Utility Regulator
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RP7 - NIE Networks Price Control 2025-2031

Final Determination Annex M
Incentives
30 October 2024

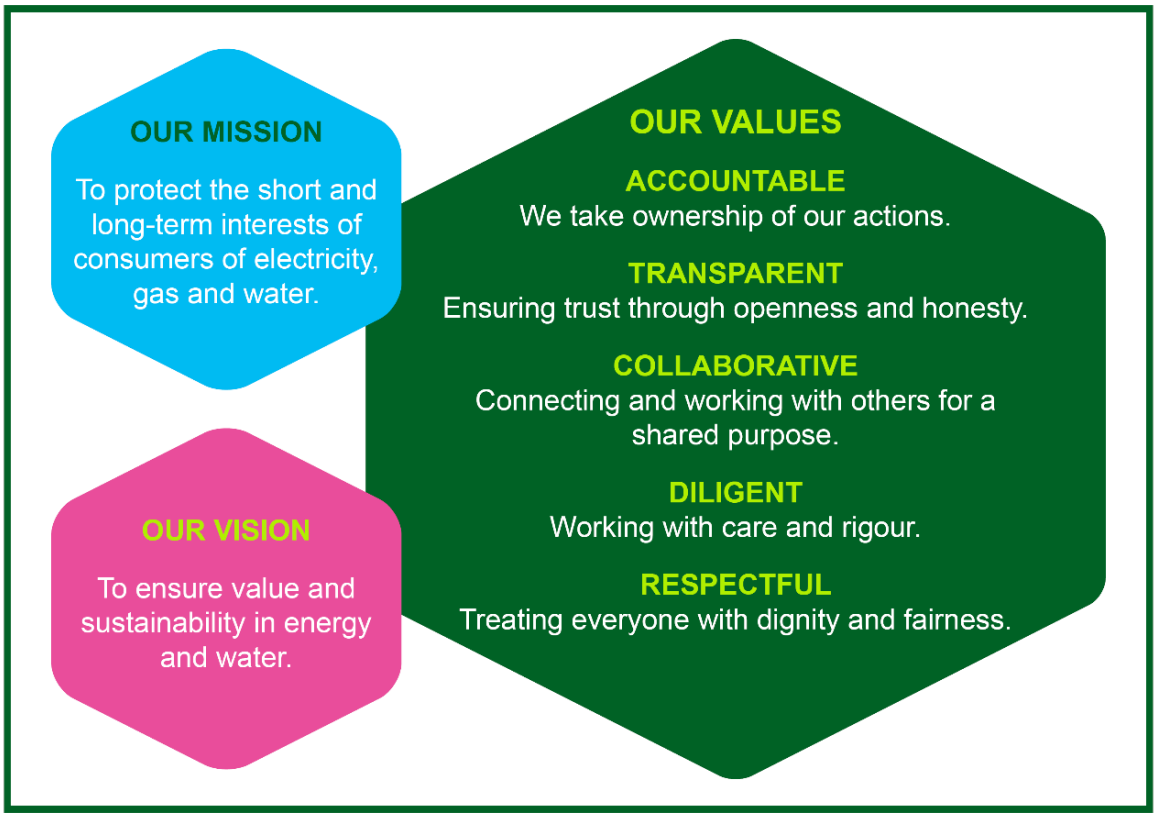
About the Utility Regulator

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.



Abstract

The objective of this annex is to explain the targets and incentives to improve performance for NIE Networks in certain key areas. The reliability incentive aims to build on improvements to customer minutes lost (CML) made in RP6.

The 50:50 cost sharing mechanism encourages efficiency whilst restraining costs and the revenue services protection incentive ensures a focus on restricting electricity theft and its impact.

We set out changes for the next price control as well as consider other issues raised by NIE Networks within its submission such as worst served customers (WSCs)

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

If implemented successfully, the incentives should improve the level of reliability and performance provided by NIE Networks to its customers in a cost-effective way.

Contents

Executive Summary

The purpose of this annex is to detail decisions on the financial incentive framework operating upon NIE Networks. Separate discussion on the Evaluative Performance Framework (EPF) is captured in Annex V.

In summary, we have determined the following changes to the reliability incentive (RI) from what currently exists in RP6:

- Move to the Ofgem methodology of setting unplanned CML targets based on fixed percentage year-on-year reductions.
- Propose a starting point using a 4-year average (and latest data) with 2% year-on-year reductions and adjustments for funded improvements.
- Amend the risk/reward exposure for unplanned and planned CML to £2.5m (2021-22 prices) per annum.
- Adjust the proportional revenue allocation to an 80:20 split (£2.0m / £0.5m) between unplanned and planned CMLs respectively.
- Update the value of lost load (VOLL) based on the latest available willingness-to-pay (WTP) research.
- Retain the planned CML metric in the RI but reduce the reward / penalty associated with it.
- Retain planned CML targets but move to a rolling 3-year average with a 2-year lag to set objectives (as per Ofgem). However, given the large capital programme increase, this mechanism has been tailored to allow some deterioration before a penalty would be incurred.
- Amendment of the unplanned customer interruption definition from one minute to three minutes, as per Great Britain approach.

For the 50:50 cost sharing mechanism, the incentive remains largely unchanged. The only difference relates to certain cost exclusions such as business rates. We also plan to retain the revenue protection service incentive unchanged from RP6.

We welcome NIE Networks proposals to address WSCs. Having initially rejected this request, we now provide full allowance. The main reason for our re-evaluation is that NIE Networks is required to carry out certain works that would not be included in the allowances for 11kV rebuild.

It is our view that the incentive mechanisms, combined with the additional WSC funding, sets the appropriate regulatory framework to encourage future improvement in customer service levels and cost efficiency.

1. Introduction

Background

1.1 The aim of this annex is to explore proposals to help incentivise NIE Networks to deliver efficiency and outstanding customer service.

1.2 In RP6 there are three financial incentive schemes that operate upon NIE Networks. These include the following:

a) Reliability Incentive (RIt licence term) – dealing with network performance in the form of both planned and unplanned CML.

b) The 50:50 cost sharing mechanism on qualifying opex/capex allowances.

c) Revenue Protection Services Incentive ($RPSIt$ term) – dealing with recovery of income from theft or damages from illegal abstraction.

1.3 In the RP7 Draft Determination, we proposed to retain these three mechanisms and add a further financial incentive linked to the Evaluative EPF. Decisions around this new EPF incentive are discussed separately in Annex V.

1.4 Excluding the 50:50 cost risk sharing mechanism, the potential financial upside and downside from these mechanisms in RP6 is of the order of c. +/- £3m per year.

Incentive	Upside £m/a	Downside £m/a
Reliability Incentive	3.0	(3.0)
Revenue Protection Services Incentive[1]	0.4	0.2
Total	**3.4**	**(2.8)**

Table 1.1: RP6 scale of financial incentives

1.5 The 50:50 cost sharing mechanism is quite extensive and provides a robust financial incentive to both control and outperform allowances. Presently it applies to most ex-ante allowances except for some pass-through cost categories such as licence fees, certain connection costs etc.

1.6 The RI is a symmetrical reward/penalty for performance against planned and unplanned CML targets. The scale of the incentive is dependent upon the

[1] Based on experience as opposed to potential. There is no financial downside to the revenue protection incentive.

VOLL, revenue exposure (1.5% of distribution revenue in RP6), weighting (66.7% unplanned: 33.3% planned) and performance against targets.

1.7 The Revenue Protection Services Incentive ($RPSIt$ licence term) is where the customer and NIE Networks share certain revenue streams on a 50:50 basis. The revenue includes:

a) Money recovered from theft of electricity.

b) Money recovered from third parties for the cost of network repairs associated with theft.

c) Income from third parties for revenue protection services.

1.8 The value of this incentive can fluctuate depending on the amount of revenue recovered. This incentive is asymmetric in that there is no downside risk or penalty, only reward.

1.9 This annex details the current position, company proposals for RP7, our draft views, consultation responses and final decisions on the incentives. Discussion of new targets is also covered, including a focus on the WSCs.

2. Reliability Incentive

RP6 approach

2.1 It is necessary for us to set reliability standards for two main reasons:

a) It is not feasible for customers to negotiate with their electricity distribution/transmission network operator directly with regards to their preferred level of reliability.

b) Focusing on reliability can help balance other regulatory objectives, most notably low prices for customers. While we expect NIE Networks to be efficient, this could adversely encourage NIE Networks to reduce reliability. By introducing reliability standards and incentives we can ensure that NIE Networks manages the cost / reliability trade-off.

2.2 The RI was first established in RP6. For this incentive we calculated separate unplanned and planned CML targets, in line with the Ofgem approach. Severe weather events were excluded from CML as the occurrence of these incidents is outside the control of NIE Networks.

2.3 An event is classified as a severe weather event when a minimum verified, number of incidents affecting the distribution HV network linked to severe weather conditions has occurred within a 24-hour period. In Norther Ireland, the “commencement threshold number” means 13 times the average daily fault rate experienced by the distribution HV network.

2.4 Transmission outages were also omitted from CML. We considered that transmission outages which cause significant customer interruptions to be exceptional events. This also assists with the comparability of network reliability data with Great Britain Distribution Network Operators (DNOs).

2.5 The key decisions / parameters of the RP6 RI can be summarised as follows:

a) The RI was structured as a symmetric incentive.

b) The unplanned CML target was set by applying a 75% weight to the benchmark CML and 25% to the historical average.

c) Given customer WTP to avoid unplanned outages is greater than planned outages, we allocated two thirds (66.6%) of the incentive to unplanned CMLs.

d) Planned CML targets were based on a 5-year historical average.

e) One third (33.3%) of distribution revenue exposure was allocated to the planned CML.

f) Targets were applied over a glidepath and are updated automatically based on outturn performance.

g) The VOLL used to derive the cost of CML was set at £15.30 per kWh (2015/16 prices).

h) Risk / reward exposure was set at 1.5% of distribution revenue.

i) Using the VOLL figures and total annual exposed revenue, we calculated the CML cap and floor of approximately +/- 7.31 CML either side of the unplanned and planned CML targets.[2]

2.6 Within RP6 to date, NIE Networks has made significant progress and outperformed targets for both unplanned and planned CML.

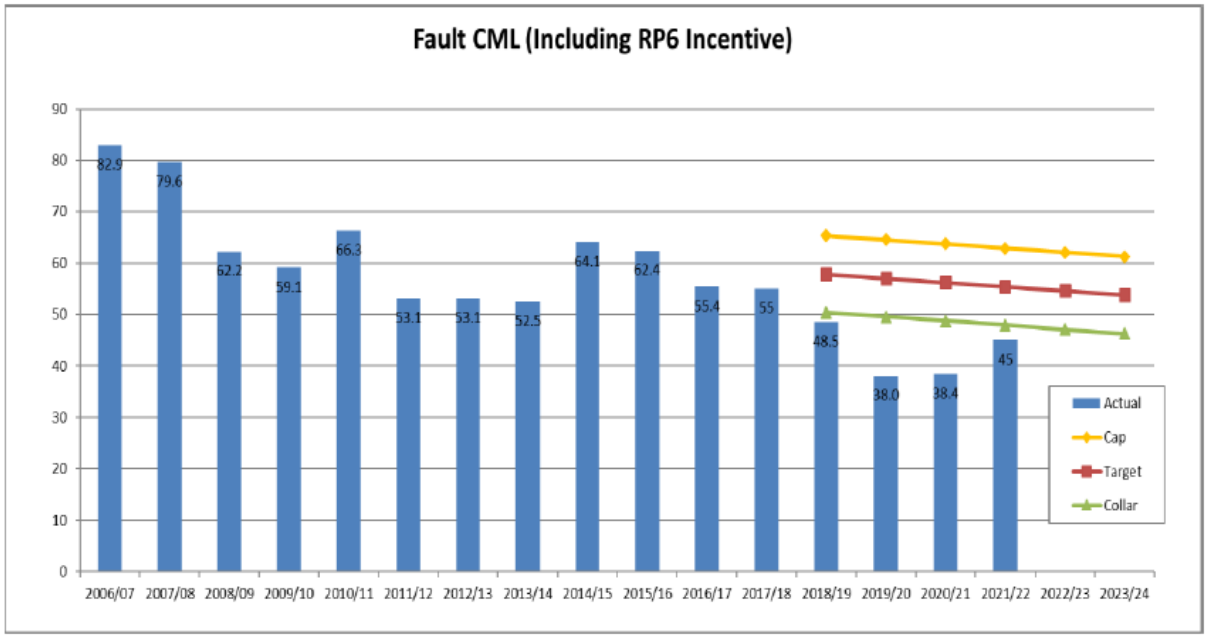


Figure 2.1: Unplanned CML performance against targets[3]

2.7 Continued outperformance has been observed in 2022-23 and 2023-24. Whilst this is a very welcome outcome, NIE Networks has also benefitted from the full reward in each year of RP6. Consumers however have also benefitted as the company has typically outperformed the collar (meaning they have received the benefit without having to pay any additional monies for the improvement).

[2] See RP6 Final Determination, Annex M, para 6.8 to 6.26, p38-42.
[3] Source: NIE Networks Network Performance Strategy, EJP 1.801, Figure 1, p8.

2.8 A similar result can be observed for planned CML performance as detailed in Figure 2.2.

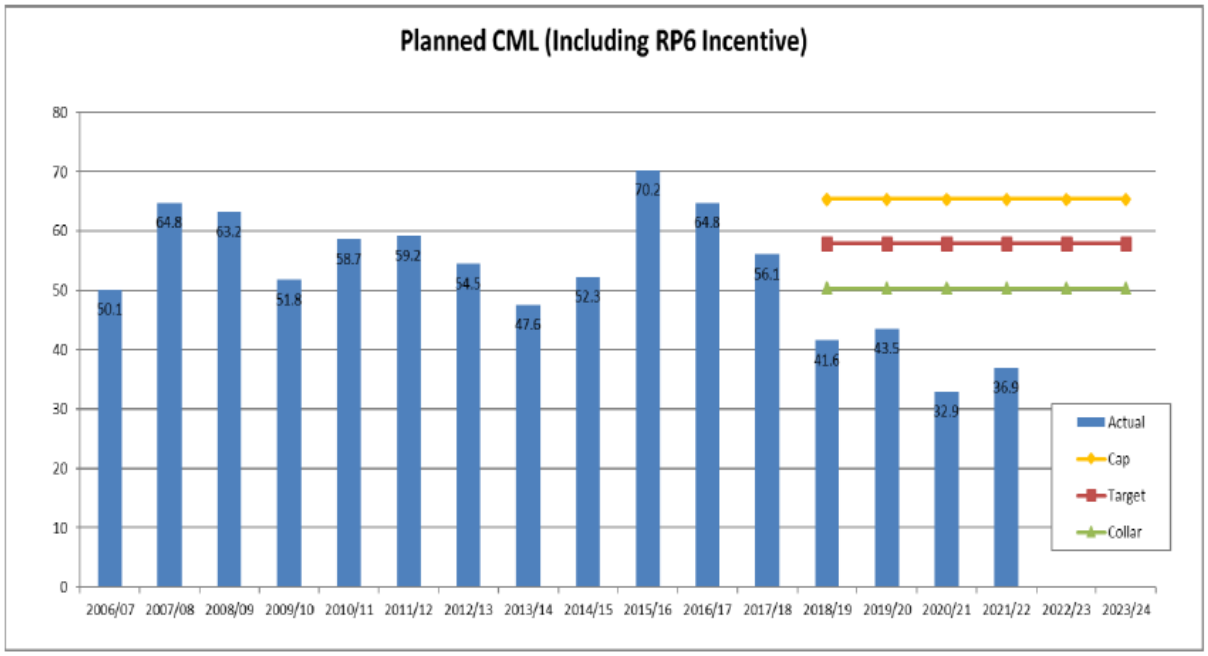


Figure 2.2: Planned CML performance against targets[4]

2.9 This outperformance has again been maintained in the most recent results reported for 2022-23 and 2023-24. The conclusion from RP6 is that the incentive has been successful with a relatively steady trajectory of improvement across the period.

NIE Networks RP7 business plan request

2.10 For RP7, NIE Networks has proposed several changes to the target setting methodology and the RI itself. Their plans can be summarised as follows:

a) Move away from the RP6 methodology for determining unplanned CML targets as it results in a worsening objective due to the way in which customer interruptions (CIs) are used to normalise data.

b) Propose to adopt the Ofgem ED-2 methodology. This mechanism applies a 0.5%, 2% or 4% year-on-year reduction based on past performance and utilises the current historic average as the starting point. Better performing DNOs have a lower target.

c) NIE Networks expect that their RP6 performance would warrant the application of the 0.5% p.a. reduction.

[4] Source: NIE Networks Network Performance Strategy, EJP 1.801, Figure 9, p21.

d) In addition, the company proposes further unplanned CML reductions based on funded investments.

e) Propose a VOLL of £18.35 per kWh and to retain the revenue exposure of 1.5% distribution revenue.

f) Retain a symmetrical incentive with a cap/collar of +/- 7.59 CML.

g) Propose that planned CML targets be removed from the RI. Instead, they suggest that planned CMLs, specifically customer perception of their impact, is incorporated into the EPF.

2.11 For the unplanned CML, the 0.5% p.a. reduction and the RP7 work programme impacts would result in the following targets:

Year	Start	25/26	26/27	27/28	28/29	29/30	30/31
0.5% Reductions	43.02	42.80	42.59	42.38	42.17	41.96	41.75
RP7 Programme		0.00	0.46	0.89	1.34	1.78	2.24
Unplanned CML Target	**43.02**	**42.80**	**42.13**	**41.49**	**40.83**	**40.18**	**39.51**

Table 2.1: NIE Networks proposed unplanned CML targets

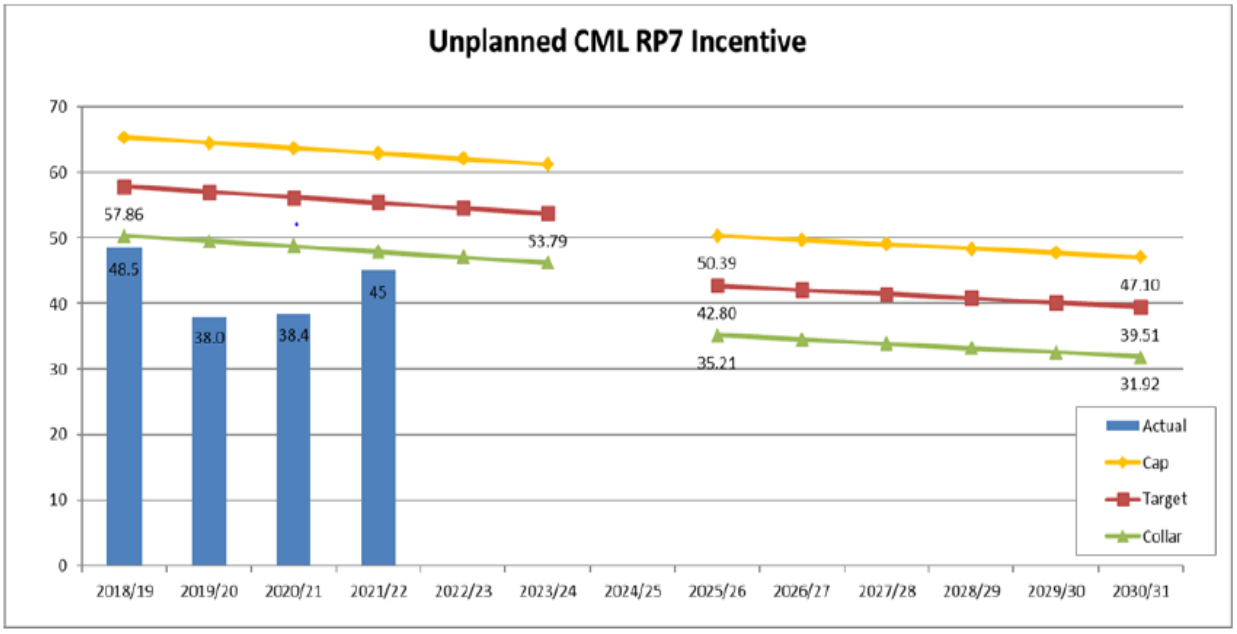


Figure 2.3: NIE Networks proposed unplanned CML targets with cap/collar[5]

2.12 For planned CMLs, NIE Networks suggest that this be removed from the incentive altogether. Their rationale can be summarised as follows:

[5] Source: NIE Networks Network Performance Strategy, EJP 1.801, Figure 8, p19.

- Significant elements of the RP7 capital programme are subject to uncertainty mechanisms which will impact the planned CML level.
- There is significant uncertainty around the impact of the HV rebuild.
- This uncertainty also extends to connections, EV charge points and small-scale generation growth.
- Stakeholder engagement demonstrated a willingness to accept / expect a rise in planned CMLs to deliver the capital programme.

2.13 NIE Networks has estimated the impact of known projects and mitigation measures from live line working as detailed in Figure 2.4 below:

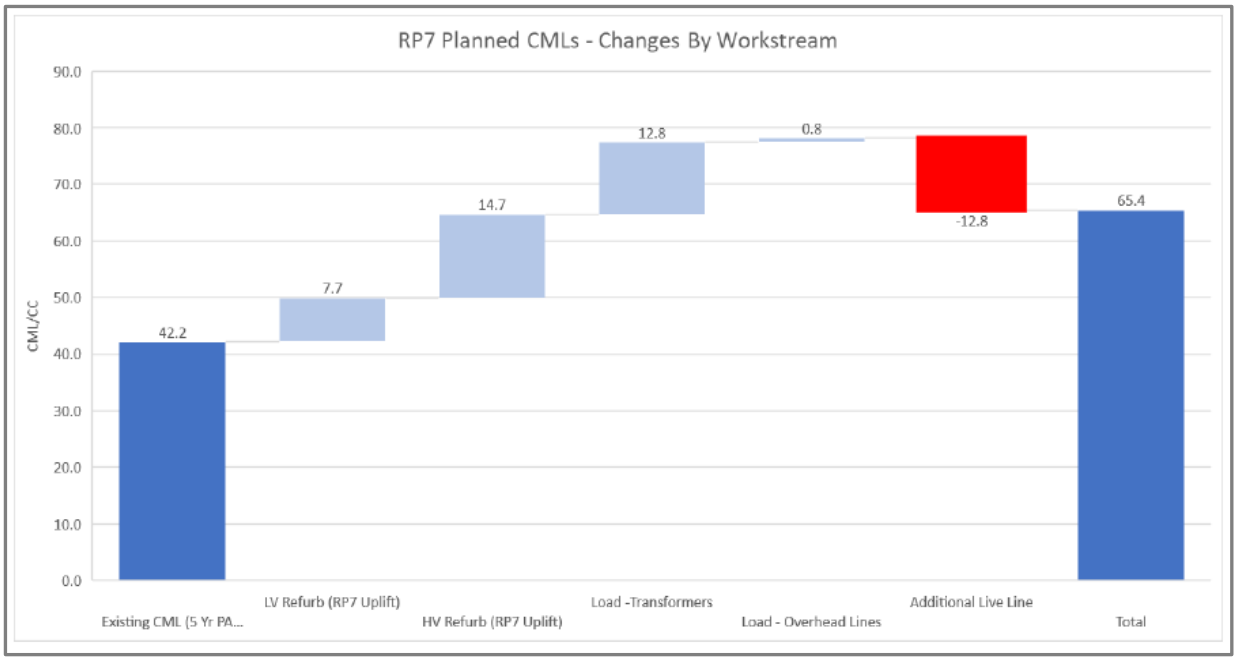


Figure 2.4: Planned CML changes by work programme[6]

2.14 NIE Networks proposed target of 65.4 planned CMLs represents a material increase from the current 5-year average of 37.9 CMLs.

Draft determination position

Methodology

2.15 Having considered the business plan arguments, we agreed that certain changes to the RI were required.

2.16 It was clear that the RP6 methodology should not be carried forward. The method of data normalisation would lead to a softening of the unplanned

[6] Source: NIE Networks Network Performance Strategy, EJP 1.801, Figure 13, p25.

target, which would be unacceptable. This is due to the different definition of customer interruptions between Northern Ireland and Great Britain.

2.17 We agreed with NIE Networks that there is benefit in adopting a simplified Ofgem type approach. However, our RP7 Draft Determination target setting methodology differed in a couple of key aspects. These included:

a) In the draft determination we updated the start point to account for the latest available year data at that point (2022-23).

b) We proposed use of a 4-year average to calculate the start point.

c) We recommended year-on-year reductions of 2% per annum.

2.18 Use of the latest available data was uncontroversial. This just represents a timing difference between the determination decision and the business plan submission.

2.19 For calculation of the start-point we recommended use of a 4-year average. This has the benefit of using the most recent and pertinent data, whilst avoiding the risks of an atypical year performance. We also noted that unplanned CML performance has been relatively consistent in this period.

2.20 The most significant departure from the company proposal is the year-on-year reductions. Whilst it was accepted that NIE Networks has outperformed in RP6, in absolute terms the company performance in unplanned CMLs still lags that compared to the Great Britain DNO average.

2.21 This might be expected to some extent given the higher proportion of overhead lines (OHL) and greater risk of adverse weather impacts. However, the absolute performance suggested scope for improvement still exists. This was also demonstrated by some DNOs[7] who have a comparable proportion of OHL but much lower levels of unplanned CMLs.

Risk and reward

2.22 We were content to accept NIE Networks proposals for VOLL which simply reflected the RP6 value uplifted to 2021-22 prices. In terms of risk exposure, the 1.5% revenue was worth simplifying as this figure is subject to change.

2.23 For the purpose of the draft determination, we recommended a fixed cap/collar incentive of +/-£2.5m per annum in 2021-22 prices. This simplifies

[7] Western Power Distribution (South Wales) and (South West) both meet the criteria of high proportion of OHL yet lower CMLs than NIE Networks. Scottish Hydro Electric Power Distribution has worse performance but has been tasked with 4% year-on-year reductions.

the calculation and is not dissimilar to NIE Networks own forecast of +/- £2.4m for unplanned CML allowances.

2.24 Given the uncertainty around planned CMLs, we also recommended adjusting the revenue allocation on an 80:20 split (£2m / £0.5m) between unplanned and planned CMLs respectively. The impact of this decision was a cap/collar of +/- 6.32 CMLs around the unplanned target using the RP6 VOLL.

2.25 The outworking of the draft approach can be summarised in Table 2.2 and Figure 2.5 as follows:

Year	Start	25/26	26/27	27/28	28/29	29/30	30/31
2.0% Reductions	39.23	38.44	37.67	36.92	36.18	35.46	34.75
RP7 Programme		0.00	0.46	0.89	1.34	1.78	2.24
Unplanned CML Target	**39.23**	**38.44**	**37.21**	**36.03**	**34.84**	**33.68**	**32.51**

Table 2.2: UR proposed unplanned CML targets

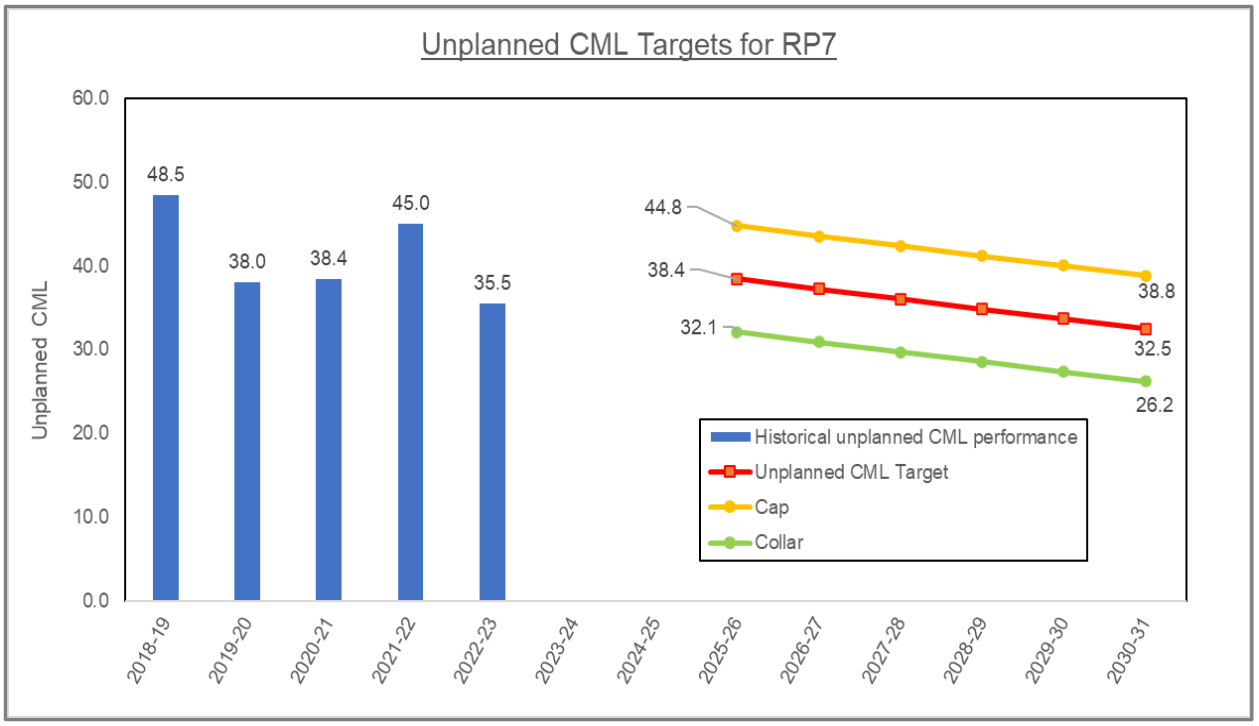


Figure 2.5: UR proposed unplanned CML targets with cap/collar

2.26 It was our view that the proposals represented a challenging but achievable improvement in reliability.

Planned CML Targets

2.27 For the draft determination we accepted NIE Networks logic that the larger capital programme could negatively impact planned interruptions and CMLs.

We also accepted that creating fixed 6-year targets was not appropriate with the proposed changes.

2.28 On the other hand, these same challenges are also being faced by Great Britain DNOs. In their final determination Ofgem state,

"The target will be set using the RIIO-ED1 approach, which is based on a rolling three-year average with a two-year lag, as per our SSMD position. We consider that this approach ensures that DNOs cannot allow their performance to deteriorate without facing a penalty and that it is sufficiently flexible to reflect changes in work programmes."[8]

2.29 Use of the 3-year rolling average takes account of historical performance and imposes penalties for deterioration. Given this, it seemed evident that the Great Britain DNOs are not anticipating the same decline in planned CML performance as NIE Networks. The reason for this difference was unclear.

2.30 We did not think the RP6 methodology of a fixed price control target was feasible. Furthermore, we considered that this metric adds value for consumers and therefore we believed it important that NIE Networks continues to focus on minimising this impact for consumers. In the draft decision we did not consider the NIE Networks proposal of an increase to 65.4 planned CMLs to be an appropriate target.

2.31 We were unclear what was meant by the company statement that, *"we propose that planned CMLs, specifically customer perception of their impact, are incorporated into the newly proposed Evaluative Performance Framework."*[9] It was uncertain how this would be measured or incentivised.

2.32 For the RP7 draft decision we suggested that the Ofgem approach be adopted for planned CML target setting. This meant targets being calculated annually using the 3-year rolling average with a 2-year lag. This would ensure that focus on this metric continues but allows flexibility for changing capital programmes.

2.33 However, this approach only allowed for the setting of a specific target for the first year of RP7. Targets will automatically be recalibrated each year thereafter depending on outturn performance.

[8] Source: Ofgem Final Determination, Core Methodology Document, para 6.125, p183.
[9] EJP 1.801, Network Performance Strategy, p20.

Year	2025/26
Planned CML Target (with cap/collar)	35.83 (+/- 8.27 CML)

Table 2.3: Proposed planned CML target at draft determination

2.34 Given the level of uncertainty, we did however recommend that the percentage of revenue exposed to this target is lowered to 20%. This reduced the risk faced by the company for declining performance.

2.35 We considered this proposal to be a balanced approach. It lowered the risk associated with the planned element of the RI but ensured that focus on this important metric was not lost.

2.36 We were however willing to engage further on the new planned CML target setting methodology. We also encouraged feedback from NIE Networks as to why their planned CML deterioration is not expected to be matched in Great Britain.

Consultation responses and UR views

2.37 Some material issues were raised by NIE Networks and other stakeholders with respect to the draft determination. Summary comments and our responses are detailed in the tables below. The most material response was received by NIE Networks. Their views and our high-level responses are set out below.

	NIE Networks Consultation Response	UR Views & Action
1	NIE Networks agrees with UR's proposal to update the start point to account for the latest available year data. However, as NIE Networks will publish the updated data for 2023/24 in its Condition 19 Report in May, UR should use this data for the start point. **[NIE Networks Response, para 11.15, p228]**	We agree with this and have included data from 2023-24 in our final deliberations.

2	NIE Networks is on target to achieve a 29% reduction in weighted average CMLs between the start of RP6 and start of RP7, which would place it amongst the best performing DNOs in the UK. However, UR has not awarded NIE Networks with the corresponding 0.5% year on year improvement factor. **[NIE Networks Response, para 11.19, p229]**	We welcome the outperformance of unplanned CML targets that has been achieved in RP6. However, the reliability incentive has been in place longer in Great Britain than in Northern Ireland. As a result, NIE Networks still lags behind in terms of absolute performance with respect to unplanned CMLs. Given this absolute gap, we are of the view that a tougher target should be imposed for RP7. We think this particularly pertinent given that funding levels in line with Great Britain provides an expectation that customer service levels are of a similar standard as well.
3	The aggregate impact of UR's approach results in a CML target for NIE Networks which is 17% (6.7CMLs) higher than the CML target of a comparative Great Britain DNO. **[NIE Networks Response, para 11.20, p229]**	We disagree with this assessment. In fact, some DNO's with comparable networks and absolute performance such as Scottish and Southern Energy Power Distribution (SSEH) have tougher objectives at 4% per annum target reductions.
4	The adoption of a straight 4-year average of unplanned CMLs diverges from established industry practice. For both RP6 and RIIO-ED2 a weighted average has been used: this uses a 4-year average for each of LV and HV (6.6/11kV) CML statistics, and a 10-year average for EHV (33kV) CML statistics. **[NIE Networks Response, para 11.23, p229]**	We accept this is a divergence. However, it is not clear why a 10-year average should be adopted for EHV faults. Even though they occur less frequently, use of such a long average captures worse historic performance which no longer seems applicable to NIE Networks. We are minded to retain a 4-year average for all aspects of the CML metric in order to set targets.
5	NIE Networks is on target to achieve a 29% reduction in weighted average CMLs between the start of RP6 (58.68 CMLs) and start of RP7 (41.53 CMLs). In light of NIE Networks expected excellent performance, the company considers that this would warrant application of a 0.5% year-on-year reduction, based on Ofgem's RIIOED2 methodology, rather than UR's proposed 2% year-on-year reduction. **[NIE Networks Response, para 11.25, p230]**	As noted above in the response to point 2, we are of the view that NIE Networks absolute performance should still be considered when setting targets. It is for this reason that we consider a tougher target than the 0.5% p.a. approach to be applicable.

6	UR has generally misrepresented NIE Networks' performance level against the Great Britain DNOs, by drawing comparisons on absolute terms. NIE Networks considers that only SSEH is a comparable DNO to the company based on OHL versus underground ratio and also customer numbers. **[NIE Networks Response, para 11.26, p230]**	We do not consider the performance to be misrepresented. NIE Networks data illustrates that Western Power Distribution [(SWALES) and (SWEST)] proportion of overhead lines (OHL) is similar to NIE Networks, yet they have much better unplanned CML performance. NIE Networks has failed to explain why these companies do not represent comparable DNOs. Using the example of SSEH which NIE Networks accept as a legitimate comparator, we see worse absolute performance but a tougher target of 4% p.a. reductions. This lends weight to our approach for RP7.
7	When the Great Britain average data is normalised against NIE Networks' network topology ratios and customer numbers, it is clear that NIE Networks is actually below the Great Britain average. **[NIE Networks Response, para 11.27, p230 & p231]**	On review of the data normalisation approach, we do not think the calculations give a fair reflection of Great Britain DNO performance. Ofgem benchmark using a CML per CI approach, but this is problematic given different CI definitions. However, what is clear is that comparable DNOs with a similar proportion of OHL have better unplanned CML performance. This suggests that scope for improvement exists.
8	UR has incorporated NIE Networks' unplanned CML savings into its unplanned CML target prior to the financial incentive being applied. This approach differs to that of Ofgem who allocated the improvement factors on the DNOs without taking consideration of each DNO's investment programme. **[NIE Networks Response, para 11.28, p231]**	This point is accepted. However, our approach simply mirrors that taken by NIE Networks in the business plan. Such a methodology seems appropriate given specific funding which will address customer interruptions. It would seem counter-intuitive for consumers to fund CML improvements and then provide NIE Networks an additional bonus for delivering agreed outputs.
9	NIE Networks requests that UR changes the unplanned CML incentive so that it: • includes a weighted average starting point, which reflects the Ofgem approach; • uses 2023/24 data for the start point; and • imposes a 0.5% year-on-year reduction, which takes account of RP7 investment programme. **[NIE Networks Response, para 11.32, p232]**	For the purposes of the final determination, we are minded to retain the starting point methodology and the 2% per annum challenge, whilst taking account of the RP7 capital programme funding. We have however incorporated the 2023-24 outturn data into the analysis, resulting in an uplift to the unplanned CML targets from the draft determination.

10	NIE Networks does not agree that the RIIO-ED2 planned CML incentive is appropriate for use in Northern Ireland because of the fact that the network programme planned for Great Britain in RIIO-ED2 is different to that planned for Northern Ireland in RP7. **[NIE Networks Response, para 12.6, p233]**	Whilst there are differences, it is also true that variations exist in Great Britain, yet Ofgem has retained the planned CML incentive for all DNOs. It is difficult to compare Northern Ireland and Great Britain capital programmes due to differences in the regulatory frameworks in terms of what is funded upfront and what is included in uncertainty mechanisms. However, it is worthwhile noting the comment from NERA in the business plan submission that, *"Our comparison exercise shows that NIE's proposed rates of increase for load related capex, while being higher than Ofgem's average allowed rates of increase in RIIO-ED2, are in line with the British DNOs submitted costs for ED2. The same conclusion holds for non-load related capex after accounting for the two large capex programmes NIE has planned for RP7."*[10] Given this viewpoint, we do not see a good reason to treat NIE Networks substantially differently for planned CML performance.
11	Proposed mechanism will generate a significant concern for NIE Networks in the planning of its programme for RP7, as it will encourage NIE Networks to either restrict its work delivery or incur higher than normal planned CMLs in the first few years of RP7 to create a scenario where a positive incentive payment could be earned in the final years. **[NIE Networks Response, para 12.7, p233]**	Restricting work delivery would have negative reputational incentives and be contrary to RP7 output obligations. Due to the two-year lag, increasing planned CMLs above target to gain a reward at period end would be somewhat illogical. NIE Networks would have to incur a number of years of financial penalties to gain a potential reward at the end of RP7. This would not be in customers or their own interests. It is however accepted that there is a risk that the cost of meeting the target may be greater than the incentive amount. As such, it is possible that performance may deteriorate. However, we would expect a prudent operator to restrict any deterioration.

[10] Source: NIE Networks business plan, Annex A03, Comparative Benchmarking to Support the Preparation of NIE Networks' RP7 Business Plan, p89.

12	UR has failed to recognise the differences between Northern Ireland and Great Britain with respect to planned CMLs. In Northern Ireland, planned CMLs are forecast to almost double in RP7 as a result of commitments to OHL replacement. In comparison, Great Britain DNOs have committed to a significantly lower amount of 11kv and LV network build as part of their network configurations during RIIO-ED2. Great Britain DNOs have also performed these types of overhead line activities in previous price control periods, whilst NIE Networks has not. **[NIE Networks Response, para 12.8 & 12.9, p234]**	Differences in timing of spend is accepted. However, planned CML performance is currently much better in Great Britain than Northern Ireland, despite having already undertaken this work. This suggests that NIE Networks has improvements to be made in terms of customer service and the focus on this metric should not be removed simply due to timing of activity.
13	NIE Networks does not consider that arbitrarily diluting the planned CML incentive is in its customers' best interest. Planned network outages remain an issue of significant importance to customers. **[NIE Networks Response, para 12.10, p235]**	We agree that planned outages remain a significant issue for consumer. This is the reason for retaining an incentive rather than removing it entirely. The dilution simply reflects our concern over uncertainty.
14	The company submits that the EPF is a strong and appropriate mechanism to incentivise the company to improve its performance with respect to planned CMLs**.** **[NIE Networks Response, para 12.11, p235]**	We might agree with this if i) reasonable planned outage targets are defined; and ii) wider customer experience expectations are set. NIE Networks has not detailed how the EPF would address these issues. In absence of this, we think retention of planned CMLs within the RI maintains focus on this key consumer issue.

15	NIE Networks requests that, in its Final Determination, UR removes the proposed planned CML mechanism set out in the draft decision and instead incorporates a qualitative assessment of planned CMLs as part of a wider customer service element within the EPF mechanism. **[NIE Networks Response, para 12.15, p235]**	We disagree with this request. NIE Networks has not properly justified the difference in performance levels between themselves and Great Britain DNOs to merit different treatment. Neither have they explained how a qualitative assessment in the EPF might work or how customers would be protected in such a regulatory framework. With planned CMLs, there is also the issue of quite a material difference in absolute performance. In the absence of this detail, we are minded to retain the Ofgem methodology for setting the planned CML target and the proposed financial reward/penalty as part of the reliability incentive. We have however tailored the approach to account for the fact that the scale of the capital programme increase is higher for NIE Networks. As a result, we have used the 3-year average plus 5 CMLs to set the target. This ensures that the company will not be penalised for some deterioration and will receive a reward for maintaining current service levels.

Table 2.4: NIE Networks issues and UR response

2.38 The other consultation response which addressed the RI in detail was that of CCNI. We have set out their comments and our views in the table below.

	CCNI Consultation Response	UR Views & Action
1	Since its introduction, it [*RI*] has led to very significant improvements in performance from NIE Networks. Therefore, we strongly agree with retaining both planned and unplanned CML. **[CCNI Response, p11]**	We agree with this and have retained incentives for both metrics in RP7.
2	We would encourage UR to develop an appreciation of the approach that Ofgem used, to consider whether Ofgem's approach is relevant to NIE Networks' performance, and hence to set CML targets for NIE Networks that reflect its comparative performance. **[CCNI Response, p12]**	For RP7 we have largely followed this approach. The Ofgem methodology has been relatively closely followed whilst adjusting targets for NIE Networks comparative performance. We think this strikes a fair balance and helps close the customer performance gap.

3	While NIE Networks has significantly improved performance since the introduction of CML, the unadjusted data suggests that it might continue to lag behind that of Distribution Network Operators (DNOs) in Great Britain, including compared to DNOs which have a high proportion of overhead lines like National Grid Electricity Distribution (South Wales and South East networks). **[CCNI Response, p12]**	We agree with this assessment. CCNI figures and Ofgem targets show a particular gap with respect to planned CML performance. This indicates that the focus on this metric should be maintained in RP7. We have tailored the approach to take account of NIE Networks particular circumstances. However, we would not wish to see the gap in the level of service decrease in RP7.
4	We disagree with UR's proposal to reduce the weight of planned CML, from one third of the total incentive to one fifth. This will weaken the incentive for NIE Networks to minimise planned CML. We understand NIE Networks justified its request for removing planned CML from the incentive by the fact that a larger investment programme will necessarily increase planned CML. While we accept this, we note that Great Britain DNOs face similar challenges which have not led Ofgem to weaken incentives on planned CML. **[CCNI Response, p13]**	This is a fair point and the main reason as to why the metric has been retained. The decision to dilute the incentive strikes a balance between retaining an incentive and uncertainty about the impact of the larger capital programme. We do however accept that there is a strong argument for maintaining the current reward/penalty allocation.

5	We have heard concerns that the current design may lead to a deterioration in CML performance at the beginning of the period and that the scale of network reinforcement may necessitate consideration of qualitative measures to address the wider customer experience related to planned CML. **[CCNI Response, p13-14]**	We do not think the issue of an early period deterioration due to a perverse incentive is a likely concern given the lagged target mechanism. Ofgem also considered this issue and stated the following: • We consider the risk of gaming to be low, and that the existing approach mitigates this through the application of penalties for DNOs who fail to achieve their targets for planned interruptions. • We consider that setting targets on a three-year rolling average basis (with a two-year lag) will ensure DNOs do not allow their performance to deteriorate without an associated penalty. • This approach to setting planned interruptions targets provides some flexibility for changes in work programmes that may arise from external requirements. • Where volumes of work increase due to external requirements, DNOs' targets in subsequent years will reflect this change. • Any reductions in revenue as a result of these increased work volumes will be offset by targets that are comparatively easier in later years.[11] It is however accepted that the Ofgem incentive is more material and there is a risk that the cost of meeting the target may be greater than the incentive amount. As such, it is possible that performance may deteriorate. However, we would expect a prudent operator to restrict any deterioration.

[11] See RIIO-ED2 Methodology Consultation (para 7.41 – 7.43, p81) and Decision (para 7.28, p76),

6	We agree with the proposal to retain the VOLL and adjust the figure to reflect inflation, in line with Ofgem's approach in RIIO-ED2. We note that Ofgem indicated they will undertake a review of the VOLL. We would expect UR to consider the results of this review once they are available. **[CCNI Response, p13-14]**	In the draft determination we used a VOLL of £18.35/kWh. This was based on the RP6 figure after uplifting for inflation. At the end of September 2023, the Single Electricity Market Committee (SEMC) published an information paper[12] detailing updated VOLL figures for use in the SEM. Based on consumer surveys carried out in early 2022 relating to specific interruption parameters, the Regulatory Authorities calculated a VOLL of €16,464/MWh. This translates to a value of £14.03/kWh using 2022 exchange rates. The research also shows that the highest average amounts that domestic bill payers are willing to pay to avoid an interruption in Northern Ireland is £15.36. In the final determination we are adopting the overall VOLL updated figure of £14.03/kWh as opposed to the RP6 figure updated for inflation.

Table 2.5: CCNI consultation response issues and UR views

2.39 Having considered the draft determination consultation response arguments, we do not believe that many changes to the RI are required for the final decision. Our final position on the key issues are set out below.

Final determination views

Methodology

2.40 Having considered the business plan arguments and consultation responses, we agree that certain changes to the RI are required.

2.41 We agree with NIE Networks that there is benefit in adopting a simplified Ofgem type approach. However, our final RP7 target setting methodology differs in a couple of key aspects. These include:

a) We have updated the start point to account for the latest available year data (2023-24).

b) We make use of a simple 4-year average to calculate the start point.

[12] See SEM-23-072, Calculation of Single Value of Lost Load within the Single Electricity Market Information Paper.

c) We have determined year-on-year reductions of 2% per annum plus funded CML reductions.

2.42 Using the latest available data is uncontroversial. It has the impact of slightly weakening the unplanned CML target from that set at the draft due to slightly worse performance in 2023-24.

2.43 For calculation of the start-point we have retained use of a 4-year average. This has the benefit of using the most recent and pertinent data, whilst avoiding the risks of an atypical year performance.

2.44 We note NIE Networks objection that this is a regulatory divergence. However, it is not clear why a 10-year average should be adopted for EHV faults. Use of such a long average captures worse historic performance which no longer seems applicable to NIE Networks.

2.45 In terms of the year-on-year reductions, we think the draft approach is still merited. This is due to the fact that in absolute terms the company performance in unplanned CMLs still lags that compared to average Great Britain DNO customer service levels.

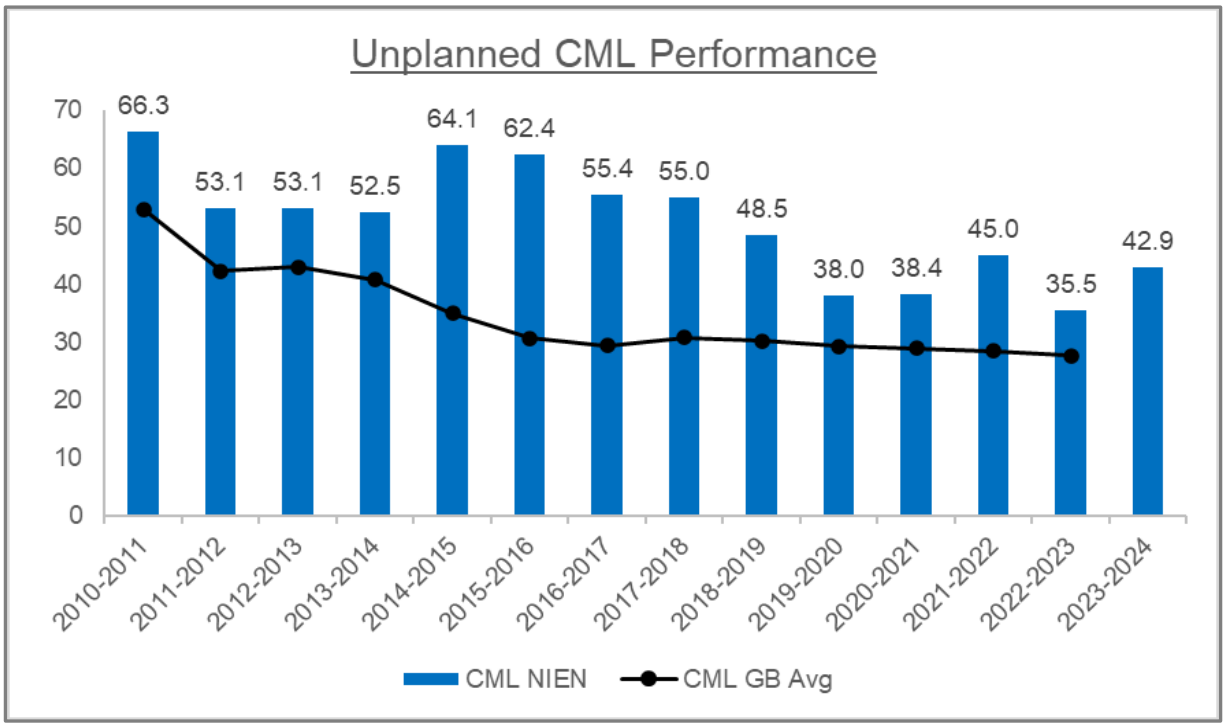


Figure 2.6: NIE Networks unplanned CML performance versus Great Britain DNOs

2.46 Although NIE Networks has a higher proportion of OHL, the absolute performance suggested scope for improvement still exists. This was also demonstrated by NIE Networks own analysis on Great Britain DNOs who

have a comparable proportion of OHL but much lower levels of unplanned CMLs.

DNO	OHL vs Underground (%)	Customer Numbers (Millions)	2021/22 CML
NIE Networks	64:36	0.88	40
SSEH	63:37	0.77	48
SWALES	50:50	1.13	19
SWEST	55:45	1.61	29
ESB Networks	86:14	2.35	100

Table 2.6: NIE Networks analysis of DNO comparisons[13]

2.47 From the table it can be seen that Western Power Distribution (South Wales) and (South West) both meet the criteria of high proportion of OHL yet have much lower unplanned CMLs than NIE Networks. Scottish Hydro Electric Power Distribution (SSEH) has worse performance but has been tasked with 4% year-on-year reductions.

2.48 NIE Networks has failed to explain why these companies do not represent comparable DNOs. Neither do we think that we have misrepresented performance levels by drawing comparisons on absolute terms. The fact remains that comparable companies have better performance which should be targeted by NIE Networks.

Risk and reward

2.49 At the draft stage we were content to accept proposals for VOLL which simply reflected the RP6 value uplifted to 2021-22 prices. However, at the end of September 2023 the Single Electricity Market Committee (SEMC) published an information paper[14] detailing updated VOLL figures for use in the SEM.

2.50 Based on consumer surveys carried out in early 2022 relating to specific interruption parameters, SEMC calculated a VOLL of €16,464/MWh.[15] This translates to a value of £14.03/kWh using 2022 exchange rates.

2.51 In the final analysis, we are adopting the updated overall VOLL figure of £14.03/kWh as opposed to the RP6 figure uplifted for inflation. This seems more appropriate as it represents the latest WTP data.

[13] Source: NIE Networks consultation response, Table 4, p230.
[14] Source: https://www.semcommittee.com/publications/sem-23-072-calculation-single-value-lost-load-within-single-electricity-market
[15] Source: Calculation of a single Value of Lost Load within the Single Electricity Market, p1.

2.52 In terms of risk exposure, the 1.5% revenue was worth simplifying. For the purpose of the final determination, we have determined a fixed cap/collar of +/-£2.5m per annum in 2021-22 prices. This follows the draft approach and simplifies the calculation.

2.53 Given the uncertainty around planned CMLs, we have also adopted the consultation position and adjusted the revenue allocation on an 80:20 split (£2m / £0.5m) between unplanned and planned CMLs respectively. Whilst we recognise that this dilutes the planned CML incentive, we think it strikes a fair balance between incentive and uncertainty around future work levels.

2.54 The impact of this decision combined with a revised VOLL results in a cap/collar of +/- 8.27 CMLs around the unplanned target.

2.55 The outworking of the final determination approach can be summarised in Table 2.6 and Figure 2.7 as follows:

Year	Start	25/26	26/27	27/28	28/29	29/30	30/31
2.0% Reductions	40.48	39.67	38.87	38.09	37.33	36.59	35.85
RP7 Programme		0.00	0.46	0.89	1.34	1.78	2.24
Unplanned CML Target		**39.67**	**38.41**	**37.20**	**35.99**	**34.81**	**33.61**

Table 2.7: UR unplanned CML targets for RP7

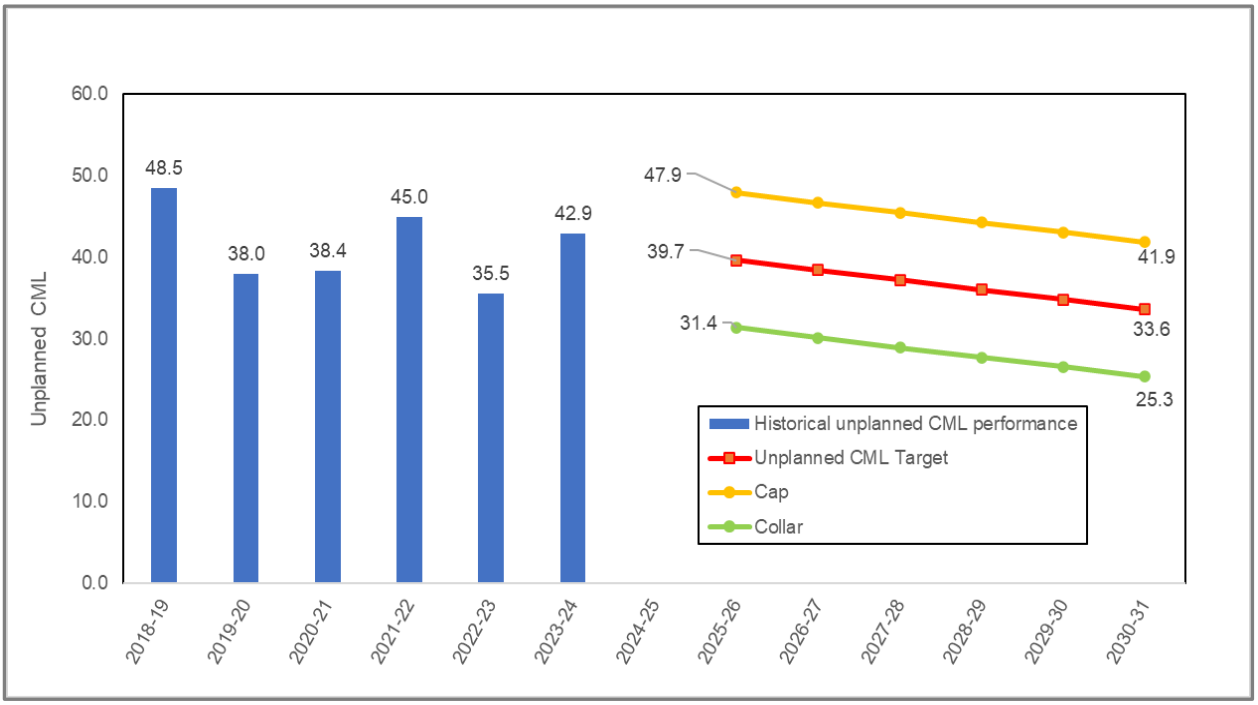


Figure 2.7: UR final unplanned CML targets with cap/collar

2.56 It was our view that the proposals represent a challenging but achievable improvement in reliability. The financial parameters for calculation of the CML cap/collar are detailed in Table 2.8 below.

Variable	Figure	Unit of Measurement
Annual electricity consumption	8,533,695,568	kWh
Total hours in a year	8,760	Hours
Number of meters	894,977	Number
Customer numbers used for CML	950,000	Number
Average consumption per hour	1.088	kWh per customer
Value of Lost Load (VOLL)	£14.03	£/kWh
Cost per hour per customer	£15.28	£/kWh
Cost of customer hour lost	£14,511,359	£
Cost of unplanned CML	£241,856	£
Cost of planned CML	£60,464	£
RP7 revenue exposure (annual)	+/- £2,500,000	2021/22 prices
Unplanned CML allowance (4/5)	+/- £2,000,000	2021/22 prices
Planned CML allowance (1/5)	+/- £500,000	2021/22 prices
CML Cap/Collar	**+/- 8.27**	**CMLs**

Table 2.8: Assumptions used to calculate the CML cap/collar

Planned CML Targets

2.57 We accept NIE Networks logic that the larger capital programme could negatively impact planned interruptions and CMLs. We also accepted that creating fixed 6-year targets is not appropriate with the proposed changes.

2.58 However, we did not consider the arguments that NIE Networks made to exclude the metric from the RI to be valid. In the first instance, we agree that there are capital programme differences. However, these exist in Great Britain, yet the same methodology applies.

2.59 As CCNI has noted, a material gap exists in planned CML performance. NIE Networks has suggested that differences exist due to work already undertaken in Great Britain. However, if this is the case it is therefore not clear why performance is much better in Great Britain.

2.60 The difference is further highlighted by the planned CML targets that have been set by Ofgem for the Great Britain DNOs for 2023-24. This is compared to what the target would be for NIE Networks in the first year of RP7 using the same methodology.

DNOs	Planned CML Target 2023-24[16]
EMID	1.26
ENWL	2.64
EPN	2.88
LPN	0.05
NPGN	2.58
NPGY	1.74
SPD	2.66
SPMW	4.67
SPN	1.55
SSEH	7.91
SSES	3.10
SWALES	4.87
SWEST	7.52
WMID	4.44
NIE Networks 2025-26	37.73

Table 2.9: Comparison of planned CML targets

2.61 This suggests that NIE Networks has improvements to be made in terms of customer service and the focus on this metric should not be removed simply due to timing of activity.

2.62 Use of the 3-year rolling average takes account of historical performance and imposes penalties for deterioration. Whilst we have largely adopted this approach, we appreciate that there is a risk of service level deterioration due to the scale of the capital programme change.

2.63 We also felt that moving the metric to the EPF without a clear view on how performance would be measured could be detrimental to consumers. We might agree with this if targets were well defined and wider customer experience expectations had been set.

2.64 However, NIE Networks has not detailed how the EPF would address these issues. In absence of this, we think retention of planned CMLs within the RI

[16] It should be noted that the Great Britain figures in this table represent 50% of actual performance as per the Ofgem approach to planned CML reporting. Comparisons are not therefore like-for-like. However, doubling Great Britain DNO figures would still represent a significant outperformance of NIE Networks.

maintains focus on this key consumer issue.

2.65 Finally, we reject the notion that adoption of the Ofgem methodology would create an incentive to incur higher than normal planned CMLs in the first few years to create a scenario where a positive incentive payment could be earned in the final years. NIE Networks has demonstrated this issue as follows:

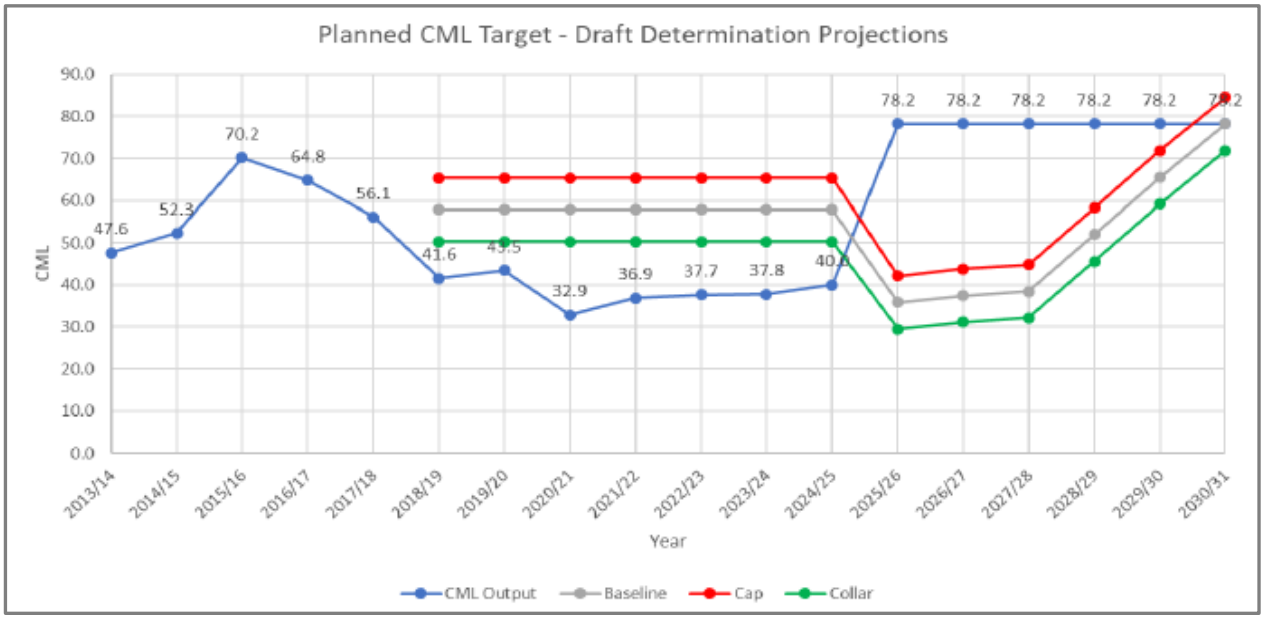


Figure 2.8: Risk of adopting Ofgem planned CML methodology[17]

2.66 As can be seen from the graphic, the target operates with a lag. Even if planned interruptions were artificially increased as suggested, NIE Networks would have to incur several years of penalties to gain a reward in the final year of RP7. This would be an unsound strategy to adopt.

2.67 Consequently, for the RP7 Final Determination we are adopting the Ofgem approach for planned CML target setting. This means targets being calculated annually using the 3-year rolling average with a 2-year lag. This ensures that focus on this metric continues but allows flexibility for changing capital programmes.

2.68 After review we have however decided to consider the differences in the scale of change in the capital programme. As a result, we have tailored the approach to make it a 3-year average plus 5 CMLs.

2.69 This has the effect of allowing for some deterioration before a penalty is incurred. It also serves to reward the company if they are able to maintain current service levels.

[17] Source: NIE Networks response to draft determination consultation, p234, Figure 2.

2.70 However, this dynamic approach only allows for the setting of a specific target for the first year of RP7. Targets will automatically be recalibrated each year thereafter depending on outturn performance.

Year	2025-26
Planned CML Target (with cap/collar)	42.73 (+/- 8.27 CML)

Table 2.10: Planned CML target for final determination

2.71 Given the level of uncertainty, we have also decided that the percentage of revenue exposed to this target is lowered to 20%. This reduces the risk faced by the company for declining performance.

2.72 As at the draft determination, we consider this to be a balanced approach. It lowers the risk associated with the planned element of the RI but ensures that focus on this important metric is not lost.

2.73 It could also be argued to be somewhat reasonable given the differences in WTP to avoid unplanned and planned interruptions.

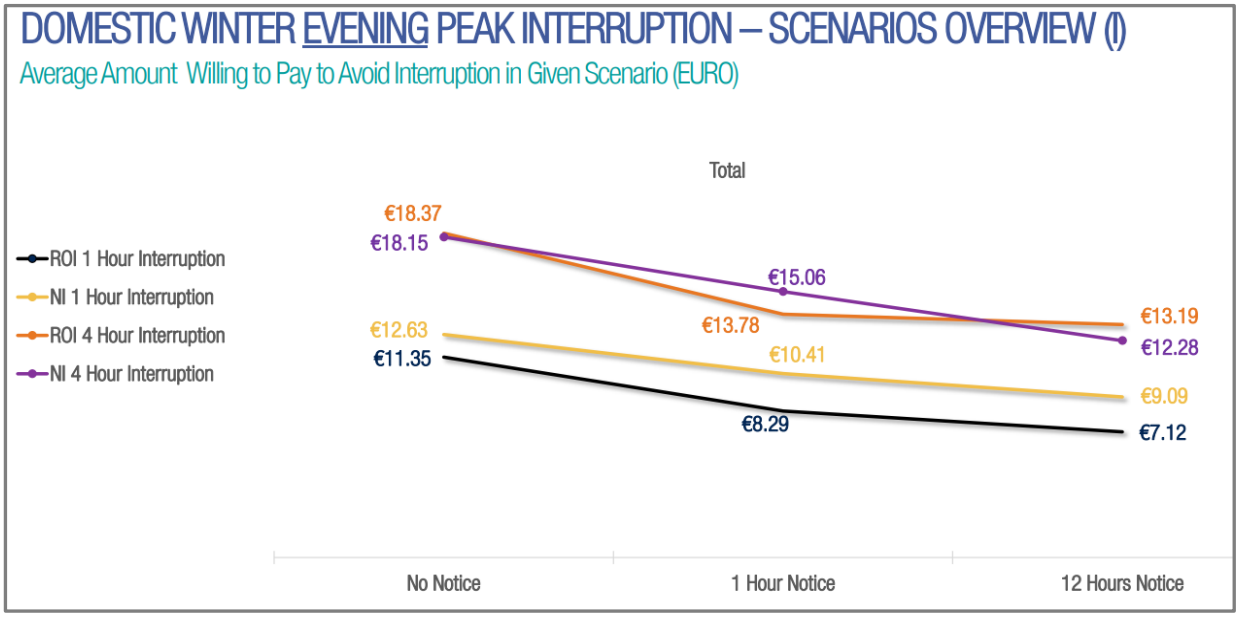


Figure 2.9: WTP values for unplanned and short notice interruptions[18]

2.74 From the research it can be seen that there is a 28% reduction in the WTP to avoid a 1-hour planned interruption with a 12-hour notice period. For the purposes of NIE Networks guaranteed standards of service they must provide at least a 72-hour notice to be properly considered a planned interruption.

[18] Source: Value of Lost Load Research, Ipsos, p8.

2.75 It is not clear what impact the 3-day notice would have on the WTP figure. However, it can be safely assumed that there is a material divergence in the impact of fault and planned interruptions. As such, a move to 80:20 weighting may not be considered unreasonable.

2.76 It is also worth noting that we have provided support for continued delivery against this planned CML target by funding c. £1m in fleet allowances for the new live line lorries.

Customer Interruptions

2.77 Within the business plan, NIE Networks highlighted an inconsistency between jurisdictions regarding unplanned customer interruptions.

2.78 In Northern Ireland any unplanned CIs in excess of 1 minute is a reportable event on the National Fault Interruption Reporting System (NaFIRS). For the Great Britain DNOs this figure is set at anything in excess of 3 minutes. Instead, a separate *Short Term Interruption Report* captures any interruption which occurs between 1 and 3 minutes.

2.79 NIE Networks propose that the 3-minute interruption window is extended to cover unplanned CI and CML statistics. They also suggest that a new Short Term Interruption Report is reported against during RP7.

2.80 This issue was not discussed in any detail in the draft determination. However, we agree with the company suggestions. This change should be implemented from the start of RP7. Correction of this inconsistency should also help address benchmarking issues for unplanned CMLs in RP8.

Licence workings

2.81 Within the distribution licence the RI is defined as follows:

"RIt is the allowed amount (if any) in Regulatory Reporting Year t, being the amount the Authority determines in a published decision to be appropriate or the Licensee to recover in respect of the reliability incentive in that Regulatory Reporting Year t, as calculated by the Authority under and in accordance with the Reliability Incentive Model."

2.82 A separate spreadsheet is published alongside this annex representing the Reliability Incentive Model. This provides detail on the calculation of the reward / penalty for unplanned and planned CML performance.

2.83 Planned CMLs have a dynamic target which will need to be updated each year based on historic actuals. This should be completed as part of the annual tariff process.

3. Cost Sharing Mechanism

Draft determination summary

3.1 In terms of the 50:50 cost sharing mechanism, NIE Networks did not propose any major structural changes. The only material consideration related to items currently included which might be subject to future exclusion i.e. business rates, innovation costs, severe weather, non-recoverable alterations etc.

3.2 We agreed with NIE Networks that this incentive still represented an important tool in encouraging efficiency and restraining cost. Consequently, no major change to the structure of the incentive was suggested.

3.3 For severe weather, it was our intention to retain these costs as part of the cost sharing mechanism. We accepted NIE Networks arguments around business rates and proposed to remove these costs from the 50:50 mechanism.

3.4 Innovation costs were expected to be removed from the mechanism as this is not an area where underspend is to be strongly incentivised. We did however expect overspend to still be subject to cost sharing.

Final determination

3.5 Few of the responses raised any points about the 50:50 mechanism. The only material views were addressed in relation to what should and should not be included in the mechanism.

3.6 For severe weather, we have decided to retain these costs as part of the cost sharing mechanism. This is discussed in Annex D. We accepted NIE Networks arguments around business rates at the draft stage and have created a separate licence term to remove these costs from the 50:50 mechanism.

3.7 Innovation costs has ultimately been retained within the 50:50 approach. We felt this to be justified on the basis that there is defined outputs/projects and we accepted that there may have been too much focus on cost restrain in the draft proposals. This is discussed further in Annex N.

3.8 We remain of the view that non-recoverable alterations are not suitable to be treated as pass-through costs. This is due to the fact that such treatment would remove the company's incentive to keep costs and activity to a minimum. This is discussed further in Annex P.

3.9 As part of our engagement with the company we did briefly discuss some alternatives to mitigating against risk. This included the potential option of moderating the strength of the cost sharing mechanism (for example reduce NIE Networks share of over-run and underspend to 35%).

3.10 We further raised the option of capping the cost risk sharing mechanism such that NIE Networks share of over-run and underspend reduces to zero once a threshold is exceeded. Another option included a review of the mechanism if a particular threshold was reached.

3.11 NIE Networks suggested that the retention of the 50:50 incentive was appropriate if other regulatory mechanisms were in place to address volatility i.e. real price effects (RPE) true-up or capital unit cost re-opener.

3.12 In the final analysis we agree with NIE Networks that this incentive still represents an important tool in encouraging efficiency and restraining cost. Consequently, no major change to the structure of the incentive has been adopted apart from removal of business rates.

4. Revenue Protection Services Incentive

Draft determination summary

4.1 The Revenue Protection Services Incentive ($RPSIt$ licence term) is where the customer and NIE Networks share certain revenue streams on a 50:50 basis. The revenue includes:

a) Money recovered from theft of electricity.

b) Money recovered from third parties for the cost of network repairs associated with theft.

c) Income from third parties for revenue protection services.

4.2 The value of this incentive can fluctuate depending on the amount of revenue recovered. This incentive is asymmetric in that there is no downside risk or penalty.

4.3 NIE Networks did not propose any change to the working of this incentive. We agreed and did not suggest any further changes.

Final determination

4.4 Despite expecting a continued increase in revenue protection activities during RP7, no further amendments to this incentive were suggested. Given that no stakeholder responses were received, we see no reason to make any changes. The currently mechanism will therefore continue unamended.

5. Worst Served Customers

Draft determination summary

5.1 Although not a financial incentive for NIE Networks, Ofgem has a fund for the WSCs who may not benefit from the relevant RIs.

5.2 For RP7, NIE Networks proposed an ex-ante allowance of £3m to address some of the issues by targeting some of the worst performing circuits. The investment includes:

- Automatic sectionalising links
- Network reconfiguration
- Undergrounding overhead line sections
- Targeted tree cutting (beyond the scope of existing tree cutting specification)
- Fitting of bird diverters
- Fitting shrouded conductor
- Use of other innovative technologies

5.3 Whilst we were supportive of the plans to address WSC issues, it was our draft view that allowance for HV overhead line works during RP7 provided sufficient funding and flexibility to allow the company to deliver its WSC aspirations.

5.4 Consequently, we did not propose a separate ex-ante allowance or WSC fund. We did however think that the WSC numbers should be monitored and reported against as part of the annual cycle, either via the RIGS or the system performance report.

Final determination

5.5 As well as the company, various stakeholder responses (including CCNI, Kelvatek and UFU) requested that we amend our position regarding this fund. It was generally felt that this was a missed opportunity to improve customer service.

5.6 During our engagement with NIE Networks, the company provided additional information to justify its request for funding. We were convinced by the new information that our draft determination of disallowing all funding required

revision. The main reason for our re-evaluation was that NIE Networks is required to carry out certain works that would not be included in the allowances for 11kV rebuild.

5.7 We are of the opinion that allowing the funding requested together with a reporting regime to measure the number of Worst Served Customers is a relatively low risk and will provide valuable learning for RP8.

5.8 To this end the funding request has been accepted along with the associated 50% WSC reduction target. We expect to develop the necessary reporting structure in the first year of the RP7 price control.