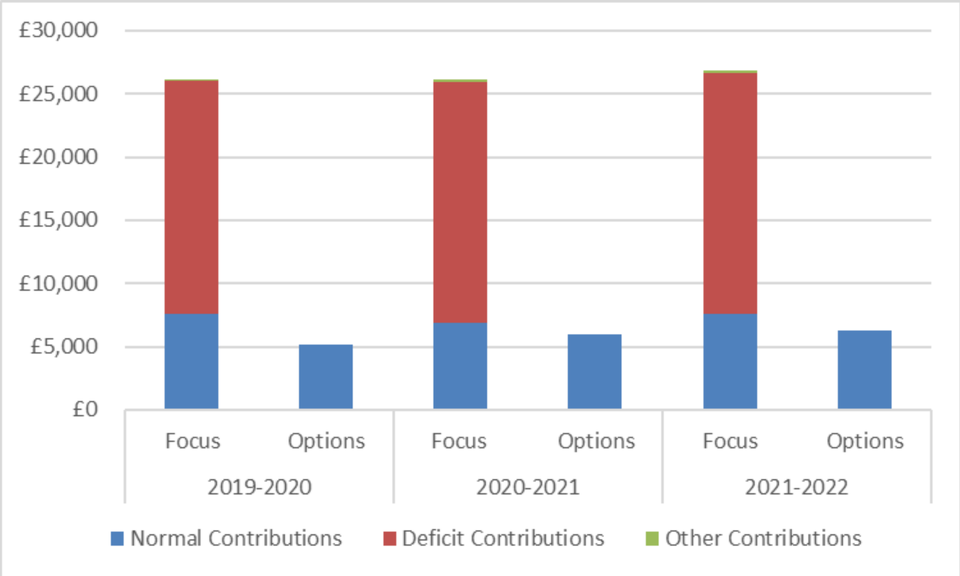


Figure 4.1: Employer contributions in the NIEPS From 31 March 2019 to 31 March 2022

Ongoing pension contributions

4.6 Ongoing pension contributions for the Focus scheme are discussed in greater detail in section 6 of this Annex.

Pension deficit

Deficit recovery and RP7 Business Plan submission

4.7 Pension schemes can be in surplus or deficit – this is measured by reference to the value of pension assets against the respective pension liabilities to produce an overall deficit or surplus. A key feature of the DB scheme is the current deficit - the most recent triennial actuarial valuation is at £29.0 million (Technical Provisions), with a £189.0 million Solvency Estimate.

[34] NIE Networks, 'Northern Ireland Electricity Pension Scheme: Annual Report & Accounts, Year Ended 31 March 2022.'

4.8 The deficit changes with movements in financial markets, level of contributions, membership changes and other assumptions. This may result in a deficit in relation to a final salary scheme which the employer will be required to address via additional contributions. By the same merit, when a fund is in surplus, an employer may take contribution holidays.

4.9 Deficit contributions of c.£19-20m a year were paid over the period 31 March 2020 to 30 September 2023. No further deficit contributions are due to be paid to the scheme; however, it is possible that further contributions may need to be paid in the future – this will depend on scheme experience.

4.10 NIE Networks has requested that a re-opener be included as part of RP7 should any “deficit” contributions, beyond 30 June 2026, which is when the results of the next funding valuation is due, arise. If “deficit” contributions beyond 30 June 2026 are to be allowed for, we will need to consider implications for future reviews.

4.11 Under the RP6 framework, the Company can request engagement with us if an increase in the deficit leads to a funding ratio below a certain threshold. However, the threshold funding ratio set at RP6 of 75% could be deemed as being low. Accordingly, NIE Networks proposes that there is no funding ratio threshold in any future re-opener and allowances for pensions are reviewed in line with each Triennial Valuation. We understand that this is the approach followed by Ofgem.

PDAM framework

4.12 Following the introduction of the PDAM Framework, the shareholders are fully responsible for any surplus or deficits established in respect of the post cut-off date subfund. This should continue to act as an incentive for NIE Networks to operate the pension scheme efficiently.

4.13 We recognise that NIE Networks’ ability to manage the established deficit in the pre-cut-off date subfund is limited due to Protected Persons legislation and the scheme’s mature membership profile. However, we still expect where appropriate, an efficient company to be exploring options to reduce, or manage, the cost of running its pension scheme.

Early Retirement Deficit Contributions

4.14 Between 1997 and 2003, when the NIEPS was in surplus, early retirement benefit enhancements were granted, increasing the scheme’s liabilities, but no additional contributions were paid into the scheme at the time. At RP6, following extensive consideration, it was decided that shareholders should fund part of these unfunded liabilities by disallowing 30% of deficit repair contributions.

4.15 It was proposed that adjustments for ERDC are to be applied in line with principles agreed at the previous reporting reviews and are not expected to give rise to significant costs.

4.16 We recognise that, in comments on our consultation on our RP7 Draft Determination, NIE Networks said the ERDC disallowance has been addressed in full, and there is no need to include an ERDC mechanism in the final determination. We note these comments and have not included an ERDC mechanism in the final determination.

Deficit recovery period

4.17 There is a deficit on the NIEPS, at the last valuation. However, this had declined since the last valuation.

4.18 At the previous valuation at 31 March 2020, there was a deficit of £200.5 million relative to the technical provisions, which corresponded to a funding level of 84%, and there was a deficit of £510.3 million relative to the solvency liabilities, which corresponded to a funding level of 67%.

4.19 The Trustees and Company agreed a recovery plan that was designed to restore the funding level to 100% by 31 March 2029 through equal monthly instalments of £19.011 million per annum from 1 April 2020 to 31 March 2029, increased each subsequent 1 April by the increase in the Retail Prices Index between the previous 1 September to 31 August period.

4.20 Figure 4.2 quantifies the key reasons for the change in the NIEPS's deficit from £200.5 million in the scheme at the previous valuation, to £29.0 million at the most recent valuation:

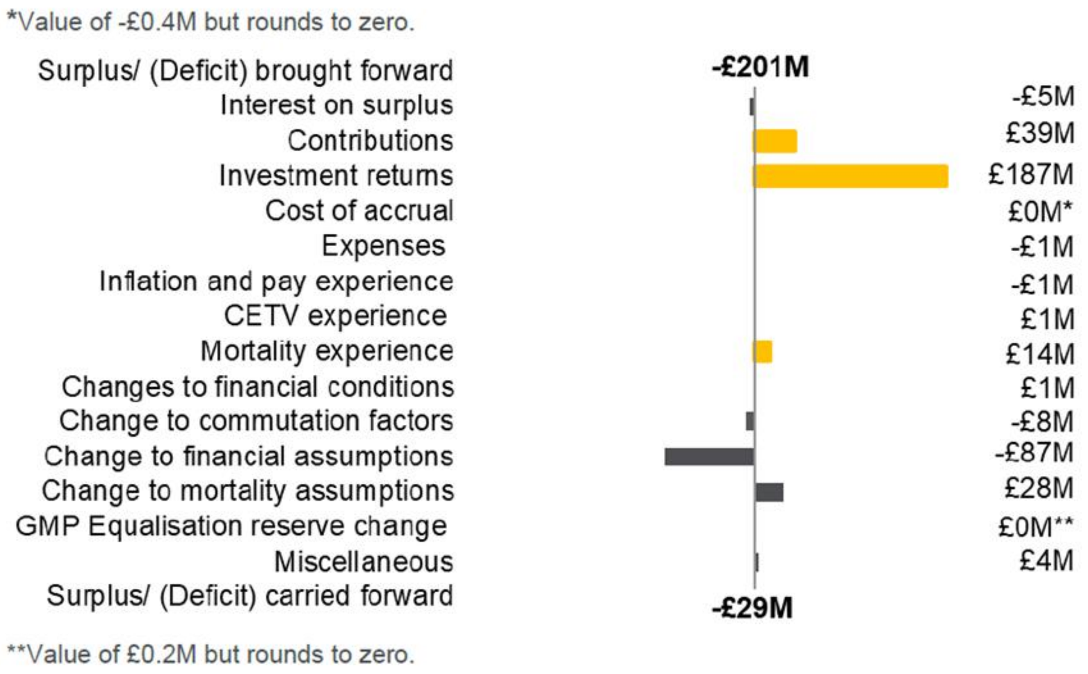


Figure 4.2: NIEPS funding valuations – change in valuation surplus (deficit) between 2020 and 2022. Source: AON, Scheme Funding Report: Actuarial Valuation of the Northern Ireland Pension Scheme at 31 March 2022.

4.21 Figure 4.2 shows that the principal reason for the decrease in the deficit between the 2020 and 2022 valuations was the higher than expected investment returns and deficit contributions paid into the scheme. This was partially offset by a change in financial market conditions.

4.22 The 2017, 2020 and 2022 funding valuations of the NIEPS used an actuarial method called the projected unit method. This is a standard method which is commonly used for funding valuations.

4.23 NIE Networks' employer SCR is high compared with other schemes and has increased significantly since the 2020 valuation. This is consistent with the NIEPS's benefits being slightly more generous than average and may also reflect the age profile of the active membership. It also reflects the lower-risk, lower-returning investment strategy compared with previous valuations and the level of prudence in the valuation assumptions:

	2017 Valuation	2020 Valuation	2022 Valuation
Employers share of SCR (% of pay)	39.6%	43.0%	52.1%
Funding level (%)	89%	84%	98%
Length of deficit recovery period	8 Years	9 Years	1.5 Years

Table 4.2: NIEPS 2017, 2020 and 2022 funding valuation results (DB section)

4.24 As the SCR only impacts a small number of active, mature members, then the cost is low overall (and is expected to decrease further over time). We note that the cost of providing these benefits is expected to have decreased since the 2022 valuation as a result of higher interest rates. Scheme trustees have a duty to monitor expenses and ensure the level incurred is reasonable. We note that paying a higher upfront cost for ongoing service contributions reduces the risk of further deficit contributions becoming payable in future.

4.25 We consider the SCR to be significantly high, and we would welcome input from stakeholders in regard to this amount. Given the lower numbers of active members, and the resultant lower impact, we are minded to allow this, but think this is significantly high.

Level of prudence in valuation results

4.26 This would need to be agreed by the Trustee and company in future valuations; however, a broad indicator of the level of prudence in the current valuation is the ratio of best estimate against funding basis. GAD have calculated that this ratio is 93% in 2017, 91% in 2020 and 91% in 2022, which is an increase in the level of prudence since the last RP6 review.

4.27 NIE Networks has confirmed the intention that all the prudence in the valuation assumptions is contained in the discount rate, although GAD have not been able to independently verify this at present, as they have not been provided with the valuation assumptions reports. It appears that the level of prudence in the discount rate assumption was increased on the basis that it appeared high compared to other schemes of similar maturity, rather than derived using consistent principles with previous valuations.

4.28 We do not know the rationale underlying the trustee’s derivation of the level of prudence in the funding basis. NIE Networks has confirmed they do not have access to the valuation assumption reports. We might expect NIE Networks to take further steps to understand the theoretical level of prudence in the assumptions before agreeing to the funding valuation basis and lower levels of prudence.

4.29 NIE Networks states they do not have an approximate funding update since the valuation at 31 March 2022, however we note that previously they appear to have been monitoring the funding position closely following the 2020 valuation, identified an improved funding position at 31 March 2022, and negotiated and carried out a full valuation by February 2023. We commented in the draft determination that it was surprising that the Company are not aware of an indicative funding position given large market changes, change of investment strategy, and the approach adopted in the previous year where the Company requested an out of cycle review.

4.30 In its consultation response to our draft determination, NIE Networks stated they receive a formal annual update from the Trustees in relation to the funding status of the Focus scheme "as at 31 March [2023], via the Scheme Actuary's annual actuarial report." NIE Networks states the 2023 update was not available "either at the time of making the RP7 submission or addressing queries raised by the UR." The funding update as at 31 March 2023 has since been received by NIE Networks, which they say "confirms that the funding level was broadly in line with the projections of the March 2022 triennial valuation." NIE Networks has also commented that it also "monitors developments in funding informally during intervening periods taking account of changes to market conditions over time."

4.31 We note the response supplied to us to a query, as to why the 31 March valuation was conducted out of cycle (rather than waiting until 31 March 2023). NIE Networks, in response, stated that the developing Covid-19 pandemic resulted in a significant pension deficit of £200million at the time of the March 2020 triennial valuation. "The associated deficit repair plan agreed with the Trustees was designed to address this deficit over the nine year period to 31 March 2029, with deficit repair contributions being retained at the same level as previous valuations." Submission of the RP7 plan had been expected to be due in October 2022, the company considered whether it was appropriate to bring forward the next valuation or use high level funding updates. The factors included:

4.32 The deficit at March 2020 was considered to be extremely high due to the impact of the pandemic on market conditions, and the funding update at 31 March 2021 indicated a significant improvement in the funding level compared to the 31 March 2020 valuation.

4.33 The Company became aware that, after submitting the 2020 valuation results, the Pensions Regulator wrote to the Trustees asking a significant number of questions about the 2020 valuation. NIE Networks did not consider an appropriate basis to use funding updates to inform the RP7 submission, as they were based on the March 2020 derivation of assumptions. "Given the expected improvement in the finding position which had emerged since 31 March 2020, a revised valuation would likely require lower deficit repair contributions and/or a shorter recovery plan which would be in the interests of consumers and also ensure a balance is maintained with the requirements of the Pensions Regulator." The Company, in response to a query from UR, stated that they did not have a copy of the correspondence between the Trustees and the Pensions Regulator regarding the 2020 valuation.

4.34 It was ultimately decided to request to bring forward the next valuation to 31 March 2022, and this resulted in a shorter deficit repair plan and lower funding request. NIE Networks consider "as the agreed recovery plan from the 2022 valuation is scheduled to conclude before the end of RP6, it is important for all parties that an appropriate flexibility mechanism is included in the RP7 Price Control should a deficit re-emerge at a later date."

4.35 In response to a query from UR, NIE Networks stated that the impact of the new investment strategy (reducing the Scheme's strategic absolute return allocation to 5%, in favour of high quality corporate bonds) was considered by the Trustees in January 2023. "It was discussed and agreed that the action proposed was not expected to materially impact the Scheme's balance of investment risk vs expected return, nor the Scheme's best estimate timeframes to reaching full funding on Technical Provisions or more 'prudent' liability measures. As such, there was no change to the Scheme's funding strategy/deficit contribution schedule as a result of this change to investment strategy."

Approach taken by other regulators

4.36 Ofgem, in previous consultations, have explored different options for pension deficit recovery periods. These have explored flexibility over the funding period, the weight given to present and future consumers, and the use of 'stop dead' dates to eliminate a deficit.

4.37 Under the RP6 framework, the Company could request engagement with us if an increase in the deficit leads to a funding ratio below a certain threshold.

4.38 NIE Networks has requested that a re-opener be included as part of RP7 should any deficit contributions beyond 30 June 2026 (when the results of the next funding valuation are due, arise). Under the RP6 framework, the Company can request engagement with us if an increase in the deficit leads to a funding ratio below a certain threshold.

4.39 However, the threshold funding ratio set at RP6 of 75% was low, and NIE Networks has proposed that there is no funding ratio threshold in any future re-opener and allowances for pensions are reviewed in line with each Triennial Valuation.

4.40 We note that NIE Networks and the Trustees of the NIEPS, in response to consultation on the draft determination, both said the existing approach should not be retained, and we should follow the Ofgem approach, which is to allow for a triennial recalibration of pension allowances following each actuarial valuation. Ofgem is currently consulting on whether to review this policy. We will take the outcome of the Ofgem review into consideration and are likely to then review our own policy on the existing approach. Before we conduct this review, we will not change the existing framework, as change in this area would impact other areas, and all areas should be considered in tandem.

NIE Networks business plan submission – deficit recovery

4.41 The deficit is forecasted to be cleared in 2026/27. The NIE Networks request is to make a revenue request of -£15.8 million (Distribution) and -£4.7 million (Transmission) for 2025/26 for pension deficit repair payments (£20.5 million in total). No further request is made for the remaining period of RP7. This request amounts to a split of 22.9%/77.1% (Transmission/Distribution)[35].

4.42 Note that for RP6, as is noted in NIE Networks' Business Plan submission, it is stated that Pension Deficit Repair costs are £19.6 million in excess of allowances – "mainly due to the ERDC disallowance included as part of RP6." (The actual value from October 2017 – March 2022 being £77.4 million)[36]. We note that for RP7, there is no amount requested for ERDC disallowance (compared to a £30 million request for RP6), and the pension deficit contribution total is significantly lower than that requested for RP6, meaning the utility of detailed comparison to RP6 figures is limited[37].

Pre and post cut-off date assets and liabilities

4.43 In the RP5 CMA Final Determination, the CC decided that with regard to the scheme deficit, in which the current scheme has insufficient assets to cover its liabilities, it was split into 2 areas:

- between an historic deficit (represents the difference between assets and liabilities attributable to pensionable service up to 31 March 2012 and 100% funded by consumers) and;
- an incremental deficit (represents the difference between assets and liabilities for pensionable service from the 1 April 2012 and 100% funded by shareholders;).

4.44 Valuation at 31 March 2020 reflected a deficit of £200.5 million relative to the Technical Provisions, and £510.3 million relative to the solvency liabilities. The Trustees and Company agreed a recovery plan designed to restore the funding level to 100% by 31 March 2029 through equal monthly instalments of £19.011 million per annum from 1 April 2020 to 31 March 2029.

4.45 Below is the comment the CMA made on this issue in the RP5 Final Determination (12.27):

"Based on our view that NIE is likely to have a limited ability to mitigate the

[35] NIE Networks. 'NIE Networks Business Plan: 1 April 2025 to 31 March 2031'.
[36] NIE Networks, 'NIE Networks Limited Business Plan: 1 April 2025 to 31 March 2031: All Submission Pdf Files, P.4522.'
[37] 'RP7 Business Plan Pensions Commentary Template: August 2022.'

historic scheme deficit, we decided that in principle (and before considering any special items) 100 per cent of historic deficit repair costs should be passed through to consumers during RP5."

4.46 This principle is similar to the one Ofgem has in place for GB DNOs, and we have decided not to change this principle.

4.47 The CC also suggested an in period adjustment Mechanism (which makes changes to the payment schedules, normally after an actuarial valuation, to reflect the scheme needs) is deferred to the start of the next price control on the basis that NIE and consumers are kept NPV neutral due to timing;

4.48 We continue to follow the CC recommendations. As part of its Business Plan submission for RP7, NIE Networks was required to complete a PDAM spreadsheet. This is based on the Ofgem methodology and demonstrates the methods used by the company to allocate the pre and post cutoff assets and liabilities.

4.49 We are continuing to retain the CMA's approach to allocating pre and post cutoff assets and liabilities and funding principles - with consumers responsible for the pre fund and shareholders for the post fund.

Update of regulatory fraction & regulatory proportion

4.50 This simplification would provide both the Company and consumers with increased certainty about the split between regulated Pre Cut-Off Deficit and other components of deficit in future.

4.51 The Regulatory Fraction is used to allocate pension costs deemed to be associated with regulated activities.

4.52 The funding allowances for RP6 incorporated an adjustment to the Regulatory Fraction to take into account the Article 75 payment made by Powerteam Electrical Services in 2013/14. The pre-adjusted Regulatory Fraction was 99.26%, which was carried over from RP5, and the post-adjusted Regulatory Fraction was 102.96%. The purpose of the adjustment was so that the surplus emerging in respect of the Article 75 payment was treated as non-regulated surplus, which then led to an increase in the RP6 allowances. This fraction is relevant for the established deficit (which covers accrued benefits up to 31 March 2012).

4.53 NIE Networks has proposed a Regulatory Fraction of 100% is adopted for RP7.

4.54 For simplification and in view of the materiality considerations, we consider accepting this regulatory fraction as 100% for RP6 and going forward. We will not make a retrospective adjustment in respect of RP6 and previous price controls since this would involve adjustment for other price control aspects, as it could not be adjusted in isolation.

Longevity

4.55 The longer a pension scheme member lives after retirement, the greater the cost of providing a DB pension. Ongoing funding valuations require an assumption regarding the assumed longevity of members and their dependants. The assumptions do not appear unreasonable compared with typical private sector schemes.

4.56 The longer a pension scheme member lives after retirement, the greater the cost of providing a DB pension. Ongoing funding valuations require an assumption regarding the assumed longevity of members and their dependants. Such assumptions should reflect the particular membership of the scheme e.g. members' industry or geographical factors and should allow for expected future improvements in longevity.

4.57 NIE Networks comments in the Statement of Funding Principles that "In setting the Scheme's funding target, mortality assumptions are made based in standard tables appropriate to comparable pension schemes with adjustments to reflect the Scheme's membership profile and recent experience. Allowance is also made for expected future improvements in longevity. The mortality assumptions are reviewed at formal triennial actuarial valuations."

4.58 The 2022 valuation of the NIEPS utilised an updated mortality experience and postcode analysis using the Aon Demographic Horizons model, and a move to using the latest CMI Projection model (CMI_2021).

4.59 The Pensions Regulator, in its 2023 Scheme Funding Analysis[38] suggest that this approach is consistent with others, as almost all schemes (95.2%) use the CMI mortality projection model when allowing for future improvements.

4.60 Like the NIEPS, 82% of schemes assumed a long-term rate of improvement/underpin of 1.5% or higher.

4.61 Overall, the allowance made for future longevity improvements do not appear unreasonable compared with typical private sector schemes.

Salary strain and inflation

4.62 NIE Networks comments that "For the 31 March 2022 actuarial valuation, and prior actuarial valuations, NIE Networks has agreed with the Trustees

[38] Scheme funding analysis 2023 | The Pensions Regulator

that allowance will be made in the technical provisions for discretionary pension increases in line with increases in price inflation should inflation exceed the maximum increase guarantee of 10% in any year under the Scheme. However, the Company retains discretion to restrict such increases to 10% in practice, and elected to do so in respect of the 2023 pension increase which will be paid at 10% (with underlying CPI inflation over the year to September 2022 being 10.1%)."

PPF levies

4.63 In addition, NIE Networks pays the NIEPS's Pension Protection Fund (PPF) levy, which the scheme is required to pay.

4.64 Whilst the PPF levy represents a relatively small proportion of the cost of financing a pension scheme, we would still expect NIE Networks to take steps to reduce the annual amount payable.

4.65 We would expect to see steps such as bespoke investment tests and deficit reductions contributions certification (DRCC) being continued in future and for the scheme to explore other ways in which the levy might be reduced (for example using asset backed contributions, which take account of contingent assets pledged to the pension scheme).

4.66 NIE Networks' submission projects the PPF levy paid directly by the employer will be circa £300,000 over the RP7 period[39].

Augmentation of benefit cost

4.67 We are not aware of any relevant augmentation of benefit costs in relation to RP7 and are not minded to make any adjustments in respect of these costs.

4.68 We note that there are figures included in the NIE Networks PDAM RP7 submission of £6 million (31 March 2017 to 31 March 2020) and £3.1 million (31 March 2014 to 31 March 2017) which are based on employer contributions in respect of augmentations.

4.69 NIE Networks has further commented that "Employer payments made towards pension strain cost relate to augmentation payments made by the Company to members at retirement. Payments were made for 5 members in year ending 31 March 2022, 5 members in year ending 31 March 2021 and 2 members in year ending 31 March 2020."

[39] NIE Networks, 'RP7 BPT Pensions Reporting Workbook.'

5. Pension Scheme Expenses

5.1 Scheme trustees have a duty to monitor expenses and ensure the level incurred is reasonable. As part of our RP6 report we suggested that we would discuss this aspect with NIE Networks to understand the reasons why expenses are above average so it can consider whether any further action is appropriate.

5.2 Additional employer contributions of £87,500 per month are payable to cover Focus administration expenses, from 1 April 2022 to 31 March 2023, increasing to £100,000 per month from 1 April 2023. We have compared the annual level of administration expenses incurred by the NIEPS between 2018 and 2022 (that is, a 5-year period broadly aligned with the RP6 period) with data published by the KGC administration survey[40], which looks at administration services only. The expenses data is classified according to scheme size to enable a more informative comparison (larger schemes are expected to have lower per member expenses charges). Accordingly, NIEPS expenses are compared with expenses incurred by schemes of a similar size; that is with very large schemes (over 5,000 members) and large schemes (between 1,000 and 5,000 members).

5.3 Figure 5.1 compares the cost per member for total administrative charges.

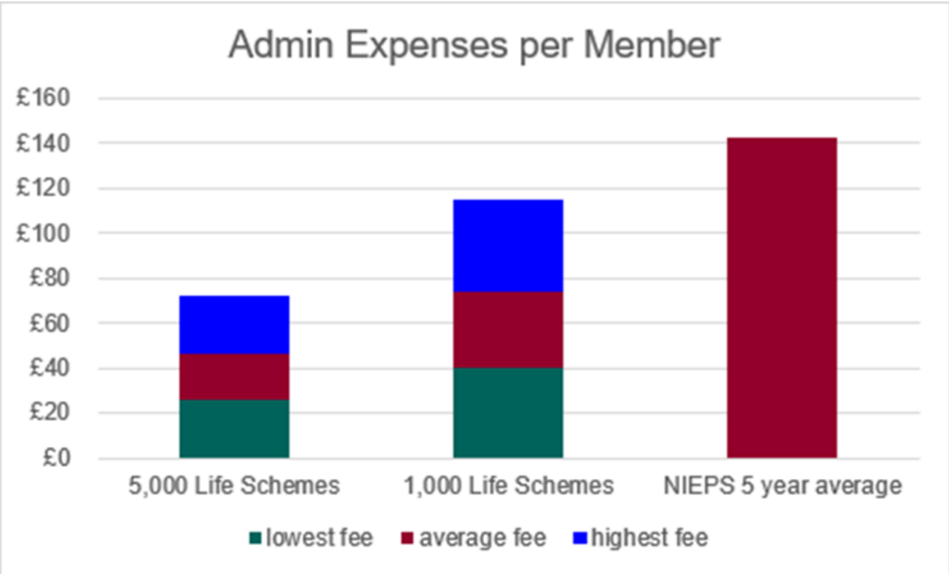


Figure 5.1: NIEPS Administrative Expenses per member

5.4 NIEPS has 4,541 members as at 31 March 2022 and therefore the direct administration expense comparison lies somewhere between the 1,000 life and 5,000 life sample size. NIEPS expense costs appear high when

40 11th-Admin-Survey-VFinal.pdf (kgcassociates.com).

compared to the sample data for schemes of similar size and even higher than the highest fee in the KGC Administration survey. The total administration fees were more comparable with the very large schemes (c.20,000).

5.5 NIE Networks in its response to the consultation on our draft determination, has noted the comments in the draft determination concerning NIEPS administration expense costs, and their high level in comparison to similar sized schemes (1,000-5,000 members). NIE Networks commented that it is difficult to compare scheme specific expenses and published surveys due to the range of factors that may be included. "It is not clear to NIE Networks how this analysis has been carried out for the draft determination. NIE Networks remains committed to monitoring scheme expenses and will engage with the Trustees as appropriate."

5.6 This assessment was included in the draft determination, after GAD had benchmarked the average annual level of expenses incurred by the NIEPS between 2018 and 2022 with data published by the Pensions Regulator in 2014 (where it was noted that NIEPS expense costs were significantly higher than the average 'large scheme' expense costs), and the KGC Administration survey (which looks at administration services only, where NIEPS expenses costs were higher than the sample data, for schemes of a similar size).

5.7 We noted in the draft determination that this was a high level exercise, requiring some simplifications, but useful to understand differences between the NIEPS and other schemes. This partially aligns with NIE Networks' comments in the consultation response, and we have retained the analysis above in this final determination. The suggested action in the draft determination was that we would, as expense costs of the NIEPS appeared high, engage further with NIE Networks to understand the reasons why. Over the RP7 period we envisage that we will have further discussions about what action is being taken in areas that may assist minimising expense costs. If there are further thoughts NIE Networks has on our analysis, these can be outlined during this engagement.

6. UR determined allowances

UR approach to setting RP7 allowances

6.1 We have considered NIE Networks' Business Plan Submission including its PDAM submission in addition to a range of other material in formulating our approach to RP7 including regulatory precedents, CMA (previously CC) RP5 decision and other relevant material. Below we summarise our decision on key pension aspects.

6.2 We note that NIE Networks has asked for changes in pensions related measures as part of RP7.

Deficit separation methodology

6.3 We have decided to continue to use the CMA methodology to allocate a deficit cutoff date of 31 March 2012. Under this methodology, the historic pre cutoff fund is designated as being the consumers responsibility and the incremental post 31 March 2012 fund is designated as being shareholders responsibility.

ERDC disallowance

6.4 We recognise the ERDC disallowance has been addressed in full during the RP6 period, and this does not need to be considered for the period of RP7.

Regulatory fraction

6.5 For simplification and in view of the materiality considerations, we proposed accepting this regulatory fraction as 100% for RP7 and going forward. We are not making a retrospective adjustment in respect of RP7 and previous price controls since this would involve adjustment for other price control aspects as it could not be adjusted in isolation.

Transmission and distribution split

6.6 We are content to apply the Transmission and Distribution splits used by NIE Networks within its Business Plan and the PDAM, and updated by inflation indices, to allocate the costs between the Transmission and Distribution elements of the business.

Methodology 2022-2024

6.7 Whilst recognising that the current funding position could worsen compared with expectations at the 2022 valuation – largely due to the performance of the scheme assets not keeping pace with the increasing value of the liabilities – fluctuations in the funding position (positive or negative) will happen in practice, and it is not certain that deficit contributions beyond 30 September 2023 will be necessary.

6.8 If the NIEPS is in deficit and it is still the consumers' responsibility, it is a matter of timing as to whether it is paid over a longer or shorter period and we must also be mindful of intergenerational equity considerations. We are mindful of the need to protect consumers and encourage the company to manage its pension scheme is an efficient a manner as possible.

6.9 For the last two years of RP6 covering the period 1 April 2022 to 31 March 2024 we are minded to allow NIE Networks the amounts proposed in its business plan.

Treatment of surpluses

6.10 We would wish NIE Networks to take appropriate action in the event of the pension scheme becoming into surplus and ensure the consumer benefits. NIE Networks should indicate to us in a timely manner that the scheme is in surplus, or they consider it will be in surplus in the foreseeable future, and accompany this with appropriate proposals to benefit the consumer.

6.11 The annual profile is as follows:

	RP7 Request
Pension Deficit Contribution	(20.5)
Pension ERDC disallowance	(0)
Net amount requested	(20.5)

Table 6.1: Total RP7 requested pension allowance (2022-23 prices) (£m)

Split by business	25/26	26/27	27/28	28/29	29/30	30/31
Transmission	22.9%	0%	0%	0%	0%	0%
Distribution	77.1%	0%	0%	0%	0%	0%

Table 6.2: Transmission and Distribution business splits

6.12 The above splits result in the following request for the Distribution and Transmission businesses.

Distribution	RP6 Average P.A.	RP7 Average P.A.	25/26	26/27	27/28	28/29	29/30
Pension deficit repair payments	11.9	-2.63	-15.8	0	0	0	0

Table 6.3: Distribution Business Plan requested amount

Transmission	RP6 Average P.A.	RP7 Average P.A.	25/26	26/27	27/28	28/29	29/30
Pension deficit repair payments	23.6	-0.78	-4.7	0	0	0	0

Table 6.4: Transmission Business Plan requested amount

6.13 These requests totalled to the amounts below in respect of the transmission and distribution sections of the business as a whole:

NIE Networks' Business Plan	RP6 Average P.A.	RP7 Average P.A.	25/26	26/27	27/28	28/29	29/30
Pension deficit repair payments	-2.63	-20.5	0	0	0	0	0

Table 6.5: NIE Networks' Transmission and Distribution total[41]

Efficiencies

6.14 We note that following the introduction of the PDAM framework, NIE Networks' interests are arguably more aligned to consumers now as its shareholders are fully responsible for any surplus or deficits in the post cut-off date subfund. However, we expect NIE Networks to continually monitor and implement mechanisms for cost savings in relation to pension scheme aspects.

6.15 In respect of the established deficit, we note that NIE Networks' ability to manage the deficit is limited due to Protected Persons legislation and the scheme's mature membership profile, however it would be reasonable to expect an efficient company to explore any opportunities to mitigate unnecessary costs by considering an increase in member contributions or reforming scheme benefits (for staff who are not subject to Protected Persons legislation).

6.16 Going forward, we expect NIE Networks to work in conjunction with its actuaries to reduce pension costs.

[41] Note these figures are based on those submitted in the NIE Networks Business Plan and may change.

7. Monitoring of Pension Scheme Funding

7.1 We are proposing that we continue with the same pensions 'trigger' framework that adopted in RP6.

7.2 Under this, NIE Networks would only approach us when it is clear that there has been a substantial fall in the NIEPS funding position at triennial valuations during RP7. A substantial fall could signal the possibility of materially higher deficit contributions.

7.3 This framework should also include an 'upside' trigger when the pension scheme funding has improved.

7.4 These proposed triggers would act as a mechanism to initiate a discussion between NIE Networks and ourselves before the end of RP7. We would not consider a simple mechanism triggering automatic actions to be appropriate as it will not fully account for changes in future circumstances. Should a trigger point be breached, any action(s) could then be taken in light of the circumstances at the time.

7.5 Whilst the application of a 'simple' trigger framework will not allow for all relevant considerations at future valuations, it is not appropriate for us to be involved in extensive valuation discussions (covering changes in assumptions, investment strategy, recovery period covenant assessment etc) during RP7 unless they are essential and not simply reactionary.

7.6 We recognise that funding a pension scheme is a long-term commitment and sponsors should not over-react to short-term fluctuations in the scheme's funding level. Further, in NIE Networks' case, any NIEPS deficit in respect of pre March 2012 accrual is fully supported by consumers, so the provision of deficit contributions would mainly be a timing point, and actual contribution payments during RP7 would be subject to review at RP8.

7.7 We also note that NIE Networks has a significant advantage over many non-regulated companies which are similarly exposed to the risk of unexpected higher costs related to legacy DB pension scheme deficits. However, such nonregulated entities will not automatically have the option of passing on higher costs to customers.

7.8 We recognise that determining trigger points may involve a degree of subjectivity; however, we will assess each application on its own merits. We have considered assessing the scheme funding level at future valuation dates (31 March 2025, 2028, and 2031) using the 2022 valuation basis (updated for market conditions, e.g. gilt yields, but maintaining the same margins for prudence) as a benchmark to assess against the trigger points. In determining whether a trigger point has been reached it is imperative that pension scheme valuations and funding levels are conducted in a consistent manner.

7.9 Trigger events should be very rare by their nature. Such events should be significant and represent a marked fall in funding levels.

7.10 We consider that a reduction in funding levels to 75% would represent a downward trigger event – however, each event will be analysed on their individual merits. By contrast, we consider a level of 105% pension scheme funding to be appropriate for an upward trigger event.

7.11 The pension funding trigger mechanism may be activated, either by the company and/or us. We will consider funding levels and pension scheme characteristics and future outlook to determine whether or not any adjustment is required to e.g., funding levels, deficit recovery payments (either up or down), bill adjustments, etc.

7.12 We recognise that NIE Networks and the Trustees of the NIEPS both wrote in their consultation responses to the draft determination that we should move to the Ofgem framework of allowing for a triennial recalibration of pension allowances following each actuarial valuation.

7.13 NIE Networks has highlighted what they believe are risks associated with the present monitoring framework, which could lead to NIE Networks having to carry excessively large deficits, up to the c.£300 million cited.

7.14 While we recognise this is a theoretical possibility, we also do not view it as a likely prospect at this stage. NIE Networks has echoed our position on the low likelihood of a deficit of this scale having to be carried, without recourse to a re-opener.

7.15 We note NIE Networks thinks the new funding code would be restrictive. However, we maintain there would be some flexibility in the regulations for NIE Networks and NIEPS to agree an appropriate valuation result and recovery plan period.

7.16 We will update the funding thresholds for a re-opener to be in line with the amounts given in the RP6 Final Determination, as suggested by NIE Networks. However, we have decided to not otherwise change the thresholds at this time. Even if the threshold was modified in the direction suggested by NIE Networks and the Trustees of the NIEPS (with the downward trigger value increased), it would still be unlikely to be triggered during the RP7 period. There are other mechanisms through which NIE Networks can, during the RP7 period, engage with us on the issue.

7.17 We note that the 31 March 2023 funding update reflects that the Scheme funding level may have a small surplus, further reducing the concern about material deficits emerging.

7.18 We note that Ofgem's current approach is to allow for a triennial recalibration of pension allowances following each actuarial valuation. Ofgem is currently consulting on whether to review this policy. We will take this into consideration and are likely to review our own policy in the near future.

Adjustment of pension scheme funding – Licence mechanism

7.19 There is a mechanism for adjusting pension scheme funding at price control reviews by considering whether any adjustment is required in respect of the pension contributions allowed at the previous price control. In addition, NIE Networks' Transmission and Distribution licences provide adjustment mechanisms which are outlined below.

Licence treatment of pension deficit

7.20 Pension deficit amounts may be adjusted via the Maximum Regulated Distributions Revenue (MRDR) in accordance with NIE Networks' licence in Annex 2. There is a separate calculation for the Maximum Regulated Transmission Revenue which is a mirror image of the MRDR but for the Transmission business.