

Regulatory Financial Performance Reporting

Scottish Hydro Electric Transmission Plc
Financial Year 2022/2023



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1. Executive Summary

1.1. This commentary summarises the regulatory performance of Scottish Hydro Electric Transmission plc (SSEN Transmission) in line with the Regulatory Financial Performance Reporting (RFPR) Guidance document.

1.2. The primary focus of the RFPR is to summarise the key components of the financial performance of regulated networks by way of the Return on Regulatory Equity (RoRE). The commentary has been prepared based on the forecast average over the RIIO-T2 period rather than prioritising in-year, cumulative, historical or year-on-year performance. Analysis of average expected RoRE over the period demonstrates the forecast outcomes for SSEN Transmission, influenced by improvements in service quality for customers alongside ensuring expenditure is incurred efficiently. It is important to therefore highlight the following for readers:

- RoRE is not a reflection of customer bills, whereby a higher RoRE does not equate to higher customer bills. RoRE is intended as a reflection of Network performance whereby higher RoRE is likely to mean greater cost efficiency which leads to lower customer bills while delivering better service levels;
- The RoRE measure does not include the interest costs on borrowing. Electricity network infrastructure is financed by both borrowing funds (debt) and shareholder investment (equity) and hence, a measure which only takes into account the part of the business financed by investment is not a complete measure. The overall Return on Capital Employed (ROCE), or as we have referred to the Rate of Return (RoR), is an alternative measure which more appropriately reflects the costs to customers for the overall electricity network. This commentary therefore sets out the RoRE and the RoR for completeness; and,
- RoRE must be interpreted across the full RIIO-T2 period considering any Enduring Value (EV) adjustments and interpretation is needed as to what RoRE means for customers. Ofgem refer to EV as adjustments that are required to reflect the performance after completion of the price control including true-up and close out adjustments. Our EV adjustments are therefore reflective of our expectation for these adjustments based on Ofgem Final Determinations, the Regulatory Licence and discussions with Ofgem over the price control period. We have not reflected any adjustments from RIIO-T3 that may be interpreted as affecting the RIIO-T2 performance i.e. RoRE.

This document includes our Methodology for EV in Appendix 1. We have also briefly summarised our financial performance in this document, which corresponds to information provided to Ofgem set out in documents submitted under the Regulatory Instructions and Guidance (RIGs). Note that the financial values required to be reconciled within the RFPR have been reconciled to the audited statutory accounts for each applicable year in accordance with the Regulatory Instructions and Guidance (RIGs).

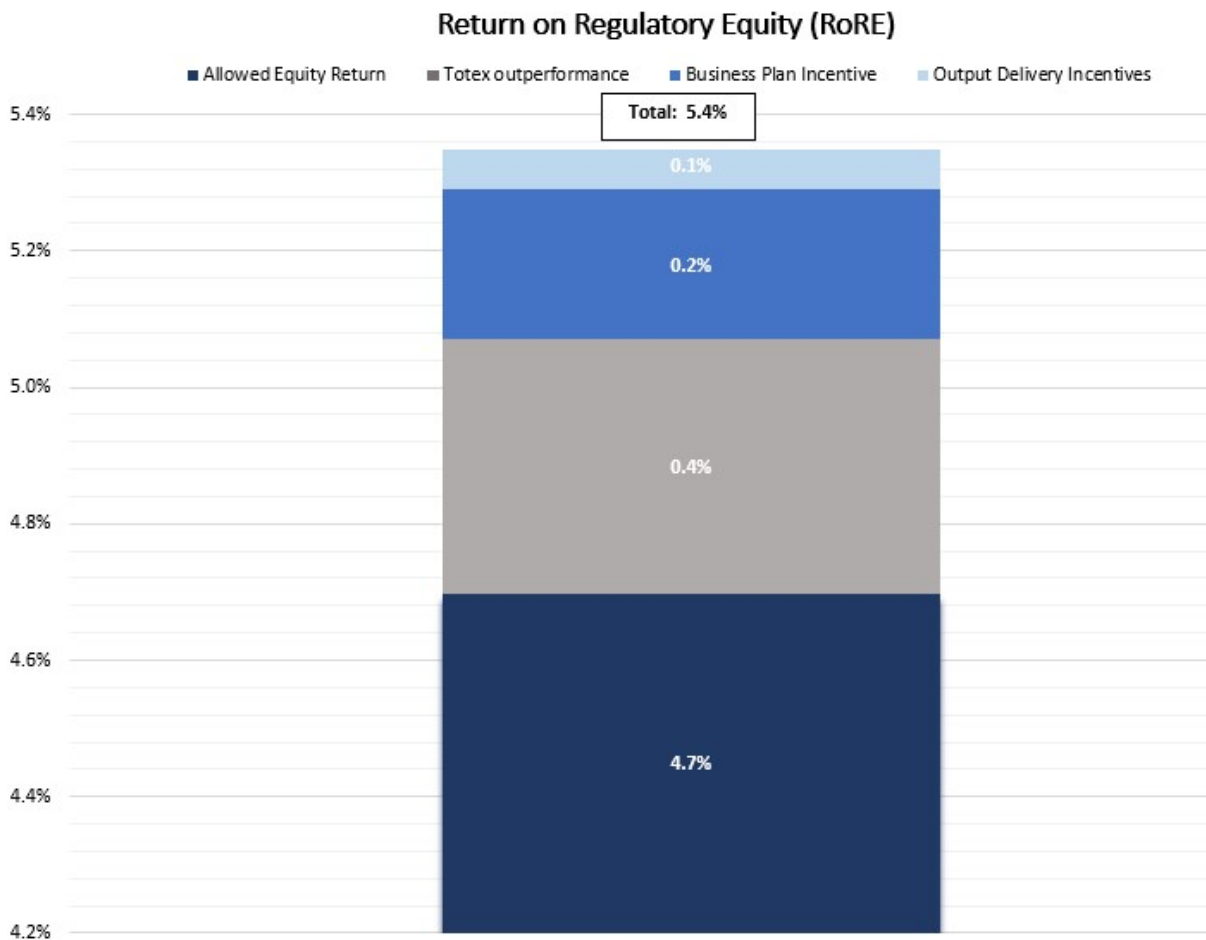
2. Return on Regulatory Equity (RORE)

2.1. The RoRE for the RIIO-T2 period on average for SSEN Transmission can be seen in Figure 1 below. SSEN Transmission has the opportunity to earn above its base return on equity through (allowed return on equity) delivering efficiency savings on operating and capital expenditure (referred to as total expenditure or 'totex'). Additionally, if customer service levels improve against targets set by Ofgem, there is an opportunity to earn additional income through incentives. In the event that service levels fall below targets set, a penalty will be incurred which reduces network revenue and therefore customer bills. This ensures that customers only compensate networks where they receive improving service levels. Further, customers benefit from reduced bills when networks achieve efficiency savings on totex expenditure.

2.2. SSEN Transmission seeks to improve customer service levels while also delivering efficiency savings. We believe this strategy ensures customers obtain a better service while targeting lower bills.

2.3.

Figure 1 – Operational Return on Regulatory Equity (RoRE) for the RIIO-T2 period for SSEN Transmission



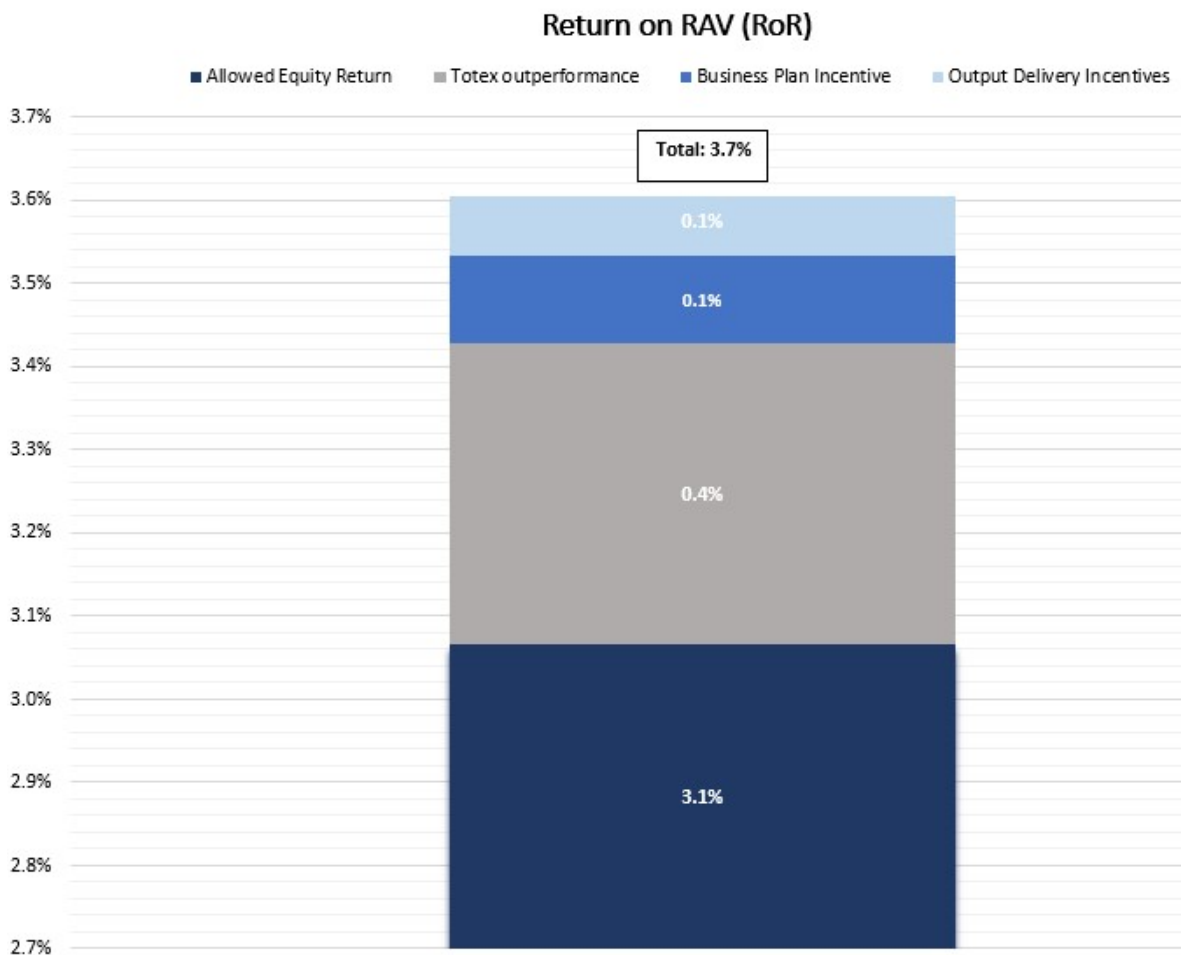
2.4. SSEN Transmission is forecasting efficiencies in totex on large capital projects across the period resulting in an outperformance of c.0.7% RoRE over the allowed return on equity of 4.7% for the period. It is worth emphasising that the incentive framework for RIIO-T2 is predominantly focused on totex efficiency as earned from the Totex Incentive Mechanism (TIM) due to the large capital programme expected across Transmission Operators (TOs).

2.5. SSEN Transmission is focussed on improving customer satisfaction and network reliability and this has been realised through incentive rewards of c.0.1% increase to RoRE. SSEN Transmission is making above the allowed or base return on equity at an operational level. This is a measure of the performance of each Network excluding the impact of borrowing and tax costs, and is referred to as the operational RoRE.

2.6. As noted above, at the operational level, SSEN Transmission is achieving above base return at 5.4%. The impact of debt performance accounts for an additional 2.9% return whilst tax performance accounts for a (0.2)% return. The total return including debt and tax performance is there 8.1%, however the tax underperformance is due to timing. Ofgem’s inflation forecast for the remainder results in a real reduction in SSEN Transmission’s cost of debt. The result is an effective debt outperformance, increasing RoRE.

2.7. Figure 2 below sets out the Rate of Return (RoR) as an alternate measure of performance (this is measured by a Return on RAV instead on Regulated Equity). This is reflective of the gearing and cost of borrowing that customers pay for through use of the Transmission Network, as opposed to a shareholder focused rate of return in the form of RoRE.

Figure 2 – Operational Return on RAV (RoR) for the RIIO-T2 period for SSEN Transmission



2.8. At an operational level, SSEN Transmission forecasts c.3.7% due to a higher base cost of equity and efficiencies made on totex. SSEN Transmission continues to make a return above the allowed Weighted Average Cost of Capital (WACC) when including the impact of financing and tax performance. The impact of financing and tax performance improves the overall return for SSEN Transmission by c. 1.4%.

3. Reconciliation to Revenue and Profit

Reconciliation to Revenue

3.1. Revenues are in line with the Price Control Financial Model (PCFM) and the revenue tariff setting process. This process allows each licensee to recover base revenue plus any incentive revenues earned and pass through items. Allowed revenues captured within the RFPR are directly sourced from the Revenue RRP submitted to Ofgem.

3.2. We recover our revenues through charges to the system operator, National Grid, who in turn, levy charges on users of the transmission system across Great Britain.

- 3.3.** Recovered Transmission Network Revenue totalled £632.8m for 2022/23. Given the timeline, the use of forecasts and other economic factors which can affect demand; we may under or over recover what our allowed revenue is set as for tariff setting. Consequently, we true up, by increasing or decreasing, future allowed revenue under the K correction factor term as detailed in our licence. The amount of under recovered revenue for 2022/23 totals £29.6m which will be adjusted through future years allowed revenues.
- 3.4.** The reconciliation to Statutory Accounts is based on SSEN Transmission's underlying accounting records, which report revenues separately between statutory segments. As such, the reconciling items disclosed in the table are derived from non-regulated revenue. We receive income for non-regulated activities. These services are called Directly Remunerated Services (DRS). These are not covered by the price control, however charges are calculated in accordance with our license. Other reconciling non-regulated revenue segments include innovation and de-minimis income.

Reconciliation to Profit

- 3.5.** The reconciliation to Statutory Profit is based on SSEN Transmission's underlying accounting records. Differences between regulatory and statutory profit are to be expected and arise from the varying treatment of regulatory and statutory items. An example of this is the accounting for regulatory tax against statutory tax.
- 3.6.** The 2021/22 reconciliation to profit has been restated to reflect an updated tax position in alignment with the final CT600 return for the 2021/22 financial year.

4. Totex Performance

(18/19 prices)

- 4.1.** Both the actual and forecast totex performance built into the RFPR is in line with the latest Regulatory Reporting Pack (RRP) submitted to Ofgem at 30 September 2023.
- 4.2.** SSEN Transmission's total forecasted expenditure for RIIO T2 is £5,137m against allowances of £5,239m (after accounting for EV adjustments) resulting in an underspend of c.2% totex allowances during the five-year RIIO-T2 period.
- 4.3.** Outperformance has been forecast for our load RIIO-T2 Certain view schemes driven by a combination of innovation, intelligent/value engineering and efficiencies in the contracting strategy. Outperformance has also been forecast in Closely Associated Indirect (CAI's) costs in part due to the automatic allowances funded through the opex escalator for Medium Sized Investment Projects (MSIP) and Volume Driver Reopener projects. Overall outperformance was however partially offset by both higher CAI costs driven by increased headcount, required for pathway to 2030 projects and increased Business Support Costs (BSC) costs attributed to corporate recharges, part of which is attributed to ASTI works.
- 4.4.** Totex forecasts include relevant EV adjustments, see Appendix 1 for EV Methodology and detail on the adjustments made.

5. Incentives and Other Revenue

- 5.1.** This section details our Output Delivery Incentive performance and other Revenue for the regulatory year 22/23. Incentive values are directly sourced from the Revenue RRP submitted to Ofgem. SSEN incentive performance for 2022/23 is explained below. Forecast incentives are based on average of historic performance and management's experienced best estimate unless otherwise stated.
- 5.2.** This year the Electricity Transmission business has again continued to deliver strongly on the five primary RIIO-T2 output areas: Safety, Reliability, Customer Satisfaction, Connections and Environment. All Output Delivery Incentives are meeting or exceeding their baseline.

Energy Not Supplied Output Delivery Incentive

- 5.3.** The number of Transmission System Loss of Supply Incidents in 2022/23 was low, decreasing on the prior year from 3 to 2. The incidents were non-incentivised events and as a result did not impact the incentive reward. The Loss of Supplies incentive was fulfilled with these Loss of Supply incidents discounted, thus achieving 102MWh to meet targets. There is continuing focus on maintenance and investment, with a view to keeping the number of incidents low, by ensuring high availability, good design and prudent operations.
- 5.4.** Building on its strong track record of consistently delivering over 99.99% network reliability - and in line with its RIIO-T2 goal to aim for 100% transmission network reliability for homes and businesses - in 2022/23, the Company achieved the full incentive reward of £0.7m (18/19 prices) through the Energy Not Supplied Incentive. We expect to achieve the maximum reward for the remainder of the RIIO-T2 price control period.

Insulations and Interruption Gas (IIG) leakage Incentive

- 5.5.** During 2022/23, our IIG leakage was 0.29% - outperforming the incentive target (0.38%) and sector leading. However, our ambitious Science-Based Target requires absolute leakage reductions even as our installed volume grows with our growing network. This is extremely challenging and all efforts are focussed on reducing our SF6 emissions wherever possible.

Timely Connections Output Delivery Incentive

- 5.6.** For the period April 2022 to March 2023, 177 connection offers were issued to NGENSO; 100% of the offers issued were issued in line with our licensed obligations. Of these, 49 offers were for onshore wind (28%), 57 were for battery storage (32%), and 8 were for offshore wind (5%). This is a penalty only incentive and the 2022/23 result of nil penalty has been forecasted for the remainder of the RIIO-T2 price control in line with business targets.

Quality of connections satisfaction survey Output Delivery Incentive

- 5.7.** The Quality of Connections Satisfaction Survey Score is based on connection customer survey responses at six key milestones over the duration of the connection process:
- Pre Application Engagement
 - Application Process & offer
 - Development Phase
 - Delivery Phase
 - Outage Management
 - Connected Customer Reviews

5.8. For 2022-23 reporting, we achieved over the baseline target with an overall Quality of Connections score of 8.6 which is estimated to achieve an incentive reward of £1.8m (18/19 prices). Forecasted incentive rewards are reflective of a programme of work under way which we are aiming to deliver throughout 2023/24. This work will involve engaging with customers and stakeholders to develop and adapt ways of working. We would expect to see the benefits reflected in a further increase in the QoCS score for 2023/24 and beyond.

SO-TO Optimisation Output Delivery Incentive

5.9. This represents our submission in accordance with Part C of Special Condition 4.7 of the electricity transmission licence and the SO:TO Optimisation Governance Document. During 2022/23, we delivered one additional project under STCP 11-4 and within scope of the Output Delivery Incentive (ODI).

5.10. The project supports the installation of a new 275kV quadrature booster (QB) on the XT2 feeder bay at Tealing 275kV substation. Its purpose is to adjust flows through the XT2 circuit, in order to utilize higher available capacity on the larger boundary transfer circuits. Civil works for the QB are being completed during late 2022 and early 2023, with the QB installation and commissioning in late 2023.

5.11. The consumer benefit associated with delivering this project was estimated by the ESO at a total constraint saving of £29.95M, however the actual outturn savings at the 2022/23 year end amounted to £12.37m. Our potential incentive reward per the licence is calculated as 10% of the ESO's forecast constraint savings, capped at £1.2m (18/19 prices).

5.12. The ODI continues to encourage us to proactively consider solutions in the form of enhanced service provisions that minimise outage impact, and, ultimately, pass cost savings to end consumers.

Environmental scorecard Output Delivery Incentive

5.13. This table and narrative is not required for year 1 and 2 of the RIIO-T2 price control. This is an optional incentive which we have opted not to switch on at present. We have retained the option to switch on some elements of this ODI in the future years of RIIO-T2.

Innovation

Network Innovation Allowance (NIA)

5.14. The Network Innovation Allowance (NIA) project progress is detailed in the annual summary of NIA activity stipulated by the RIIO-2 NIA Governance Document. The report is available on the Smarter Networks Portal, at <https://smarter.energynetworks.org> and published at <https://www.ssen-transmission.co.uk/about-us/innovation/> on 31st July 2023.

5.15. Throughout 2022/23 we have been engaged in developing further NIA innovation projects to grow the RIIO-2 portfolio. Projects in development are aimed at delivering significant value and cost savings back to the consumer and include addressing the following:

1. Alternative insulating gas performance (to SF6)
2. Alternative methods for foundation uplift design
3. Alternative ice accretion and corrosion mapping methods; and
4. Probabilistic modelling for connection studies
5. Overhead line alternatives

5.16. In 2022/23, SSEN Transmission incurred £1.0m (18/19 prices) of NIA expenditure.

Carry forward RIIO-1 Network Innovation Allowance (CNIA)

5.17. RIIO 2 permits a carry forward allowance on NIA for the first year only in RIIO-2, therefore no expenditure has been incurred relating to RIIO-1 NIA projects in 2022/23.

Strategic Innovation Fund (SIF)

5.18. For RIIO-2, Ofgem launched the Strategic Innovation Fund (SIF), a new funding mechanism for networks that aims to find and fund ambitious, innovative projects with the potential to accelerate the transition to net zero. We participated in the first round of the SIF by identifying and developing three innovation proposals that had the potential to meet the challenge criteria's set out by Ofgem for participation in this project. The first phase, known as 'Discovery,' provides project funding up to a maximum of £150k, to deliver an early-stage feasibility over an 8-week period that seeks to inform the approach for the later stages of the project.

5.19. Our Round 1 Discovery projects successfully completed in June 2022 and two of these progressed to the second phase being the Round 1 Alpha phase. Both of our Round 1 Alpha phase projects completed successfully in January 2023 and these have both been submitted to the Round 1 Beta application process, expected to be decided later in 2023. We also participated in the second round of the SIF by, again, identifying and progressing three innovation proposals to meet the new challenge criteria specified by Ofgem. These three SIF Round 2 projects are currently in the Discovery phase.

5.20. We incurred £0.8m (18/19 prices) of SIF funding expenditure in 2022/23.

6. Financing and net debt

6.1. The actual gearing for the SSEN Transmission has generally been in line with the notional gearing set for RIIO-T2, with annual variations due to the timing of expenditure, revenues and cash flows.

6.2. The cost of debt performance against allowance varies across each network due to the cost of embedded debt and differing cost of debt allowance mechanisms. It is worth highlighting that the methodology does not reflect the cash cost of interest and is instead the economic form of outperformance due to removal of inflation from the effective interest rates. Furthermore, the methodology does not allow for additional costs of borrowing such as transaction costs, liquidity costs and the impact of issuing longer or shorter-term debt depending on the most appropriate and efficient treasury policy.

6.3. SSEN Transmission outperforms the cost of debt allowance due to the low interest rate environment. This has pulled down the cost of debt index allowance while the licensee has been able to borrow in line with capital markets.

6.4. The updated presentation of R6 – Net Debt in 2022/23 has resulted in an additional disaggregation of debt by type. The 2021/22 net debt has been restated in order to reflect all Group intercompany loans only excluding any intercompany trading balances in line with the statutory and regulatory definition of net debt. The Other category reflects finance lease balances.

7. RAV

7.1. RAV is presented as per the PCFM. The totex forecast per the RRP has been reflected in forecast RAV additions, which are calculated based on a set capitalisation rate. EV adjustments have been made to totex for SSEN Transmission, with the impact being reflected in RAV. The EV Methodology in Appendix 1 outlines details of the EV adjustments made for SSEN Transmission as well as the basis of assessment.

8. TAX

8.1. The tax allowance is calculated through the PCFM, based on a fixed split percentage of tax pool additions, and forecast nominal financing costs (net interest paid). There are several variances between the regulatory allowance and the CT600 tax liability, primarily due to differences between regulatory and statutory accounting treatments.

8.2. The CT600 reflects company performance on items both within and outwith the price control, including total collected revenue inclusive of an in year over recovery. Other variances relate to differences in regulatory and statutory asset lives and capital allowances.

8.3. Additionally, the CT600 calculates allowances on the actual annual opening balances of each respective tax pool category whilst the PCFM has not reflected a true up on opening balances since the commencement of RIIO-T2.

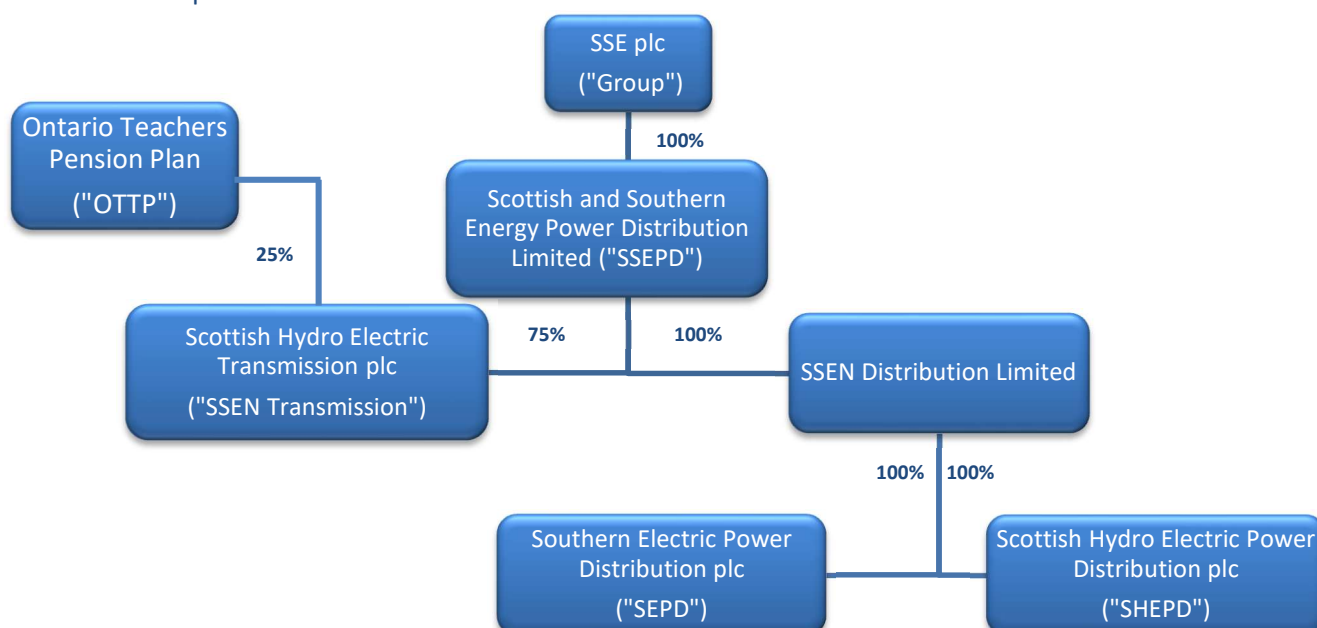
8.4. Most of our assets are Special Rate Pool items and have attracted a rate of 50% from the Government's Super Deduction regime on main rate and special rate items in both 2021/22 and 2022/23 (for first year additions only). The 2023 CT600 is not yet due for submission to HMRC, consequently the 2022/23 value in tab R8 is a forecast to compare against the allowance.

8.5. In March 2023, the government announced that full first year allowances would be available on qualifying expenditure from 2023/24 to 2025/26. The government has also relaxed the contractual eligibility restrictions for qualifying expenditure. It is now expected that the majority of SSEN Transmission main and special rate expenditure will qualify for first year allowances. The forecast tax liability is expected to lower which also equates to a lower expected PCFM tax allowance for the remainder of RIIO-2.

9. Corporate Governance

9.1. SSEN Transmission was a wholly owned subsidiary of SSE plc (the "Group") until 25 November 2022, following the Group's sale of a 25% non-controlling equity stake in SSEN transmission to Ontario Teachers' Pension Plan. The Company's immediate parent is Scottish and Southern Energy Power Distribution Limited (SSEPD). Included within the SSEN group are sister companies, Scottish Hydro Electric Power Distribution plc (SHEPD) and Southern Electric Power Distribution plc (SEPD). The Company owns the Electricity Transmission network in the north of Scotland.

Summarised Corporate Structure:



9.2. The Company was governed by the Scottish and Southern Energy Power Distribution Board - which also governed sister companies, Scottish Hydro Electric Power Distribution plc (SHEPD) and Southern Electric Power Distribution plc (SEPD) - until 25 November 2022. This changed following the sale of a 25% non-controlling equity stake in SSEN Transmission to Ontario Teachers' Pension Plan, from which point the governance of SSEN Transmission's activities transferred to the Company Board.

9.3. As at 31 March 2023, the Company Board comprised of two Executive Directors and seven Non-Executive Directors one of whom is the Chair of the Company Board, an Executive Director of the Group Board and member of the Group Executive Committee. None of the Directors are Directors of Group Companies involved in Retail or Wholesale activities.

9.4. Two of the Non-Executive Directors on the Board during the course of the financial year were Sufficiently Independent Non-Executive Directors as required under the terms of Standard Condition B22 of the Company's regulatory licence. The Directors believe that the Company Board is an appropriate size and has a good balance of independence and experience, ensuring that no one individual or group of individuals has undue influence over the Company Board's decision making. The Board of Directors are as follows:

- Gregor Alexander (Non-Executive Director) (Chairman) (appointed 1 October 2002)
- Rob McDonald (Executive Director) (appointed 31 January 2019)
- Maz Alkirwi (Executive Director) (appointed 23 February 2021)
- Charlotte Brunning (Non-Executive Director) (appointed 22 December 2022)
- Charles Thomazi (Non-Executive Director) (appointed 30 November 2022)
- Rachel McEwen (Non-Executive Director) (appointed 27 May 2016)
- Ronald Fleming (Non-Executive Director) (appointed 30 November 2022)
- Laura Sandys (Independent Non-Executive Director) (appointed 1 February 2022)
- Gary Steel (Sufficiently Independent Non-Executive Director) (appointed 1 April 2014)

9.5. The Executive Directors are experienced senior business leaders and are deemed to possess the appropriate breadth of knowledge and expertise to discharge their role effectively. The Non-Executive Directors provide an appropriate degree of independent judgement and challenge to ensure balanced and

fair decision-making and outcomes. The operation and effectiveness of the Board is the ultimate responsibility of the Chair, who is supported in their role by the Company Secretary. Agreed procedures are in place to manage and mitigate actual or potential conflicts of interest with Board or Company business.

- 9.6.** The Board presides over matters including the Company's purpose, value and strategy, as well as dividend policy. The Board does not have a supporting Nomination, Remuneration or Audit Committee. These functions are dealt with, where required, in conjunction with the relevant committee of the SSE Group Board.
- 9.7.** On appointment all Directors receive induction to the Board and briefings on areas pertinent to their role such as a Director's legal duties. The ongoing effectiveness of the Board is supported by performance evaluation and a commitment to personal development and training by each Director.
- 9.8.** Regular Board evaluation is facilitated by the Company Secretary, through which the Director's reflect upon, and agree, areas for improvement based on an objective assessment of the Board's operations. Following such assessments, actions are implemented and tracked in advance of further performance evaluations in 2023/24.

Executive Remuneration Policies

- 9.9.** The Remuneration of the Director's is set in line with overall SSE Group policy. Dividends are paid based on cash flow management of the licensee over a prolonged period. The licensee's dividend policy is therefore subject to annual variations based on cash flow requirements and expectations of shareholders while maintaining actual gearing in line with notional gearing and continuing to invest in each electricity network accordingly. All Dividends are approved by the Board of Directors and paid up to SSE plc. The SSE plc Board are responsible for proposing the dividend issued to shareholders in line with SSE plc's dividend policy which is subject to approval at the SSE plc Annual General Meeting.

10.Pensions

- 10.1.** Pension allowances are in line with the Pensions Reasonableness Review submitted in September 2023. This is subject to ongoing review by Ofgem. The figures in R10 Pensions & Other Activities reflect the total of established and incremental TO costs associated with the Scottish Hydro Electric Pension Scheme (SHEPS). The actual surplus values are then compared to the allowance values that were derived from the latest Triennial actuarial valuation which took place on the 31/03/22. Pension allowances do not directly affect the RoRE or RoR, except as part of a component of totex expenditure for ongoing service contributions.

11.Data Assurance Statement

- 11.1.** This submission has been completed in line with the Data Assurance Requirements Standard Licence Condition B23. A Risk Assessment was conducted, and the Total Risk Rating was Low. The appropriate level of assurance activities has been employed commensurate with this risk rating including a submission plan, methodology and appropriate level of review and sign off.

Appendices

Appendix 1 - Enduring Value Methodology

A1.1 Introduction

The Enduring Value (EV) Methodology is based on a fundamental review of each licensee's regulatory price control, outputs, totex allowances and expenditure. SSEN Transmission's approach to making EV adjustments is underpinned by a consistent approach in applying the principles of RoRE and the underlying drivers of the price control. Only adjustments that are considered material in nature to the outcome of RIIO-T2 are considered to be appropriate in order to avoid overcomplicating the RFPR unnecessarily whereby the full price control performance is most relevant compared to in-year or year-on-year performance. Therefore, SSEN Transmission has focused primarily on price control Network Output Measures (NOMs) as known at the time of preparation of the RFPR and the known or expected outcome of submitted regulatory reopeners.

The assumptions for EV adjustments have been prepared consistently with the 2022/23 RRP submissions. Any EV adjustments are based on the assumptions by SSEN Transmission management at the time of preparing the RFPR and RRP and are subject to change as matters arise and circumstances change during the price control.

The methodology and approach considered for EV in the RFPR has been summarised below. This outlines how, in future years, SSEN Transmission will consider these factors when preparing the RFPR. The EV Methodology will be reviewed annually for appropriateness as part of preparing the RFPR.

A1.2 SSEN Transmission

For SSEN Transmission the RIIO-T2 price control is in its third year and RIIO T1 close out methodologies are being finalised by Ofgem. SSEN Transmission has adopted the following approach and considerations in relation to the EV adjustment:

1. **RIIO-T1 Legacy Outputs and expenditure** – There are a number of RIIO-T1 projects and related expenditure spanning from the final years of RIIO-T1 into the first years of RIIO-2. These are primarily in relation to Generation Connections driven infrastructure which complete in RIIO-2 (pre-31 March 2023). Adjustments have been made to remove expenditure and allowance for the delivery of load related RIIO-1 projects whereby the completion of the output falls within the first two years of the T2 period. This is in line with the RIIO-2 Final Determination.
2. **T1/T2 Volume Driver Crossover Projects** – There is spend and allowances associated with RIIO-T1 volume driver projects which deliver outputs in the first two years of RIIO-T2 have been excluded from our RIIO-T2 reported performance as these have also been accounted for within RIIO-T1 reported performance.
3. **T2/T3 volume driver** – Allowances are included for T2/T3 volume driver projects that connect within the crossover period (first year of RIIO- T3).
4. **Sole use exit/entry connections** –The sole use exit connections allowance will be trued-up to actuals at the end of RIIO-T2. Sole use entry connections will also be treated in the same way as well as the forecasted income deducted from base revenue in the PCFM. There is therefore an EV adjustment within the RFPR to reflect the allowances to actual for both sole use exit and entry connections.
5. **T1 Visual Amenity** - We have made an adjustment for the RIIO-T2 overspend on Glen Falloch (T1 approved scheme) as performance has also been accounted for within RIIO-T1 reported performance.
6. **T3 schemes** - We have made an adjustment to exclude certain costs from our RIIO-T2 performance which relate to future T3 connection schemes that are unlikely to go ahead. If these are cancelled, costs would be recovered directly from the customer. If these go ahead, these will likely form part of the RIIO-T3 or RIIO-T4 settlement.

7. **RPE Adjustment** – The revenue allowance in the latest published PCFM has an estimate in excess of internal analysis and we have therefore factored in the difference between estimate and allowance as an enduring value adjustment.

No EV adjustments have been considered for incentive mechanisms for RII0-T2. This has been deemed out of scope and is based on earned in year calculations or awards.

Appendix 2 - Basis of any estimates and allocations

Estimates are restricted to forecast information. Forecasts have been constructed as follows:

Totex – forecasts match the latest 2022/23 submitted RRP. Within the reconciliation to totex, the 'Other' line includes elements of rounding in line with the materiality agreed with Ofgem.

Incentives – forecasts are based on of the average incentives earned for the price control period to date as well as taking account of the future targets which licensees have set to the end of the price control. Incentives earned in year are based on the same model, with the 2 year lag and inflation adjusted out.

Innovation – forecasts are based on the average innovation revenues for the price control period to date.

Financing – forecasts for interest on existing debt are based on SSE Treasury forecasts of interest payable based on the expected interest rate for each instrument. Forecast interest cost for new debt is based on the value of new debt multiplied by the price control cost of debt for the relevant year.

Net debt – forecasts for existing debt are based on SSE Treasury forecasts of the movement in debt based on the arrangements in place.

Tax – forecast tax liability is based on the proportion of the average adjusted actual tax liability for the price control to date versus the forecast regulated profit for the remainder of the price control period.