FGO

OUTLINE FOR FINANCIAL TRANSITION

This paper sets out the arrangements for financial transition which will be included in the Transitional Arrangements Document.

1 Basic principles

1.1 All costs of all Xoserve activities carried out on and from 1 April 2017 (**FGO Implementation Date - FID**) will be costs of the CDSP to be included in the CDSP's first year budget (**First Year Budget**) and recovered under the Budget and Charging Methodology.

1.2 Consistent with the accruals basis of accounting for CDSP, subject as set out below:

(a) costs and revenues accruing before the FID are excluded from the First Year Budget (and in the year-end reconciliation for the first year)

(b) costs and revenues accruing on or after the FID are counted in the First Year Budget (and in the year-end reconciliation for the first year).

1.3 Under the ASA, GTs will fund the investment costs of Xoserve which accrue up to FID. Investment costs accruing on or after FID (including costs associated with on-going investment projects) will be included in the First Year Budget and covered by the Budget and Charging Methodology.

1.4 CDSP continues with the activities, assets and liabilities of Xoserve on an 'as-is' basis on the FID. There is no basis on which any cost or saving of the CDSP which accrues after FID can be excluded from the CDSP budget (or from recovery or rebate under the DSC) on the grounds that it results from anything done before the FID. The statutory accounts for Xoserve for the 2016/17 year will make provision (in accordance with GAAP[1]) for liabilities then known.

2 First Year Budget

2.1 The First Year Budget, and the charging statement for the first year, will be established in accordance with the Budget and Charging Methodology as if the DSC were already in force. The Transitional Arrangements Document will deem the budget to have been so established.

2.2 The appeal mechanism provided for in the FGO licence condition will apply to the First Year Budget[2].

3 Initial Working Capital

3.1 Xoserve forecasts that there should be no requirement for additional financing from a third party to provide the working capital required by the CDSP on the FID, as set out in the First Year Budget. If this expectation changes Xoserve's expectation is that financing would be obtained from a commercial lender.

4 Specific matters

4.1 Nexus

Following FID GTs will fund Nexus delivery and GTs will continue to have residual liability for a defined period following the Project Nexus Implementation Date and the later date for implementation of the RAASP elements of Nexus. In each case the period will approximate to the three month period after the relevant date when 'post implementation support' is available, and the residual liability will extend to specific 'fix on fail' costs to be identified[3].

5 Close-out of existing arrangements

5.1 The arrangements for closing out the existing arrangements, together with the closing dividend, correspond to the exclusion from CDSP recovery of costs/revenues accruing pre-FID.

5.2 ASA[4][5]

5.3 User Pays Agreements[6]

5.4 The activities under 5.2 and 5.3 are treated as taking place under the ASA / User Pays Agreements and are outside of the scope of authority of any DSC Committee.

5.5 [Issues around third party services[7]]

A note on pensions[8]

To date any Xoserve pension deficit liability is not separately identified within the NGG defined benefits pension scheme. Any deficit would be recoverable through the transmission price control. There is no proposal to change this treatment.

Since the start of RIIO any deficit costs relating to post-March 2013 service are not directly recoverable. Under RIIO pension provision is treated as an employment cost, and costs post-March 2013 are treated as part of the total expenditure calculation (totex). The totex incentive mechanism allows for some sharing between licensees and customers, so some element of the additional costs are recoverable.

The first calculation of any deficit for post RIIO service will be based on a March 2016 valuation, and a portion of any deficit will be notionally attributable to Xoserve employees. It is yet to be determined whether any such cost will be treated as totex or allocated to Xoserve. If the cost was allocated to Xoserve and recovered over a period of up to 15 years the annual cost is expected to be < £100,000 (though this is subject to the actual valuation).

In summary, most deficit risk relates to the pre-March 2013 period and is funded through the transmission price control. Post-March 2013 risk is limited as it relates only to post-March 2013 service and the defined benefit membership is in decline.