BEFORE THE COMPETITION AND MARKETS AUTHORITY
AN APPEAL UNDER SECTION 11C OF THE ELECTRICTY ACT 1989

BETWEEN

Scottish Hydro Electric Transmission plc

(trading as SSEN Transmission)

(***Appellant***)

and

Gas and Electricity Markets Authority

(***Respondent***)

APPELLANT'S REPLY SUBMISSION

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10 May 2021

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Defined terms and abbreviations

Abbreviations and capitalised terms used but not defined in this Reply have the meaning given in SSEN Transmission's Notice of Appeal filed with the CMA on 3 March 2021.

Section 1: Introduction

1.1 This Reply is filed on behalf of SSEN Transmission in reply to the representations and observations of the Gas and Electricity Markets Authority (the ***Respondent*** or ***GEMA***) dated 23 April 2021 (the ***Response***).[1]

1.2 This Reply is accompanied by, and incorporates, the following supplemental witness statements responsive to points raised in the Response:

(a) ***Hope-3***: Mr Hope's third witness statement which exhibits Oxera's WACC Report;

(b) ***Hope-4***: Mr Hope's fourth witness statement which exhibits Oxera's WPD Report; and

(c) ***Alkirwi-2***: Mr Alkirwi's second witness statement addressing TNUoS.

1.3 In line with the CMA's direction, the Appellant has sought to keep this Reply concise and devoid of unnecessary repetition. Where the Appellant does not expressly respond to a particular paragraph of the Response, it should not be considered an acceptance of GEMA's position.

Section 2: Executive Summary

2.1 Although voluminous, none of the arguments in GEMA's Response alter the conclusion that GEMA has fallen into material error in each and every respect articulated in SSEN Transmission's Notice of Appeal.

2.2 This Reply, and accompanying documentation, analyses and explains why GEMA's arguments in relation to each of SSEN Transmission's four grounds of appeal are fundamentally flawed and, accordingly, why the CMA should grant the relief that SSEN Transmission seeks under those grounds. SSEN Transmission has sought to keep this Reply as short and targeted as possible, while ensuring that it provides the necessary responses to the wide-ranging (and often irrelevant / obfuscatory) positions that GEMA has adopted.

2.3 The key conclusions of this Reply are set out from paragraphs 2.4 - 2.13 below.

2.4 **GEMA cannot shield its serious errors from correction under the cloak of "*discretion*".** GEMA does not have unlimited "*discretion*" to set the cost of equity. As a key component of GEMA's price control decision, GEMA's decision on the cost of equity is subject to appeal before the CMA on the same basis as all other aspects of its price control decision. Contrary to the position put forward by GEMA, the WACC is not an 'unknowable' value. Nearly all of GEMA's arguments responding to the cost of equity grounds are underpinned by the refrain exemplified in Mr Wilde's claim: "*if the true WACC can never be known, GEMA's view for Step 1 (CAPM) should be difficult to be found 'wrong'*".[2] In reality, the value of the CAPM parameters, and the method followed to set them in regulatory decision-making, is objective and well-understood by regulatory economists. Like other UK economic regulators, GEMA is required to make its decision after taking into account relevant evidence and information. GEMA's decisions on whether to take account of and/or place (or not place) weight on particular evidence are therefore not matters of unfettered discretion. Where, as in this case, GEMA has not taken account of relevant evidence or data, and placed weight on unreliable data, this is clearly an error which can – indeed must – be corrected by the CMA. GEMA's submission that its decision on the cost of equity was within its unreviewable discretion would negate the basis of the appeal process before the CMA under section 11E(4) of the EA 1989 and undermine confidence in the system of regulation and appeals for price control decisions. GEMA's attempt to hide behind discretion betrays a lack of confidence in the substance of its decisions and must be rejected.

2.5 **GEMA's Response on RFR fails to engage with SSEN Transmission's evidence on the convenience premium embedded in its chosen ILG proxy and SSEN Transmission's better evidence on AAA-rated corporate bond yields**. GEMA baldly asserts that "*ILGs are what they are and provide a reasonable proxy*

[1] The Reply adopts the defined terms from its Notice of Appeal unless stated otherwise.

[2] **Wilde 1** / **Para. 29.1**.

for the unobservable RFR".[3] This loose assertion does not begin to overcome SSEN Transmission's position, which adduced the: (i) weight of academic and expert evidence that ILGs are affected by the convenience premium, including Oxera's finding of a negative correlation between UK gilts and equity returns; (ii) observable gaps between corporate and sovereign risk-free rates; and (iii) fact that equity analysts covering UK regulated utilities use RFR assumptions that account for the convenience premium. GEMA seeks to dismiss SSEN Transmission's evidence on AAA-rated corporate bond yields solely on the basis that those yields would require some adjustment (for corporate bond-specific factors). GEMA's position is unsustainable because it is clear that its chosen ILG cannot properly be used without adjusting for the convenience premium. GEMA's decision to ignore relevant evidence of AAA-rated corporate bond yields and to rely on its unadjusted ILG is wrong and the Response does not set out any convincing submissions or evidence to the contrary.

2.6 **GEMA's Response fails to explain why it ignored the best evidence on inflation data.** Nothing in GEMA's Response on TMR effectively addresses the evidence set out in SSEN Transmission's Notice of Appeal that: (i) the RPI data series is the best inflation data for use in setting the TMR element of the cost of equity (which was also relied on by the CMA in its recent PR19 decision); (ii) the CPI data relied upon by GEMA has flaws; and (iii) it was a clear error to employ geometric rather than arithmetic averaging.

2.7 **GEMA's Response on its use of water company comparators to estimate beta fails to engage with the objective market data showing that energy networks carry a systematically higher beta than water companies**. Instead, GEMA relies on a **subjective** "***judgment…in the round***"[4] without any proper basis for this "*judgment*" or verifiable mathematical weighting. GEMA's Response exposes that, in reality, it had no proper basis for this decision. Furthermore, GEMA provides no convincing answer to the additional errors identified by the Appellant, in particular that GEMA: (i) included illiquid outliers in its sample of European energy network comparators to estimate asset beta; (ii) relied on inappropriate comparisons between the French energy sector and the UK energy sector; and (iii) relied on biased data in its debt beta calculation.

2.8 **GEMA puts forward no convincing basis for its decision to depart from regulatory practice and principle on 'aiming up'.** Instead of engaging with the substance of SSEN Transmission's arguments and evidence, GEMA again seeks to hide behind its "*discretion*". This misses the point. SSEN Transmission's Notice of Appeal sets out clear economic and statistical evidence demonstrating (i) the consumer benefits associated with aiming up; and (ii) the particular need to do so in the electricity transmission sector in RIIO-2 given the significant investment required over the period (especially in light of the significant drop in the cost of equity since RIIO-1). GEMA did not have "*discretion*" to ignore this evidence and nothing in the Response refutes SSEN Transmission's submission that GEMA was wrong, and inconsistent with its statutory duties, to depart from this established principle (recently reaffirmed by the CMA in its PR19 decision).

2.9 **GEMA's Response on cross-checks** fails to adequately address the catalogue of errors identified in SSEN Transmission's Notice of Appeal. GEMA's attempt to exaggerate the significance of the WPD transaction as a further plausible cross-check is misleading because it is not possible to draw any valid inferences relating to sector-wide outperformance from a single acquisition involving: a complex deal structure; a frontier company; and likely synergies.[5]

2.10 **GEMA's Response on the Expected Outperformance Adjustment** fails to engage with SSEN Transmission's (and all nine Appellants') arguments that the advent of this adjustment represents an unprincipled departure from regulatory precedent, and from the position set out in the RIIO model's foundational documents. GEMA does not explain why its decision to introduce this adjustment will not undermine the fundamental principles of incentive-based regulation or why it was necessary to adopt this unprecedented measure given the other measures it adopted in RIIO-2 to increase the challenges for company performance. GEMA's Response illustrates that it inappropriately disregarded the detrimental impact of

[3] GEMA's Response on Finance Issues and TNUoS, **Para.74**.

[4] GEMA's Response on Finance Issues and TNUoS, **Para. 157**.

[5] See Oxera (2021), 'National Grid's acquisition of WPD from PPL and the simultaneous sale of NECO to PPL', **PH-4 / Tab 1**.

introducing the outperformance adjustment on sector-wide incentives to perform and invest at this critical time.

2.11 **GEMA's Response on Reserved Powers fails to engage with SSEN Transmission's legal submissions.** GEMA seeks to defend its decision on Reserved Powers on the basis that it is 'convenient' to GEMA and that compliance with the applicable statutory framework would impose a "*disproportionate administrative burden*" on GEMA because it would be required to follow the Statutory Modification Procedure each time it wishes to amend a licence. GEMA's submissions are unconvincing and incoherent. If GEMA were correct, as a matter of law, the Statutory Modification Procedure laid down by primary legislation would become entirely optional, to be used by GEMA only if and when it chooses to follow it as a matter of its own convenience. This is not what is provided for in the EA 1989 and cannot be what Parliament intended. The case law is clear that strained constructions should not be given to wording to grant extensive powers that are not clearly provided for.

2.12 **GEMA's Response on TNUoS demonstrates that it had no convincing reason for its decision.** GEMA wrongly suggests that there is no historical evidence of bias towards under-recovery and that it has put in place sufficient accuracy incentives to prevent the ESO's forecasting performance from deteriorating in the future. GEMA also wrongly suggests that the risk has been captured in SSEN Transmission's price control decision and that the issue is 'immaterial'. As explained in the witness statement of Mr Alkirwi accompanying this submission, all these claims are wholly incorrect and disproven by the clear and indisputable evidence to the contrary. In short, it remains the case that the disconnect between risk and responsibility introduced by GEMA's unevidenced decision, combined with the contemporaneous weakening of the ESO's accuracy incentives, will in all likelihood lead to a perpetual under-recovery of SSEN Transmission's allowed revenue. This would result in the company facing material financing costs that have not been accounted for elsewhere in its price control decision.

2.13 **In conclusion**, none of the arguments that GEMA has advanced in its Response undermines the conclusion that the matters set out in SSEN Transmission's Notice of Appeal amount to material errors by GEMA within the statutory grounds of appeal set out in section 11E(4) of the EA 1989.[6] Accordingly, SSEN Transmission respectfully requests that each of its four grounds of appeal be upheld by the CMA.

Section 3: Appeal Ground 1 – Methodological errors in the cost of equity

3.1 **GEMA's decision on the cost of equity jeopardises the vital investment needed in the price control period to deliver both the UK and Scottish Governments' Net Zero targets.**

3.2 Electricity networks in Great Britain face huge challenges to adapt to the evolving nature of the energy system and meet Net Zero objectives. Electricity consumption is expected to double over the course of the next 30 years due to various factors including the growth in demand for new technologies such as electric vehicles, heat pumps and the electricity needed to undertake the electrolysis to produce hydrogen.[7] At the same time, there will be significant changes in the sources of energy generation due to the proliferation of renewable energy in the system (which, although bringing considerable environmental benefits, is less predictable than fossil fuel generation). The electricity transmission system therefore has a critical role in ensuring that these varying generation sources meet growing demand, and that the transmission system remains robust and reliable as the vital link between the two.

3.3 For the reasons explained in SSEN Transmission's Notice of Appeal, Ofgem's decision to set the cost of equity too low creates a high risk that electricity transmission companies will be unable to attract the investment necessary to meet these challenges and achieve even the minimum pathway to Net Zero.[8] Earlier

[6] GEMA's Response states that "*the test of materiality should be applied to each of the specific errors advanced by an Appellant*" (GEMA's Response on Finance Issues, para. 50). First, the Appellant disagrees with GEMA's attempt to seek to artificially divide up the issues into isolated points in order to seek to undermine the materiality of the issues under appeal. In any event, each of the matters raised by SSEN Transmission is clearly material both individually and collectively to the price control set by GEMA for the reasons SSEN Transmission has already set out in its Notice of Appeal – for example, see paragraphs 2.44-2.46 and 1.54.

[7] Committee on Climate Change, 'The Sixth Carbon Budget: The UK's path to Net Zero' (December 2020), **Reply-1 / Tab 1 / Figures 3.4a and 3.4c**.

[8] SSEN Transmission's Notice of Appeal, **Paras. 1.23 -1.26**; **Alkirwi-1** / **Paras. 5.3 – 5.4**.

this month, the UK Government announced its even more ambitious Net Zero targets, now also enshrined in law, to cut emissions by 78% by 2035 compared to 1990 levels (i.e. to ensure that a certain milestone is met by 2035 on the pathway to the 2050 Net Zero goal).[9]

3.4 These most recent Government announcements reinforce SSEN Transmission's submission in its Notice of Appeal that investment in the RIIO-T2 period is urgently required to meet the Net Zero commitments and that any delay to unlocking key investments in this price control period arising from an insufficient cost of equity will jeopardise the attainment of these important Net Zero targets.

3.5 GEMA has repeatedly suggested that it can 'self-correct' by adjusting its cost of equity decision 'after the fact' if it did set it too low.[10] This is no answer to any of the grounds of appeal. Neither GEMA nor the CMA can avoid engaging with the objectively available evidence relevant to the cost of equity now. Investment decisions in the electricity transmission sector are made over a long time horizon and investors require confidence now on the cost of equity parameter. There is no evidence that investors would have any confidence in any 'self-correcting' decision-making on the cost of equity by GEMA in future. Uncertainty as to the cost of equity would lead to delay and uncertainty over urgently required investment.

3.6 Overall, it is abundantly clear that the decisions taken by GEMA in this RIIO-2 price control in estimating CAPM parameters and in deciding on the appropriate cost of equity have significant bearing for regulated companies and their current and future customers.

3.7 **GEMA overstates the boundaries of its regulatory discretion.**

Decisions made using the CAPM model must be accountable and appealable

3.8 Despite the importance of the matters under appeal, GEMA seeks to avoid scrutiny of its decisions before the CMA by suggesting that CAPM parameters are inherently uncertain and that the points under appeal fall within its regulatory "*discretion*". Indeed, Mr Wilde states in his witness statement that "*if the true WACC can never be known, GEMA's view for Step 1 (CAPM) should be difficult to be found 'wrong*'".[11] This submission is fundamentally incorrect and should not be allowed to obscure the true position. If GEMA were correct, essentially any value attributed to CAPM parameters, or any approach to estimating them, would be equally valid. This is not correct. GEMA made choices regarding the evidence on which it decided to rely and the methodology it decided to follow. SSEN Transmission has set out evidence in its Notice of Appeal demonstrating that, in several respects, GEMA made the wrong choices. These are all matters that can – indeed must – be corrected by the CMA.

3.9 GEMA goes so far as to imply that the CAPM model itself is not fit for purpose. First, SSEN Transmission notes that GEMA has, in fact, relied on the CAPM model which forms the basis of 'Step 1' of its methodology. The CAPM model is and has for many years been relied on by UK economic regulators (including, most recently, the CMA itself in the PR19 water redetermination). Contrary to the position GEMA seeks to imply, estimating CAPM parameters is not "*an exercise in the unknown*"[12] – indeed the whole purpose of the model is to deal with the uncertainties of a price control in the most robust way possible. Mr Wilde himself acknowledges that CAPM "*is still widely viewed as the most reliable way to estimate Cost of Equity*".[13] The CMA should not be distracted by this attempt to obfuscate the key issues in the appeal. The fundamental question is whether the inputs to the CAPM model have been estimated by GEMA in a way that is robust, evidence-based and accountable, in view of their respective intended purposes.

3.10 The underlying premise behind the position advocated by GEMA is that GEMA (and all other regulators subject to an appeal system akin to that in energy) can in future use incorrect CAPM estimates safe in the knowledge that their decisions will be regarded as an exercise in unappealable "*regulatory discretion*". But

[9] UK Government Press Release, 'UK enshrines new target in law to slash emissions by 78% by 2035' (20 April 2021) (https://www.gov.uk/government/news/uk-enshrines-new-target-in-law-to-slash-emissions-by-78-by-2035), **Reply-1 / Tab 2**.

[10] GEMA's Response on Finance Issues and TNUoS, **Para. 257.5**.

[11] **Wilde 1** / **Para. 29.1**.

[12] GEMA's Response on Finance Issues and TNUoS, **Para. 59**.

[13] **Wilde 1** / **Para. 43**.

GEMA's decisions on the evidence and methodology employed to set the cost of equity are no more an exercise in discretion than any other decisions taken as part of the price control. These decisions are equally subject to appeal to the CMA on the same basis as any element of the price control. Contrary to GEMA's suggestion, the CMA should therefore not be "*slow to interfere*"[14] in decisions relating to the cost of equity. There is no special statutory test or process applicable to such decisions. Where the CMA is satisfied that the decision appealed against was wrong on one or more of the grounds of appeal set out in section 11E(4) of EA 1989, the decision must be set aside and remedied.[15]

GEMA uses precedents selectively and disregards the most reliable evidence available

3.11 In the Response, GEMA seeks to make much of the different procedure applicable to energy appeals and redeterminations in other sectors. In particular, GEMA seeks, on the basis of this difference in procedure, to minimise the importance that the CMA places on the PR19 Final Determination regarding the cost of equity. This misses the point. SSEN Transmission's Notice of Appeal sets out why the errors made by GEMA satisfy the statutory test in section 11E(4) of the EA 1989. The statutory test is met because GEMA chose to dismiss key evidence and made other methodological choices without any proper basis, leading to a decision on the cost of equity that is contrary to its statutory duties. PR19 is relevant because the Appellant relies on the same evidence and/or methodological choices that have been explicitly recognised as correct by the CMA in that redetermination.[16] In other words, the CMA's recent determination in PR19 endorses the correctness of the position set out in the Notice of Appeal and is a strongly persuasive recent decision validating the Appellant's submission that GEMA's decision was wrong. GEMA chose to ignore the relevant and cogent evidence put forward by the Appellant, which included public statements by the CMA available at the time of the RIIO-T2 Final Determination. Instead, GEMA seeks to place undue reliance on the NATS decision which was taken in very unusual and specific circumstances (e.g. for RFR and TMR[17]). The CMA has itself recognised that the NATS appeal "*should not be considered as the definitive view of the CMA at the time*".[18]

3.12 It is worth noting for completeness that GEMA's approach to the CMA's PR19 Final Determination is inconsistent. GEMA seeks to rely on PR19 in its Response where it suits its arguments (e.g. cost of debt and totex),[19] but then downplay the relevance of that decision on the cost of equity grounds where the CMA's position is more aligned with that of the Appellant.

3.13 This inconsistent and cherry-picking approach to evidence is pervasive throughout the Response. For instance, GEMA uses selective evidence from US markets to support its position: US data is used for its TMR cross-check, but then rejected in the context of proving the convenience yield for RFR.[20] Further, when discussing the choice of a point estimate, GEMA cites a New Zealand Commerce Commission decision for the telecoms sector rather than the more relevant decision of the same regulator for the energy sector which supports the principle of 'aiming up' in energy.

GEMA's Response seeks to obscure the key issues before the CMA

3.14 Another theme prevalent throughout the Response is GEMA's attempt to confuse the Appellants' points by artificially over-complicating the issues before the CMA in an attempt to create divisions between the arguments made by the Appellants. GEMA seeks to use this rhetoric to persuade the CMA that the points at issue are matters of disagreement rather than errors.[21] This strategy is both transparent and unconvincing.

[14] GEMA's Response on Finance Issues and TNUoS, **Paras. 110 and 141**.

[15] The CMA has highlighted the standard of review on an appeal to the CMA goes beyond the conventional grounds of judicial review and that the merits of GEMA's decision must be taken into account by reference to the specific grounds of appeal laid down in the statute: *CMA, British Gas Trading Limited v the Gas and Electricity Markets Authority, Final Determination* - see **NOA-1 / Tab 57**.

[16] See SSEN Transmission, PR19 Submission (23 April 2021).

[17] CMA (2021), PR19 'Final Report' – Final Report, **SSEN Transmission PR19 Submission, Annex 2. / Para. 9.60**.

[18] CMA (2021), PR19 'Final Report' – Final Report, **SSEN Transmission PR19 Submission, Annex 2. / FN. 2252**.

[19] GEMA's Response on Finance Issues and TNUoS, **Paras. 431 – 440**.

[20] GEMA's Response on Finance Issues and TNUoS, **Paras. 134 – 136** and **Friend 2**, **Para. 55**.

[21] GEMA's Response on Finance Issues and TNUoS, **Paras. 116 – 117**.

(a) First, the overarching methodological errors identified by each of the Appellants are consistent and GEMA's Response focuses on subtleties in the explanation of these points in the various notices of appeal rather than addressing the substance of the errors.

(b) Second, none of the subtle differences between Appellants' positions that GEMA points to support GEMA's decision on the cost of equity. In reality, each of the Appellants has pointed to the same key errors made by GEMA in its cost of equity decision which, in the view of all the Appellants and their experts, was set too low.

3.15 The Appellant has explained further below in relation to each ground of appeal why nothing that GEMA has raised in its Response could change the conclusion that GEMA's decisions on cost of equity are wrong under section 11E(4) EA 1989. These Reply submissions are supported by a table of further detailed rebuttals of the points made in GEMA's Response on the cost of equity in the Oxera WACC Report exhibited to Mr Hope's third witness statement (PH-3 / Tab 1).

GROUND 1A: ERRORS IN RFR

3.16 **GEMA's decision on RFR is wrong in accordance with the statutory grounds outlined in section 11E(4) EA 1989.**

3.17 GEMA set the RFR at -1.58% (60% gearing, CPIH-real). GEMA erred by relying entirely on evidence based on the spot yield of ILGs as a proxy for the RFR. For the reasons explained in the Notice of Appeal at paragraph 4.16, GEMA's decision was wrong under section 11E(4) EA 1989 and its attempts in the Response to shield this decision from scrutiny under the guise of regulatory discretion do not withstand scrutiny for the following reasons:

(a) First, GEMA's Response baldly asserts that "*ILGs are what they are and provide a reasonable proxy for the unobservable RFR*".[22] However, this response fails to take into account the widely acknowledged convenience premium embedded in government bonds. The existence of the convenience premium can be seen in practice through (i) the gap between corporate and sovereign risk-free rates;[23] (ii) risk-free rate assumptions used by equity analysts covering UK regulated utilities;[24] and (iii) the fact that it is widely recognised in the academic literature.[25] GEMA's Response does not provide any convincing reason why it was appropriate for GEMA to ignore the effects of the convenience premium.

(b) Second, GEMA's Response fails to acknowledge that the convenience features of government bonds mean that they do not conform to the definition of the risk-free rate in the CAPM. For the CAPM, the risk-free rate serves to represent the expected return on a 'zero beta' asset. The convenience premium gives ILGs *negative* beta properties and using ILG data alone (as GEMA did) biases the CAPM equation downwards. GEMA's attempt to dismiss the implications of the convenience premium on the basis that the evidence provided "*related largely to US Treasuries and it was not clear whether this analysis would hold for UK gilts*" is incorrect.[26] GEMA's Response does not engage with Oxera's evidence in its Cost of Equity Report that the correlation between government bond returns and equity returns is **consistently and significantly negative** using daily return data in the UK, a finding that is similar to the Federal Reserve's finding for US Treasuries.[27] Unadjusted ILGs therefore cannot be considered a "*reasonable proxy*" for the zero beta RFR for use in the CAPM and GEMA's Response does not contain any evidence to the contrary.

(c) Third, GEMA seeks to defend its dismissal of evidence on AAA-rated corporate bonds as "*an entirely reasonable exercise of its regulatory discretion*".[28] However, GEMA's Response makes clear that it

[22] GEMA's Response on Finance Issues and TNUoS, **Para.74**.

[23] SSEN Transmission's Notice of Appeal, **Paras 4.13- 4.15**.

[24] Oxera, Cost of Equity Report, **PH-1 / Tab 1**.

[25] Krishnamurthy, A. and Vissing-Jorgensen, A. (2012), 'The Aggregate Demand for Treasury Debt', Journal of Political Economy, 120:2, April, **PH-1 / Tab 7**.

[26] **Friend 2 /Para. 55**. Also see GEMA's Response on Finance Issues and TNUoS, **Para.74**.

[27] Oxera, Cost of Equity Report, **PH-1 / Tab 1 / Section 5B.2**.

[28] GEMA's Response on Finance Issues and TNUoS, **Para. 86**.

had no proper basis to dismiss this evidence. GEMA's purported reason for doing so was that AAA-rated corporate bond yields may require adjustments.[29] This too is an error and is not a proper basis to dismiss evidence on AAA bonds while relying exclusively on ILGs. ILGs themselves require adjustment in order to account for the convenience premium.

(d) Fourth, GEMA suggests there is regulatory precedent for its approach to RFR.[30] Oxera is not aware of the regulatory precedent GEMA has in mind for using spot yields directly in the CAPM for setting a price control. In any event, the problems with using ILGs came to prominence following the recommendation in the UKRN report that economic regulators adopt spot yields.[31] The wider adverse implications of this approach were revealed in the CMA provisional findings for NATS, where the resulting underestimation of the RFR was a key driver of the apparent upward-sloping relationship between gearing and WACC.[32]

(e) Fifth, GEMA seeks to distance itself from the CMA's recent PR19 decision on RFR on the basis that its decision is open to it "*as a regulator taking a different decision for a different sector, under a different statutory scheme*".[33] However, RFR is not a sector-specific decision. None of the CMA's conclusions on RFR were specific to the water sector and there is no principled basis to adopt a different decision on RFR in the water and energy sectors. GEMA's Response does not set out any evidential basis for departing from the approach of the CMA in PR19, which endorses SSEN Transmission's approach in its Notice of Appeal.

(f) Finally, GEMA states that *"[t]he Appellants' objections are to the way in which GEMA has exercised its discretion in respect of the evidence on how best to estimate the RFR, rather than challenging any conclusion of fact or factual inference"* (emphasis added).[34] This is plainly incorrect. The Appellant *has* squarely challenged the evidence which GEMA relies on to support its exclusive use of unadjusted ILGs. GEMA's factual conclusion that the yield on unadjusted ILGs is a reasonable proxy for the RFR and its rejection of the factual evidence that such yield contains a convenience premium is clearly challenged in SSEN Transmission's Notice of Appeal and Oxera's Cost of Equity Report. The evidence shows that these factual conclusions were incorrect and resulted in GEMA's decision being wrong. In addition to amounting to an error of fact, the Appellant considers that GEMA's decision on RFR is wrong because it constitutes an error of law (in particular, the public law duty to reach reasonable decisions), GEMA failed to achieve its stated effect to appropriately compensate investors, and GEMA failed properly to have regard to and/or to give the appropriate weight to its statutory duties.

GROUND 1B: ERRORS IN TMR

3.18 **GEMA's decision on TMR is wrong in accordance with the statutory grounds outlined in section 11E(4) EA 1989.**

3.19 GEMA set the TMR range too low at 6.25%-6.75% (CPIH-real), with a midpoint of 6.5%.[35] This decision was wrong because it relied on a synthetically created and unreliable 'back cast' of the CPI as a measure of inflation and incorrectly relied on an incorrect geometric averaging methodology. For the reasons explained in SSEN Transmission's Notice of Appeal at paragraph 4.47, GEMA's decision on TMR was wrong under section 11E(4) EA 1989 and its attempts in the Response to classify this decision as an unreviewable matter of regulatory discretion do not withstand scrutiny for the following reasons:

(a) First, GEMA's Response states that the Appellants raise "*narrow, esoteric points, all of which concern matters of regulatory judgement, in a context where it is common ground that TMR is, as a measure of investors' ex ante expectations of equity returns, unobservable*".[36] It is common ground that TMR is

[29] GEMA's Response on Finance Issues and TNUoS, **Para. 86**.

[30] GEMA's Response on Finance Issues and TNUoS, **Paras. 79 and 82**.

[31] UKRN (2018), 'Estimating the cost of capital for implementation of price controls by UK Regulators', **PH-1 / Tab 38 / Page 8**.

[32] Oxera (2020), 'Are sovereign yields the risk-free rate for the CAPM?', 20 May, **PH-1 / Tab 4 / Page 4**.

[33]. GEMA's Response on Finance Issues and TNUoS, **Paras. 90 – 92**.

[34] GEMA's Response on Finance Issues and TNUoS, **Para. 69**.

[35] RIIO-2 - Final Determination, Finance Annex, **NOA-1 / Tab 12 / Para 3.86**.

[36] GEMA's Response on Finance Issues and TNUoS, **Para. 110**.

not an observable measure of investors' expectations, just as the cost of equity element of the CAPM is not observable. However, the manner in which GEMA chose to estimate the TMR and the evidence it chose to take into account (or not) are not matters of discretion. GEMA's decisions in this respect are equally capable of being wrong as any other aspect of the price control. Indeed, the fact that a variable is unobservable points to the need for particular care and robustness to the methodology employed by GEMA and the evidence on which its decision was based.

(b) Second, GEMA suggests that the Appellant's objections to its decision to rely solely on CPI data "*amount to disagreements with GEMA's exercise of its regulatory judgement and disclose no appealable error*",[37] particularly since "*there is no perfect data series but GEMA's judgement is that the CED/CPI series is more reliable than the CED/RPI series*".[38] However, the choice of dataset is not purely a matter of regulatory discretion – GEMA must consider the available evidence and choose a dataset that is reliable and fit for purpose. Yet GEMA's Response has continued to provide no convincing basis for its decisions to rely on CPI data which suffers from acknowledged data reliability issues. Nor does GEMA's Response set out any convincing basis for its rejection of the RPI data, which is a better reflection of historical investor expectations. Furthermore, contrary to GEMA's assertions,[39] the Appellant does not ignore the criticisms of the RPI – Oxera has pointed to an adjusted RPI data set which would take account of those criticisms and provide a more reliable and robust data set with which to model historical inflation than the data set used by GEMA.[40]

(c) Third, GEMA is no doubt conscious that the CMA's recent decision in PR19 is aligned with the Appellant's position as the CMA took account of the RPI dataset rather than GEMA's approach of relying solely on CPI. GEMA therefore attempts to downplay the differences between the CMA's PR19 decision and its RIIO-2 decision by describing the CMA's TMR range as only "*slightly"* higher.[41] However, the difference cannot be considered "*slight*" given the materiality of the underlying error, both for the current Appellants and for other future regulatory decisions on cost of capital.

(d) Fourth, in relation to the averaging error, GEMA again seeks to dismiss the grounds of appeal by describing them as "*either wrong, or simply amount[ing] to disagreements with GEMA's exercise of its regulatory discretion*".[42] GEMA's Response does not set out any convincing reason to support its incorrect reliance on the geometric average with a subjective uplift rather than the directly observed arithmetic average – this approach erroneously produced a downwardly biased TMR estimate.[43] The CMA's PR19 Final Determination also supports the Appellant's position on this error. The CMA noted that the modelling of uplifts to the geometric average is controversial and decided that it could not put any weight on such analysis.[44] Instead, the CMA took into account the arithmetic averages of returns over holding periods ranging from one to twenty years.[45] The Appellant notes that the CMA includes average returns based on overlapping and non-overlapping holding periods of up to twenty years, presumably to address concerns about serial correlation and predictability in annual returns. Oxera has considered the evidence on serial correlation and the impact on average returns and concluded that "*there is no strong evidence of serial correlation or predictability in returns. Our recommendation is to use direct arithmetic averages of annual returns*."[46]

GROUND 1C: ERRORS IN BETA

3.20 **GEMA's decision on beta is wrong in accordance with the statutory grounds outlined in section 11E(4) EA 1989.**

[37] GEMA's Response on Finance Issues and TNUoS, **Para. 117**.
[38] GEMA's Response on Finance Issues and TNUoS, **Para. 118**.
[39] GEMA's Response on Finance Issues and TNUoS, **Para. 118**.
[40] Oxera (2019), 'Estimating RPI-adjusted equity market returns', 2 August, **PH-1 / Tab 34.**
[41] GEMA's Response on Finance Issues and TNUoS, **Paras. 121-123**.
[42] GEMA's Response on Finance Issues and TNUoS, **Paras. 127 and 130**.
[43] SSEN Transmission's Notice of Appeal, **Paras. 4.40-4.47**.
[44] CMA (2021), PR19 'Final Report' – Final Report, 17 March 2021, **SSEN Transmission PR19 Submission, Annex 2 / Para. 9.338**.
[45] CMA (2021), PR19 'Final Report' – Final Report, 17 March 2021, **SSEN Transmission PR19 Submission, Annex 2 / Para. 9.334**.
[46] Oxera, Cost of Equity Report, **PH-1 / Tab 1 / Para. 6.30**.

3.21 GEMA set the asset beta for energy networks at 0.349.[47] In reaching this decision, GEMA made a number of errors including wrongly considering water companies as comparators for electricity transmission operators, use of flawed European comparators, incorrect estimation windows and errors in estimating debt beta.[48] However, GEMA again considers that "*[t]he alleged 'errors' identified by the Appellants are in reality disputes about the exercise of GEMA's regulatory judgement*".[49] For the reasons explained in the Notice of Appeal at paragraph 4.71, GEMA's decision was wrong under section 11E(4) EA 1989 and its attempts in the Response to classify this decision as a matter of regulatory discretion do not withstand scrutiny for the following reasons:

(a) First, the asset beta estimates presented by GEMA show that National Grid's asset beta is consistently higher than the average asset beta of UK water companies across all estimation windows, including the ten-year window preferred by GEMA.[50] This is confirmed by Oxera's Cost of Equity Report.[51] This **objective market data** provides clear evidence – which remains unchallenged – as to why the asset beta for energy networks would be materially higher than for water companies. Even Ofwat did not consider energy networks to be relevant for determining the asset beta of water companies in PR19. GEMA's assertion in the Response that it has not placed equal weight on the betas of National Grid and the water companies[52] fails to acknowledge the key point which is that GEMA was incorrect to place any weight on the betas of water companies. GEMA's Response also makes it extremely difficult to interrogate *how* the water betas were taken into account by stating that it was a **subjective** "***judgement … in the round***", rather than a mathematical weighting.[53] The evidence shows that water companies have fundamentally different asset risk profiles and consistently show lower asset betas in empirical evidence and are therefore not an appropriate proxy to use for estimating energy company betas.[54]

(b) Second, GEMA used an incorrect sample of European networks as comparators in estimating the asset beta. GEMA itself acknowledges that the results of the European comparators "*depend on the sample companies chosen*".[55] Oxera's sample starts with a broad group of European comparator firms and 'screens out' illiquid firms to avoid specific statistical problems in calculating beta. In contrast, GEMA selectively 'screens in' firms, including illiquid comparators. GEMA has concerns with illiquidity elsewhere in its Response (e.g. concerning the use of AAA-rated corporate bonds to inform the estimate of RFR)[56] but is inconsistent when it comes to selecting the sample of comparators for beta. GEMA's estimate based on this incorrect sample was below the bottom end of a plausible range supported by observable and robust empirical data.

(c) Third, GEMA incorrectly relied on long-term estimation windows of 10+ years as opposed to two years and five years, and failed to recognise a significant break in the time series for UK utilities in September / October 2008.[57] Specifically, GEMA fails to take into consideration the fact that the risk profile of National Grid has changed over time, as evidenced by five-year betas of 0.29 as at 31 December 2014 and 0.37 as at 31 December 2019.[58] By relying on long-term estimation windows of 10+ years, GEMA therefore inappropriately placed weight on periods of time that do not accurately reflect the current risk profile of National Grid.

(d) Fourth, in its Response, GEMA does not even address the errors it has made in: (i) incorrectly comparing the French energy sector with its fundamentally different regulatory and economic

[47] RIIO-2 - Final Determination, Finance Annex, **NOA-1 / Tab 12 / Table 9**.
[48] SSEN Transmission's Notice of Appeal, **Ground 1C**.
[49] GEMA's Response on Finance Issues and TNUoS, **Para. 176**.
[50] Oxera, Cost of Equity Report, **PH-1 / Tab 1 / Para. 7.13**.
[51] Oxera, Cost of Equity Report, **PH-1 / Tab 1 / Para. 7.14-7.15**.
[52] GEMA's Response on Finance Issues and TNUoS, **Para. 157**.
[53] GEMA's Response on Finance Issues and TNUoS, **Para. 157**.
[54] SSEN Transmission's Notice of Appeal, **Paras. 4.55-4.58**.
[55] GEMA's Response on Finance Issues and TNUoS, **Para. 160**.
[56] GEMA's Response on Finance Issues and TNUoS, **Para. 86**; **Friend 2**, **Para. 60**.
[57] SSEN Transmission's Notice of Appeal, **Para. 4.53 (d)**.
[58] Oxera Cost of Equity Report, Asset beta, **PH-1 / Tab 1 / Section 7C**.

conditions to the UK energy sector;[59] and (ii) estimating debt beta, including relying on biased data and incorrectly interpreting the academic literature.[60] GEMA has offered no further evidence to support these aspects of its decisions which further contributed to GEMA underassessing the appropriate level of beta for energy networks.

GROUND 1D: ERRORS IN AIMING UP

3.22 **GEMA's decision on aiming up is wrong in accordance with the statutory grounds outlined in section 11E(4) EA 1989.**

3.23 The cost of equity parameters require the choice of a point estimate. GEMA's Response errs by claiming that the choice of a point estimate is purely a matter of regulatory discretion on the basis that there is no rule requiring 'aiming up'.[61] This conclusion ignores the economic and statistical evidence that the consumer benefits of selecting a point estimate in the upper end of the calculated range increase as the uncertainty of the range itself increases, and the particular need for aiming up in the electricity transmission sector in the RIIO-2 price control. For the reasons explained in SSEN Transmission's Notice of Appeal at paragraph 4.100, GEMA's decision was wrong under section 11E(4) EA 1989 and its attempts in the Response to classify this decision as a matter of regulatory discretion do not withstand scrutiny for the following reasons:

(a) First, GEMA continues to discount the risk of SSEN Transmission not being able to attract sufficient investment, particularly in light of Net Zero objectives and the quantum of uncertain investments over the course of the price control. A cost of equity that is too low will therefore ultimately harm consumers, contrary to GEMA's principal objective and statutory duties.[62] GEMA's Response demonstrates that its decision is out of touch with the way investors make decisions by suggesting that - despite an insufficient cost of equity allowance - ODIs, quality of service obligations and UMs will be enough to attract investment.[63]

(b) Second, GEMA has not addressed the concern that aiming up in RIIO-2 is even more important to promote investment and appropriately balance the level of bills against risk to customers given GEMA's decision results in a reduction of 357 bps in the cost of equity compared to RIIO-T1,[64] which is even greater than the 247 bp reduction in PR19 compared to PR14.[65] It is also worth noting that most of the RIIO-2 reduction is due to changes in methodology introduced by GEMA that are disputed and all act in the same direction of reducing the cost of equity estimate. The accuracy of the resulting range is highly uncertain as a result of these changes introduced by GEMA.

(c) Third, GEMA belittles the importance of whether or not it aimed up by describing this debate as "*an arid linguistic quibble*".[66] This is an incorrect characterisation of this ground of appeal. It is clear from GEMA's CAPM steps that it 'aimed straight' down the middle of its already incorrect low range and has ignored well-accepted UK and international regulatory practice in so doing.

(d) Fourth, GEMA continues to compare its proposed WACC to other international regulatory WACCs, in order to claim that it has 'aimed-up' relative to other countries.[67] This argument has already been dismissed by the CMA in its PR19 decision where it observed that "*[a] number of the comparator levels of return provided were not like-for-like, and in any case the regulatory frameworks are very different*" and also "*that some higher comparators were not included in the data*".[68]

[59] SSEN Transmission's Notice of Appeal, **Paras. 4.53(c) and 4.63**.

[60] Oxera's evidence supports a debt beta of no more than 0.05; SSEN Transmission's Notice of Appeal, **Para. 4.66**.

[61] GEMA's Response on Finance Issues and TNUoS, **Paras. 260, 264, 266-267, 275**.

[62] s. 3A(1) EA 1989 states that GEMA's principal objective is to "*protect the interests of existing and future consumers in relation to electricity conveyed by distribution systems or transmission systems*".

[63] GEMA's Response on Finance Issues and TNUoS, **Paras. 257.6 and 257.7**.

[64] Cost of equity reduced by 3.57% (from 7.82% to 4.25% real) - Oxera Cost of Equity Report, **PH-1 / Tab 1 / Figure 1.1**, **Page. 8**.

[65] Cost of equity reduced by 2.47% (from 5.65% to 3.18% real) – CMA (2021), PR19 'Final Report' – Final Report (17 March 2021) SSEN Transmission PR19 Submission, **Annex 2 / Page 1103**.

[66] GEMA's Response on Finance Issues and TNUoS, **Para 259**.

[67] GEMA's Response on Finance Issues and TNUoS, **Para. 273.3 and Figure 1**.

[68] CMA (2021), PR19 'Final Report' – Final Report, 17 March 2021, **SSEN Transmission PR19 Submission, Annex 2 / Para 9.1267**.

3.24 Mr Wilde highlights that the CMA's NATS decision states that the selection of a point estimate involves a degree of judgment.[69] Furthermore, he seeks to rely on the fact that the mid-point was chosen in NATS and therefore suggests it is open to GEMA to do the same for RIIO-2. This does not answer the arguments made in SSEN Transmission's Notice of Appeal as to why GEMA was wrong not to aim up in the context of electricity transmission in RIIO-T2. Furthermore, not only did the NATS decision not reach a definitive view at the time in light of the specific circumstances of that case (see above), but the CMA specifically stated in its decision that it did not take a view as to whether this position for air traffic control would be justified in other sectors.[70]

3.25 The Appellant draws the CMA's attention to far more relevant precedents such as the price control decision for energy of the New Zealand Commerce Commission (***NZCC***) which follows a policy of setting its point estimate based on the 67th percentile of the WACC range.[71] Mr Wilde continues to try and downplay the relevance of this precedent by making reference to the NZCC's fibre decision,[72] entirely ignoring the fact that the CMA has already dismissed this decision as a basis for not aiming up in the electricity sector in its PR19 decision: "*Our view is that this does not fully reflect all the relevant analysis in the NZCC decision, which explicitly recognises the differences between the effects of failure on the electricity network and the fibre network*".[73]

3.26 Therefore, for the reasons explained in SSEN Transmission's Notice of Appeal[74] and above, and in line with regulatory best practice, there is overwhelming compelling evidence as to why aiming up is critical in the electricity transmission sector for the RIIO-T2 period to attract the level of equity investment needed so as to enable it to undertake and plan for the considerable investments required in the course of RIIO-T2 and in subsequent price control periods. GEMA's Response does not set out any convincing basis capable of supporting its decision to fail to aim up.

GROUND 1E: ERRORS IN CROSS-CHECKS

3.27 **GEMA's decision on cross-checks is wrong in accordance with the statutory grounds outlined in section 11E(4) EA 1989.**

3.28 The Appellant is concerned by comments in GEMA's Response that seek to disproportionately elevate the importance of the cross-checks on the basis that the CAPM model involves a process of estimation. For example, Mr Wilde states that "*if the true WACC can never be known, GEMA's work in Step 2 (cross-checks) is justified in principle, in an effort to reduce the uncertainty and the cost it could create for consumers*".[75] First, the CAPM model should be the primary basis upon which to base the decision on WACC. Second, where cross-checks are undertaken, they cannot be accorded weight that they cannot bear and if reliance is placed on such cross-checks it is important that they are free from significant levels of inaccuracy. However, GEMA has misapplied and misrepresented the cross-checks on which it relied as part of the RIIO-2 price control. For the reasons explained in SSEN Transmission's Notice of Appeal at paragraph 4.126, GEMA's decision was wrong under section 11E(4) EA 1989 and its attempts in the Response to classify this decision as a matter of regulatory discretion do not withstand scrutiny for the following reasons:

(a) GEMA's Response either fails to engage at all with a number of the errors identified or fails to address the criticisms adequately– see the Oxera WACC Report exhibited to Mr Hope's third witness statement (PH-3 / Tab 1) for detailed rebuttals on each cross-check.

[69] **Wilde 1 / Para 77**; CMA (2020), NATS (En Route) Plc / CAA Regulatory Appeal 'Provisional Findings Report' – Provisional Findings Report, 24 March 2020, **SW1 / Tab 19 / Para. 12.262**.

[70] **Wilde 1 / Para 7**9; CMA (2020), NATS (En Route) Plc / CAA Regulatory Appeal 'Final Report' – Final Report (23 July 2020), **NOA-1 / Tab 59 / Para. 13.297**; CMA (2020), NATS (En Route) Plc / CAA Regulatory Appeal 'Provisional Findings Report' – Provisional Findings Report (24 March 2020), **SW1 / Tab 19 / Para. 12.290**.

[71] CMA (2021), PR19 'Final Report' – Final Report, 17 March 2021, SSEN Transmission PR19 Submission, **Annex 2**, **Para. 9.1231**.

[72] **Wilde 1 / Para 104**.

[73] CMA (2021), PR19 'Final Report' – Final Report, 17 March 2021, SSEN Transmission PR19 Submission, **Annex 2 Para 9.1235**.

[74] SSEN Transmission's Notice of Appeal, **Ground 1D**.

[75] **Wilde 1 / Para 29.2**.

(b) Of particular note, SSEN Transmission has already highlighted that MAR data is unreliable because it is driven by a wide range of factors and is also subject to a significant degree of interpretation error.[76] This was reiterated by the CMA in its PR19 Final Determination on this topic which states that "*[o]n balance, we remain cautious about using market prices to determine the point estimate for the cost of equity or overall cost of capital*".[77] With that in mind, GEMA's stylised MAR analysis, and their attempt throughout the Response to inflate the relevance of the acquisition of Western Power Distribution (***WPD***) by National Grid plc (***NG***), is incomplete and incorrect.[78] In particular, GEMA uses the premium paid by NG in its takeover of WPD to argue that the sector-wide cost of equity is too low and that the market expects sector-wide outperformance. The Appellant has provided an overview in the Oxera WPD Report exhibited to Mr Hope's fourth witness statement Hope-4 (PH-4 / Tab 1) explaining why GEMA is seeking to draw unsubstantiated and strained conclusions from this transaction which do not stand up to scrutiny. In summary:

(i) First, it is incorrect to draw inferences about sector-wide outperformance and cost of equity based on a single transaction for a top-performing company such as WPD. The premium paid by NG can be explained by reasonable expectations of WPD-specific outperformance, expected synergies realised by the merged NG/WPD firm, the premium that WPD's parent paid to NG for NECO, and a terminal value RAV exit multiple.[79]

(ii) Second, modelling the value of WPD based on a long-term discounted cash flow analysis shows that the valuation can be explained using a 6.20% cost of equity (CPIH, real) (at 60% gearing), in line with the midpoint of Oxera's range for SSEN Transmission in RIIO-2. This shows how valuation analysis depends on the assumptions assumed by the investor and undermines GEMA's argument that it can draw reliable conclusions about the cost of equity based on market valuations of utility companies.[80]

(iii) Third, GEMA's stylised models ignore important market information, such as the NECO premium. Using Oxera's assumptions on WPD-specific outperformance and RAV growth, GEMA's models do not support its conclusion that the WPD premium indicates "*a revealed cost of equity materially below the 4.55% assessment in RIIO-2 Final Determination*"'.[81][82]

3.29 Finally, GEMA's Response is also inconsistent as regards its cross-checks. GEMA simultaneously seeks to attach importance to the cross-checks as a means of reducing the cost of equity range, while at the same time suggesting in its Response that the cross-checks are not material.[83] This is unconvincing. As a result of the cross-checks, GEMA reduced the midpoint of the CoE range produced by its CAPM analysis at Step 1 from 4.55% to 4.40% (and then uses the uplift to 4.55% at Step 3 to misleadingly imply that it 'aimed up').[84] Moreover, GEMA emphasises in its Response that its cross-checks (especially MARs) make it "*very confident"* in its cost of equity estimates.[85] Since GEMA's Response confirms that it has clearly placed reliance on its cross-checks to support its inadequate cost of equity estimates it cannot resist scrutiny of its decision on the basis that the cross-checks are not material or significant.

[76] SSEN Transmission's Notice of Appeal, **Para. 4.116**.

[77] CMA, PR19 Final Determination, SSEN Transmission PR19 Submission, **Annex 2**, **Para. 9.1358**.

[78] GEMA's Response on Finance Issues and TNUoS, **Para. 317**.

[79] Oxera (2021), 'National Grid's acquisition of WPD from PPL and the simultaneous sale of NECO to PPL: Is the WPD premium a robust and reliable evidence for cross-checking allowed equity returns for RIIO-2?' (5 May 2021) **PH-4 / Tab 1 / Section 3**.

[80] Oxera (2021), 'National Grid's acquisition of WPD from PPL and the simultaneous sale of NECO to PPL: Is the WPD premium a robust and reliable evidence for cross-checking allowed equity returns for RIIO-2?' (5 May 2021) **PH-4 / Tab 1 / Section 3**.

[81] **Wilde 1 / Para. 62**.

[82] Oxera (2021), 'National Grid's acquisition of WPD from PPL and the simultaneous sale of NECO to PPL: Is the WPD premium a robust and reliable evidence for cross-checking allowed equity returns for RIIO-2?' **PH-4 / Tab 1 / Section 3**.

[83] GEMA's Response on Finance Issues and TNUoS, **Paras. 244 – 250**.

[84] RIIO-2 - Final Determination, Finance Annex, **NOA-1 / Tab 12 / Table 12**.

[85] GEMA's Response on Finance Issues and TNUoS**, Para. 267.1**.

Section 4: Appeal Ground 2 – Expected outperformance adjustment

4.1 GEMA raises no new or compelling points in its defence of the novel and controversial outperformance adjustment. The Oxera WACC Report exhibited to Mr Hope's third witness statement[86] sets out the Appellant's detailed rebuttals to GEMA's Response. SSEN Transmission highlights three overall points below:

(a) GEMA does not adequately address the fact that the outperformance adjustment is contrary to the principle of incentive-based regulation;

(b) GEMA's claims relating to information asymmetry remain unevidenced and incorrect. GEMA relies on its unevidenced view of the size and direction of the alleged information asymmetry as the basis for its decision on the outperformance adjustment; and

(c) GEMA incorrectly downplays the negative impact of the expected outperformance adjustment on companies' incentives to invest and become more efficient.

4.2 **GEMA's Response fails to address the criticism that the outperformance adjustment is contrary to the principle of incentive-based regulation.**

4.3 GEMA's Response has failed to address the serious concern that the expected outperformance adjustment mechanism is against the fundamental principles of incentive-based regulation that underpin the RIIO price control regime. Instead, GEMA again relies on its alleged regulatory discretion to implement this mechanism.[87]

4.4 It bears repeating and emphasising that it is an error to introduce an unprecedented adjustment for expected outperformance that will harm incentives, especially given that GEMA already has an array of more empirically sound and tested incentive-based regulatory tools to set appropriately calibrated cost allowances and associated incentives for the RIIO-2 price control.[88]

4.5 GEMA's Response continues to present outperformance as an inherently negative outcome in a price control. However, Earwaker and Fincham's study of experienced regulatory practitioners revealed that a number of respondents "*pointed out that outperformance will often be a consequence of companies responding positively to incentives that consciously share gains between shareholders and customers, which is exactly what a regulator would hope for (providing incentives were well-designed)*".[89] Yet, the witness statements by Mr Kaul and Mr Wilde erroneously imply that incentive-based regulation should lead to an expected outperformance of zero:

(a) Mr Kaul's witness statement states that "*[i]t has always implicitly been assumed in the past that expected outperformance or underperformance is zero, and therefore no distinction between expected and allowed returns is necessary*."[90]

(b) Similarly, Mr Wilde's witness statement implies that regulators need to set a 'fair bet' price control: "*[i]n my view, the most compelling illustration that regulators have been unable to set up a 'fair bet' is shown at Figure 16 of Draft Determinations – a histogram of historical cost outperformance based on over 900 observations for the period 2000 to 2020. I believe this phenomenon is primarily driven by information asymmetry, which cannot, in my view, be ignored when attempting to set a 'fair bet' price control.*"[91]

4.6 With incentive-based regulation, it is not obvious that expected outperformance should not be positive. Under a well-functioning incentive-based regulation regime, companies would deliver expected

[86] Oxera WACC Report, **PH-3 / Tab 1**.

[87] GEMA's Response on Finance Issues and TNUoS, **Paras. 286.1, 298, 304, 308, 324, 336**.

[88] Oxera, Expected Outperformance Adjustment Report**, PH-2 / Tab 1 / Section 3A**.

[89] Earwaker and Fincham (2020), 'Information asymmetry and the calibration of price controls', August, **NOA-1** / **Tab 80** / **Page 21**.

[90] **Kaul / Para. 32**.

[91] **Wilde 1 / Para. 201**.

outperformance. The whole distinction made by GEMA between allowed returns and expected returns that underlies the outperformance adjustment rests on this unsubstantiated premise that expected outperformance should be zero in an incentive-based regulatory framework.

4.7 Furthermore, it is also worth noting for completeness that the "*900 observations*" that Mr Wilde refers to are mostly observations outside of the electricity transmission sector which are therefore not directly relevant and are also historical i.e. they cannot provide a reliable guide to the future of the electricity transmission sector.[92] The most relevant price control data is that relating to transmission from RIIO-T1. Following an in-depth analysis, SSEN Transmission concluded that there is no evidence that any additional price control mechanisms are needed in RIIO-T2 based on an analysis of evidence from RIIO-T1.[93] GEMA continues to refer to reports from the NAO and CEPA in support of its position.[94] However, these reports do not support the conclusions GEMA is seeking to draw from them. The NAO report is historical and does not involve an assessment of appropriate rate of return – this is because it does not provide a holistic perspective of price control mechanisms or genuine company performance. In addition, while the CEPA report highlights a number of ways in which outperformance could be controlled for in RIIO-2, at no time does it state that the most appropriate decision would be to implement an Outperformance Adjustment.

4.8 **GEMA's insistence that information asymmetry works in favour of companies is incorrect.**

4.9 Earwaker and Fincham conclude their survey of former regulators by acknowledging: "*[r]egulators sometimes have a better knowledge of the sectors they regulate (and the comparative performance of companies in it) than individual companies*" and, while "*companies may have a better understanding of the activities they manage*", it does not necessarily imply "*a better view of the degree of future efficiency improvements they can achieve*".[95]

4.10 GEMA's Response completely side-steps this evidence. The premise of its Response is that there is something problematic with companies finding savings for the RIIO-2 period: "*some companies have already begun to find savings for the RIIO2 period that will help them towards their outperformance goal*".[96] This betrays a misunderstanding of the purpose of incentive-based regulation. Companies are expected to identify efficiencies and savings on a continual basis in response to pre-specified revenue allowances. Since companies know more about their own activities, they are best-placed to find information to identify those efficiencies. That may be an asymmetry, but it is not a problem. The CMA agreed in its PR19 January Working Papers: "*[i]ncentives are part of normal regulation and operational outperformance is a desirable outcome*".[97]

4.11 Further, as explained in detail in the Oxera WACC Report,[98] it is an unsustainable leap for GEMA to assume that information asymmetry will as a matter of principle militate against regulators:

(a) Any alleged "*systemic*" – putatively cross-sectoral – "*imbalance*" is less likely to exist in RIIO-2 given extensive use of tools to mitigate residual information asymmetry, which GEMA has not adjusted for in its dataset.[99]

(b) There is no reason why the net effect of asymmetries – some benefitting regulators and some benefitting companies – will always work out in favour of companies.[100] The shortfall between the RIIO-2 Business Plans and Final Determinations exemplifies how far asymmetry acts against companies.[101]

[92] 'AR-ER database CMA Final', **PJM1 / Tab 73**.

[93] SSEN Transmission, Response RIIO-2 Framework Consultation (2 May 2018), **NOA-1 / Tab 2 / Page 13**.

[94] GEMA's Response on Finance Issues and TNUoS, **Para. 314**.

[95] Earwaker and Fincham (2020), 'Information asymmetry and the calibration of price controls', August, **NOA-1** / **Tab 80** / **Page 24**.

[96] **PJ1 / Para 154**.

[97] CMA (2021), PR19 'Final Report' – Final Report, 17 March 2021, **SSEN Transmission PR19 Submission, Annex 2 / Para. 9.1334(a)**.

[98] Oxera WACC Report, **PH-3 / Tab 1**.

[99] Oxera WACC Report, **PH-3 / Tab 1**.

[100] Oxera WACC Report**, PH-3 / Tab 1**.

[101] Oxera WACC Report, **PH-3 / Tab 1**.

(c) The fact that underperformance happens at all (as shown in Oxera's Expected Outperformance Adjustment Report) [102] indicates that information asymmetry alone does not account for outperformance. Some companies apply effort to outperform, whereas others do not. The assertion that all outperformance will occur as a matter of course due to asymmetries is unevidenced.

4.12 In summary, the outperformance adjustment is a highly damaging decision introduced by GEMA. If allowed to stand, it will blunt incentives and is likely to cause considerable harm both to regulated companies and ultimately to consumers. The whole basis upon which GEMA has introduced the mechanism is also flawed: there is no compelling evidence to suggest that information asymmetry necessarily works in companies' favour. In any event, GEMA's Response has also failed to address why the extensive suite of regulatory tools at its disposal is insufficient to set an appropriately calibrated price control.

4.13 **GEMA incorrectly downplays the negative impact of the expected outperformance adjustment on companies' incentives to invest and become more efficient.**

4.14 Although GEMA acknowledges the expected adverse impact of the outperformance adjustment on incentives, in particular within the 0-0.25% bp range, it downplays its significance by stating that "*any reduction in incentive properties within the 0-0.25% deadband is likely to be minimal*".[103] Similarly, Mr Wilde claims that "*the incentive issues raised by Appellants generally hinge on the assumption that no information asymmetry exists or that they cannot expect outperformance of 0.25%. Further, 0.25% is a very small value for expected outperformance, which means that any incentive issues would only a small effect, if any.*"[104] GEMA also argues that there is a weak feedback loop between outperformance in one price control and the level of the expected outperformance adjustment in the next price control.

4.15 However, GEMA cannot claim that there is no effect on incentives to outperform. The downward adjustment to returns based on past outperformance will act as a disincentive to outperform regardless of the precise mechanics of how this adjustment is determined.

4.16 GEMA's Response also fails to engage with Oxera's analysis at Table 4.2 of Oxera's Expected Outperformance Adjustment Report which demonstrates with a numerical example how the outperformance adjustment will have distortionary impacts on incentives to invest by favouring lower-risk projects over transformative projects even if the expected return on both is identical. The proposed adjustment would bias investment decisions against transformational projects and in favour of lower-risk projects with marginal efficiency gains, which would have a detrimental impact on companies' abilities to meet Net Zero targets.

4.17 The Appellant therefore strongly resists the implication that the impact of the outperformance adjustment is minimal, especially when it disincentivises companies from optimising their output and delivering the best service for customers. GEMA cannot suggest that this mechanism is immune from scrutiny on the basis that it is within the scope of its regulatory judgment[105] where it acts contrary to GEMA's statutory objectives to further the interests of current and future consumers. For the reasons explained in SSEN Transmission's Notice of Appeal,[106] the decision to deduct an outperformance adjustment is wrong under section 11E(4) of the EA 1989.

Section 5: Appeal Ground 3 - Reserved Powers

5.1 Ground 3 raises an important point of law regarding the statutory scheme applicable to GEMA's price control decisions which has not yet been considered in any previous CMA appeal decision or by any court. This ground is a *vires* argument which requires the CMA to rule on the correct interpretation of the statutory scheme and the true ambit of GEMA's statutory powers.

5.2 In summary, SSEN Transmission submits that the correct interpretation is as follows:

[102] Oxera, Expected Outperformance Adjustment Report, **PH-2 / Tab 1 / Table 3.1 and Para 3.19**.
[103] GEMA's Response on Finance Issues and TNUoS, **Para. 357**.
[104] **Wilde 1 / Para 202**.
[105] GEMA's Response on Finance Issues and TNUoS, **Para. 304**.
[106] SSEN Transmission's Notice of Appeal, **Para. 5.30**.

(a) price control decisions, including decisions which materially amend a price control or any part thereof (a ***Price Control Determination***), must be effected by way of the statutory licence modification procedure under sections 11A-11H of EA 1989 (***Statutory Modification Procedure***), which has important attendant rights and safeguards for licensees, including the right to be consulted and to appeal to the CMA.[107]

(b) GEMA has no power under EA 1989 to make such decisions by way of mere directions, and moreover has no power to amend SSEN Transmission's licence by way of the statutory licence modification procedure so as to confer upon itself such powers of direction.

5.3 GEMA advances various arguments as to why it would be convenient for it to have such a power, in particular to avoid the "*disproportionate administrative burden*" GEMA says it would face if it had to go through the Statutory Modification Procedure each time it wishes to amend a licence.[108] GEMA further attempts to demonstrate that the general provision in section 7(5)(b) EA 1989 does provide such a power.

5.4 However, GEMA's argument is wrong in law. In summary, whatever the precise ambit of section 7(5)(b), it cannot properly be interpreted as giving GEMA the power to make a Price Control Determination. Such an interpretation would render the Statutory Modification Procedure entirely optional, to be used by GEMA only if and when it chooses to undergo a procedure which it evidently considers burdensome and inconvenient. This plainly cannot have been what Parliament intended.

5.5 **Section 7(5)(b) (whether by itself or read with section 7(3)(a)) does not provide the legal power to make a Price Control Determination by mere direction.**

5.6 It is axiomatic that a public authority established by statute and operating within a statutory framework can only lawfully act in accordance with the powers that have been conferred on it by Parliament. If Parliament has prescribed certain procedures that the authority must follow in order to achieve a particular outcome (such as amending a licence), those statutory procedures must be followed. The issue in this case is whether Parliament has indeed prescribed a particular procedure that must be followed in order to make Price Control Determinations, namely the Statutory Modification Procedure, or whether GEMA can instead achieve the same outcome via recourse to the more general provisions of section 7 EA 1989.

5.7 GEMA refers to section 7(5) which provides: "*Conditions included in a licence may contain provision for the conditions (a) to have effect or cease to have effect at such times and in such circumstances as may be determined by or under the conditions; or (b) to be modified in such manner as may be specified in the conditions at such times and in such circumstances as may be so determined*"[109]. GEMA relies on section 7(5)(b), which it refers to as "*self-modification*".[110] However, whilst GEMA's evidence attempts to portray its approach to "*self-modification*" in RIIO-2 as one which "*continues and develops*" the position in RIIO-1,[111] in truth it goes far beyond any previous price control, with the effect that very substantial elements of the price control have simply not been decided by GEMA and instead have been deferred to the future to be decided by way of unappealable directions. As Akshay Kaul of GEMA recently told the CMA: "*it is something of a paradigm shift in terms of the way we look at price controls, because in previous controls, […] they were largely fixed in the beginning, with relatively modest in-period adjustments, whereas this one has much more adaptability in-period*."[112] Indeed, GEMA's evidence states that there is "*a significant shift in the ratio of baseline allowances (set up front at the start of the price control) compared to allowances flowing through UMs*" which could be "*a ratio of 50:50 or 60:40 in RIIO-2 as compared to a ratio closer to*

[107] A "price control decision" is defined for the purposes of section 11F EA 1989 as a decision whose purpose is "to limit or control the charges on, or the revenue of, the holder of the licence."

[108] GEMA's Response on Totex Modelling, Efficiency and Licensing.

[109] GEMA's Response on Totex Modelling, Efficiency and Licensing **Para. 207**.

[110] **MZ1 / Paras. 27-28.**

[111] **MZ1 / Para. 31**.

[112] Teach-in Transcript - Industry Background, 8 April 2021, **Page 18**. Of course, even if previous price controls had involved the same degree of deferral of decision-making for future directions as GEMA's RIIO-2 decision involves, it would not follow that either those previous price controls or the RIIO-2 decision are lawful.

80:20 under RIIO-1".[113] In other words, as much as half of the price control has simply not yet been decided by GEMA.

5.8 It is important to be clear about what GEMA's approach involves. The non-statutory phrase "*self-modification*" is apt to mislead in this context. It implies some form of purely mechanical modification flowing automatically from incontrovertible factual developments during the price control period (for example, an increase in the Bank of England base rate). This is indeed the type of modification covered by section 7(5)(b), which envisages that the manner in which the condition is modified must be specified in advance in the licence. But the relevant licence conditions which SSEN Transmission is challenging under Ground 3 confer on GEMA considerable scope for making discretionary or evaluative decisions by way of direction about whether additional revenue is to be allowed to licensees (for example in the "*re-opener*" mechanisms) or whether existing revenue is to be removed from them (for example in the Evaluative Price Control Deliverables). The amounts in issue are vast. For SSEN Transmission alone, it is estimated that between £1.3bn and £2.8bn could be awarded via the first category of licence conditions, and almost £900m could be removed via the second category.

5.9 The extensive scope that these licence conditions give to GEMA to make evaluations and exercise discretion on potentially contentious matters is clear and striking:

(a) Uncertainty Mechanisms (***UMs***): These "*mechanisms*" are simply a broad framework within which GEMA will make Price Control Determinations. By way of example, under the Large Onshore Transmission Investment (***LOTI***) "*re-opener*", the relevant licence condition[114] briefly sets out a process whereby the licensee may apply for a Project Assessment Direction from GEMA. GEMA will then decide the application by making a direction, unless its decision is (in its own view) "*significantly different*" from the licensee's application, in which case it will use the Statutory Modification Procedure. SSEN Transmission has numerous projects falling within the LOTI re-opener, of which three each exceed £500m in value and a further two each exceed £300m.[115] GEMA notes that there is not currently sufficient certainty about the need, scale and/or timing of projects falling within the LOTI re-opener to allow them to be funded at the time of setting the RIIO-2 price control.[116] However, this is merely a result of happenstance, i.e. the fact that the existing RIIO-1 price control happens to have expired now. The current lack of certainty may be a reason for not yet allowing the revenue needed for certain of these projects (albeit the overall need for these types of investment to deliver Net Zero is itself certain), but it is no reason at all for not following the Statutory Modification Procedure at such time as there is sufficient certainty for a decision to be made.

(b) Evaluative PCDs: GEMA states that "*Evaluative PCDs could see GEMA assessing the delivery of up to 35 different PCDs in the Electricity Transmission sector alone*", and that "*[a]djustments associated with Evaluative PCDs by way of 'self' modification would only be considered if the licensee failed to deliver the consumer outcome for which they were funded*".[117] This gives the lie to the term 'self' modification. The modification does not occur automatically by virtue of the licence condition itself. What is instead envisaged is an evaluative judgment being made by GEMA on a wide range of matters such as whether and to what extent the licensee has delivered the specified output, whether an alternative specification used by the licensee has delivered an equivalent or better consumer outcome, and whether any underspend achieved by the licensee is attributable to efficiency and/or innovation.[118] These matters may well be highly contentious and require judgments on precisely the type of complex economic and regulatory issues that the CMA is well-placed to address on appeal (but the High Court in judicial review is not). The effect of GEMA's decisions may well be to strip millions of pounds of revenue out

[113] **MZ1 / Para. 16**.

[114] See SSEN Transmission, *Electricity transmission licence special conditions* (3 February 2021), **NOA-1 / Tab 16 / Condition 3.13**.

[115] **Alkirwi-1, Para. 11.17**.

[116] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Para. 190(2)**.

[117] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Para. 188**.

[118] **MZ1 / Paras. 75-79**.

of the price control. There is notably no possibility of an upward adjustment in the licensee's favour if it delivers more than the volume or number of units of the relevant output.[119]

5.10 GEMA's summary of section 7 EA 1989[120] also refers to section 7(3)(a), which provides that "*conditions included in a licence…may require the licence holder…to comply with any direction given by [GEMA or the Secretary of State] as to such matters as are specified in the licence or are of a description so specified*". Although GEMA does not advance any submissions on the proper interpretation or relevance of this provision, it may be that GEMA is implicitly arguing that the combined effect of sections 7(5)(b) and 7(3)(a) is to empower GEMA to include licence conditions allowing it to vary the price control by way of direction. On any view, GEMA cannot solely rely on section 7(5)(b) in circumstances where its approach involves wide-ranging discretionary decisions made by directions and is therefore entirely inconsistent with the notion of "*self-modification*".

5.11 Properly construed, the general provisions in sections 7(5)(b) and 7(3)(a) (whether singly or in combination) do not give GEMA the power to include licence conditions which incorporate a mechanism for future modification to the conditions by way of directions whereby GEMA is in substance materially amending the price control, whether by allowing additional revenue or removing existing revenue.

5.12 It should be noted that, at present, directions are commonly used by GEMA for decisions of a much more subsidiary nature, which are in no way comparable to Price Control Determinations. For example, under Standard Condition B3.5, GEMA can issue directions containing a general consent for a licensee to dispose of relevant assets in certain circumstances, and under Standard Condition B23.14, the Data Assurance Guidance may be modified by GEMA by way of direction.

5.13 To attempt to use a direction to make Price Control Determinations would therefore not only be contrary to the intention of the empowering statutory provisions, but would also be wholly out of step with GEMA's general practice to date and the industry's desires in respect of the circumstances in which directions will be used.

5.14 **Section 7(6) does not support GEMA's argument.**

5.15 In support of its argument that section 7(5)(b) gives it the power it seeks, GEMA heavily relies on section 7(6), which provides: "*Any provision included by virtue of subsection (5) above in a licence shall have effect in addition to the provision made by this Part with respect to the modification of the conditions of a licence*". Section 7(6) merely makes clear that if and to the extent that section 7(5) is lawfully relied upon in a particular case as the basis for modifying the conditions of a licence, such modification shall have effect in addition to the standard Statutory Modification Procedure. In other words, if section 7(5) is lawfully invoked, GEMA does not additionally need to satisfy the requirements of sections 11A-11H. Section 7(6) tells one nothing about the separate (and logically prior) question of in what circumstances section 7(5) can lawfully be relied upon; for example, whether it can be used by GEMA to make a Price Control Determination.

5.16 GEMA is therefore wrong to contend that Parliament has answered the issue identified at paragraph 5.6 above in its favour simply by leaving section 7(6) in place[121] when it introduced the Statutory Modification Procedure in 2011.[122] On the contrary, section 7(6) sheds no light on the correct answer to that issue.

5.17 **Well-established principles of statutory construction contradict GEMA's argument.**

[119] **MZ1 / Paras. 77 and 79.5**.

[120] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Para. 179**.

[121] Section 7(6) had been included in the EA 1989 from its original enactment alongside the previous version of section 7(5). Like the EA 1989 in its present form, the EA 1989 as enacted also contained a bespoke licence modification procedure, whereby GEMA could only make modifications with the licence holder's consent (under s. 11, now repealed) or following a report by the Monopolies Commission on a reference (under s. 14, now repealed). This explains Parliament's decision to include the clarificatory provision in section 7(6) from the outset.

[122] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Para. 207**.

5.18 SSEN Transmission relies on the well-established canon of statutory construction that general legislative provisions will not override more specific provisions.[123] GEMA argues that this principle does not apply firstly on the basis that section 7(6) expressly indicates Parliament's intention and leaves no room for applying presumptions about what was intended – which as set out above is incorrect and secondly that this is not a case of one "general" power and one "specific" power, but merely of "*two alternative procedural routes*".[124]

5.19 The logic of GEMA's argument is that the Statutory Modification Procedure is never the exclusive means by which a particular proposed licence modification can be given effect. Indeed, in answering SPT's appeal, GEMA makes this explicit: "*[t]here is no strict dividing line…that renders the Statutory Modification Procedure mandatory*".[125] This needs only be stated to be seen as being wrong in law. If correct, it would mean that the carefully calibrated Statutory Modification Procedure, with its important attendant rights and safeguards for licensees, would be entirely optional in the hands of GEMA. This would in effect render the Statutory Modification Procedure otiose, contrary to the basic principle that Parliament does not act in vain and that each provision of a statute must have some purpose and effect.

5.20 GEMA notably has no answer to the point[126] that separate statutory provision is made for appeals against section 11A modification decisions where the appeal relates to a Price Control Determination, as regards both (i) the availability of a substitutionary remedy in price control appeals but not in appeals against other licence modification decisions; and (ii) the longer time limit for determining price control appeals. This is a very strong indication that Parliament envisaged Price Control Determinations being made – and only made – pursuant to the section 11A Statutory Modification Procedure.

5.21 The statute must be construed in a way that recognises a proper role for both the bespoke Statutory Modification Procedure (as the primary means of modifying licence conditions) and the general licensing provisions in section 7. In the context of a price control, the line falls to be drawn between modifications which in substance constitute Price Control Determinations, which must be made pursuant to the Statutory Modification Procedure, and more minor modifications that do not materially vary the amount of revenue allowed to a licensee, which may be made by way of section 7(5)(b) "self-modification" and/or section 7(3)(a) directions. A related principle of statutory construction that also points strongly against GEMA's position is that "*the Court will not construe a statutory power to give a direction as extending to giving a direction not to comply with statutory duties under that or another statute, in the absence of clear words to that effect*".[127] In that case, the Court of Appeal held that the Secretary of State's statutory power to direct Ofcom on how it should carry out its functions did not extend to directing Ofcom not to carry out its statutory duty (if satisfied of certain matters) to make regulations exempting certain telecommunications activities from the need to obtain a licence.

5.22 Equally in the present context, the power in section 7 EA 1989 to include licence conditions which make provision for the conditions to be modified (section 7(5)(b)) and/or which require the licensee to comply with directions given by GEMA (section 7(3)(a)) cannot be construed as extending to giving a direction the substance of which constitutes a Price Control Determination and which thereby relieves GEMA of the need to comply with the requirements of the Statutory Modification Procedure. In short, GEMA cannot use its general section 7 powers to exempt itself from its statutory duties under section 11A-11H, any more than the Secretary of State could use his direction power to disapply Ofcom's statutory duty in the *VIP Communications* case.

5.23 Further, as the Court noted in *VIP Communications*: "*it would be quite wrong to place a strained construction on section 5(2) CA 2003 to give the Secretary of State extensive powers when there are not clear words justifying such powers, merely to fill a perceived lacuna in the legislation. The remedy for any lacuna would*

[123] See SSEN Transmission's Notice of Appeal, **Paras. 6.35-6.37**.

[124] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Para. 209**.

[125] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Para. 224**.

[126] See SSEN Transmission's Notice of Appeal, **Para. 6.31** read with **Paras. 2.35-2.38**, referring to sections 11F and 11G EA 1989.

[127] *R (VIP Communications Ltd) v Secretary of State for the Home Department* [2020] EWCA Civ 1564, **Reply-1 / Tab 3 / Para. 54**.

be an amendment to the statute by Parliament to confer the power contended for."[128] The same applies in the present case. Even if there were any force in GEMA's contention that following the Statutory Modification Procedure would be excessively burdensome (which as set out below there is not), this would not warrant placing a strained construction on section 7 EA 1989 to relieve GEMA of its duty to follow that Procedure.

5.24 **Following the Statutory Modification Procedure is not excessively burdensome.**

5.25 Despite the clarity of the statutory provisions themselves, GEMA attempts to cast doubt on the clear position set out above by portraying the Statutory Modification Procedure as an excessively burdensome process that will frustrate GEMA's ability to act "*responsively*" and "*flexibly*" during the price control. This argument is incorrect.

5.26 GEMA notes that there is a balance to strike between *ex ante* precision at the outset and responsiveness to matters that may change over the course of the price control, in terms of both: (i) providing additional funding for projects which were not certain to happen at the outset; and (ii) potentially removing funding that was contingent upon the licensee delivering a consumer outcome that turns out not to be fully delivered.[129] In general terms, this is correct. But it does not follow that the appropriate degree of responsiveness cannot be achieved by following the Statutory Modification Procedure as and when amendments to licences need to be made.

5.27 Despite criticising the Statutory Modification Procedure as "*sub-optimal*",[130] GEMA does not identify any cogent reasons why it would be unable to follow the Procedure as and when it considers it necessary to modify licence conditions during the price control period. The closest GEMA comes to even attempting to do so is in its reference to the "*rigidity*" of the Procedure and the need to prepare consultation and decision documents, serve hard copy documents by post on network companies, and observe the 56-day standstill period under section 11A(8)-(9) EA 1989, which GEMA says it might need to do "*tens of times annually*".[131] However, there is nothing unduly onerous about these requirements, which are appropriate and proportionate in the context of decisions on which hundreds of millions of pounds of revenue may depend. There can be no objection to consultation *per se*, not least as even on GEMA's own approach it intends to consult for 28 days before making directions (i.e. the same period as is prescribed by section 11A(3)), which is plainly appropriate given the magnitude of what is at stake. As to the standstill period, this is a necessary feature of the statutory scheme in order to ensure that a licensee's appeal rights are effective.[132]

5.28 The true 'burden' of the modification process – whether leading to directions or section 11A modifications – is not on GEMA but on the licensees, who often have to frontload anticipatory work and the attendant investment risk. An additional 56-day standstill period does not constitute an undue delay in the context of projects worth hundreds of millions of pounds that are in the development stages for several years (during which time the licensee would be in discussions with GEMA on an ongoing basis).

5.29 It is not open to GEMA to choose to place very substantial elements of the revenue which licensees may stand to receive into the category of the various UMs or Evaluative PCDs, and then rely on the fact that GEMA will therefore need to make lots of decisions during the price control period as a basis for arguing that following the Statutory Modification Procedure would be too burdensome. Yet it is evident that this is precisely GEMA's thought process. For example, GEMA states in its evidence: "*Any reduction on our*

[128] *R (VIP Communications Ltd) v Secretary of State for the Home Department* [2020] EWCA Civ 1564**, Reply-1 / Tab 3 / Para. 61**.

[129] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Paras. 185-188**.

[130] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Para. 189**.

[131] **MZ1 / Para. 36**.

[132] Under Schedule 5A EA 1989, the licensee has to apply for permission to appeal within 20 working days of GEMA's decision to proceed with licence modifications; GEMA then has 10 working days to make representations; and the CMA must decide whether to grant permission to appeal within a further 10 working days. Thus, a total of 8 weeks may elapse before the CMA's decision, hence the standstill period runs for 56 days. The CMA also has power to direct that the decision is not to have effect pending the determination of the appeal.

regulatory administrative burden is of particular importance given the increased number of UMs across the RIIO-2 Price Control."[133]

5.30 **GEMA's acceptance that the Statutory Modification Procedure is to be used in certain cases undermines its position.**

5.31 In response to SPT's appeal, GEMA argues that it is for it to decide whether future licence modifications are sufficiently important to be made using the Statutory Modification Procedure, subject only to the possibility of *Wednesbury* review.[134] However, the notion that Parliament intended the regulator itself to be able to choose whether to abide by the rights and safeguards for licensees enshrined in the Statutory Modification Procedure, which it evidently considers burdensome and inconvenient, is obviously unsound.

5.32 GEMA's recognition that there are at least some scenarios covered by the relevant licence conditions that warrant the use of the Statutory Modification Procedure itself demonstrates that its stance that use of that Procedure is entirely at its option cannot be correct. Further, the attempt GEMA has made in the licence conditions to "*draw the line*" between cases which do and do not warrant the use of the Statutory Modification Procedure is itself revealing. First, GEMA only attempts to draw such a line in relation to two of the many relevant licence conditions, the LOTI re-opener and the Price Control Financial Instruments (***PCFI***) condition. For the other licence conditions, decisions to adjust the revenue allowed to the licensee will invariably be given effect by way of unappealable directions. Secondly, in the two instances where GEMA has attempted to draw such a line, the manner in which it has done so is inconsistent: (i) LOTI re-opener: Special Condition 3.13; and (ii) PCFI: Special Condition 8.1.

5.33 GEMA's evidence wrongly glosses these provisions as requiring it "*to undertake an assessment of the significance of a modification*" (original emphasis).[135] In relation to the LOTI re-opener, GEMA will in fact be assessing the significance of any difference between what the licensee applied for and what GEMA has decided. If the difference is not viewed by GEMA as "*significant*", the decision will be implemented by a direction and the licensee will be limited to bringing any challenge by way of judicial review, not an appeal to the CMA. Equally, if any third party were aggrieved about the awarding of additional revenue to the licensee by way of the LOTI re-opener, it would not be able to appeal to the CMA.

5.34 By contrast, in relation to the PCFI, GEMA will indeed be assessing whether the modification would be likely to have a "*significant impact*" on any of the identified parties, but there is no definition of what this term means and it is evidently highly subjective. As a result, the applicability of the Statutory Modification Procedure is wholly at GEMA's discretion. The possibility mentioned in GEMA's evidence[136] of judicial review of its assessment of the issue offers little if any comfort to licensees. On this approach, a licensee would first have to successfully challenge GEMA's decision as to significance by judicial review before securing to itself the rights and safeguards of the Statutory Modification Procedure, including the possibility of an appeal to the CMA. This cannot be what Parliament intended in enacting sections 11A to 11H of the EA 1989.

5.35 Further, on GEMA's approach, there is no possibility at all of the Statutory Modification Procedure being used in relation to other relevant licence conditions. To take one example, the Statutory Modification Procedure will never be followed in relation to decisions made pursuant to the Medium Sized Investment Projects (***MSIP***) re-opener, notwithstanding that "*the volume of small and medium sized projects coming through the MSIP re-opener could exceed £1bn over RIIO-2*".[137]

5.36 **The *SONI* decision does not support GEMA's argument.**

[133] **MZ1 / Para. 37**.
[134] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Paras. 225-227**.
[135] **MZ1 / Para. 52**.
[136] **MZ1 / Para. 52**.
[137] **MZ1 / Para. 113**.

5.37 GEMA seeks to support its argument by reference to the CMA's decision in *SONI Ltd v Northern Ireland Authority for Utility Regulation* (10 November 2017) (***SONI***). In its submissions on permission to appeal, GEMA wrongly attempted to portray *SONI* as addressing and rejecting SSEN Transmission's *vires* argument. GEMA now appears to recognise this was incorrect, and instead seeks to draw support from the CMA's decision on the very different arguments advanced in *SONI*.[138]

5.38 A cursory review of the CMA's Determination and SONI's Notice of Appeal makes clear that the *vires* argument set out in SSEN Transmission's appeal Ground 3 was not in fact either argued or decided in *SONI*.[139]

5.39 Put simply, *SONI* has no bearing on the correctness of SSEN Transmission's *vires* argument. GEMA now appears to accept this, and limits its reliance on *SONI* to the proposition that judicial review is an adequate alternative remedy to a statutory appeal to the CMA and that it is therefore "*misleading*" for SSEN Transmission to refer to decisions taken under the various Reserved Powers licence provisions as being "*unappealable*".[140]

5.40 However, it remains incontrovertible that these decisions will not be appealable to the CMA, and that the aggrieved licensee will be left to pursue a considerably less advantageous form of legal challenge by way of judicial review in the High Court – with (i) a less expert tribunal, (ii) a less intensive scrutiny of GEMA's decision,[141] and (iii) a less potent range of remedies.[142] This is not affected by the ruling in *SONI* that judicial review was sufficient for the purposes of EU law and the right to a fair hearing. The licensee is entitled to insist on the full statutory appeal procedure before the CMA, which is what Parliament provided for, and is not required to accept a lesser remedy by way of judicial review merely because it was viewed by the CMA in *SONI* as satisfying the baseline requirements of EU law and due process.

5.41 **Alternatively, GEMA's exercise of power was unlawful.**

5.42 If, contrary to SSEN Transmission's primary case, GEMA had the *vires* to use the "*self-modification*" procedure, its exercise of that power to enable it to make major price control decisions by direction was contrary to the purposes of the relevant provisions of the EA 1989 (applying the *Padfield* principle[143]) and/or *Wednesbury*[144] unreasonable and therefore unlawful on that basis. GEMA has no argument in its Submissions on Totex Modelling, Efficiency and Licensing in relation to that alternative submission.[145]

Section 6: Appeal Ground 4 - TNUOS

6.1 GEMA has advanced a number of arguments in its Response in an attempt to justify and augment the evidence supporting its decision on TNUoS. However, for the reasons explained in detail in the second witness statement of Mr Alkirwi, and summarised below, none of GEMA's arguments undermine the conclusion articulated in SSEN Transmission's Notice of Appeal that its TNUoS decision was wrong in accordance with the statutory grounds set out in s.11E(4) EA89.

6.2 **GEMA's Response does not undermine SSEN Transmission's evidence on the adverse consequences of its decision to create a disconnect between risk and responsibility.** GEMA's Response does not alter the conclusion that the disconnect between risk and responsibility introduced by its decision, in combination with

[138] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Paras. 210-219**.

[139] Letter from SSEN Transmission to the CMA (24 March 2021), **Reply-1 / Tab 7**.

[140] GEMA's Response on Totex Modelling, Efficiency and Licensing, **Para. 219**.

[141] See GEMA's "Response to appeals on finance issues and TNUoS" at **Para. 41**: "*the standard of review applied by the CMA is more intense than the approach taken by the courts in an application for judicial review*".

[142] For example, the High Court, unlike the CMA, has no power to substitute its own decision for that of GEMA.

[143] See e.g. *R (Britcits) v Secretary of State for the Home Department* [2017] EWCA Civ 368, [2017] 1 WLR 3345 **Reply-1 / Tab 4 / Para. 63**: "*The Padfield principle is that a discretion conferred by statute on a minister must be exercised so as to promote and not to defeat the object of the legislation in question. It is for the Court to interpret the legislation in order to identify the policy and objects of the legislation in question.*", *Padfield and Others Appellants v Minister of Agriculture, Fisheries and Food and Others Respondents* [1968] A.C. 997 **Reply-1 / Tab 5**.

[144] *Associated Provincial Picture Houses Ltd v Wednesbury Corporation* [1948] 1 K.B. 223 **Reply-1 / Tab 6**.

[145] See SSEN Transmission's Notice of Appeal, **Para. 6.39**.

the contemporaneous weakening of the accuracy incentives applicable to the ESO, will likely lead to increasing and perpetual under-recovery of TNUoS charges for TOs during RIIO-2.

(a) **GEMA's historical comparisons are invalid.** GEMA wrongly claims that its TNUoS decision returns the industry to the position prior to the introduction of the British Electricity Trading and Transmission Arrangements (BETTA) in 2005.[146] This is incorrect, and in fact the position before 2005 supports SSEN Transmission's submissions. Pre-BETTA there was no disconnect between risk and responsibility for TNUoS charging, because, at that time, the TOs forecasted demand/generation and collected TNUoS revenue directly from users of the network. In any case, the industry was fundamentally different in the pre-BETTA period at a time that the ESO did not exist including in terms of structure, number of market participants, regulatory context, size and complexity.[147] No reliance can be placed on the position in the pre-BETTA period to support GEMA's decision.

(b) **The historical data shows a clear bias in favour of under-recovery.** GEMA's claim that there is no evidence to suggest that the ESO would systematically err in the direction of under-recovery is plainly incorrect.[148] [CONFIDENTIAL] Since the ESO bore the cash-flow risk during this period, SSEN Transmission is fully justified in expecting the ESO's forecasting performance to be *at least* as bad in the future. There is no basis on which GEMA could have concluded that the ESO's performance in this respect would materially improve as a consequence of its decision.[149]

(c) **Continual annual under-recovery each year creates a situation of perpetual under-recovery.** GEMA is being wilfully obtuse in its position that SSEN Transmission is only exposed to delayed recovery.[150] If the ESO under-recovers by a material amount on an annual basis, then any reconciliation of previous under-recovery would be offset by the further under-recovery in the year in question. In other words, continual annual under-recovery amounts to de facto perpetual under-recovery for SSEN Transmission. SSEN Transmission's concern in this regard is fully justified by the ESO's historical performance.[151]

(d) **GEMA has materially weakened the ESO's accuracy incentives.** The evidence clearly contradicts GEMA's suggestion in the Response that it has introduced a sufficient incentive framework to mitigate the risk of inaccurate forecasting by the ESO (which risk is acknowledged by GEMA).[152] The strongest incentive to accuracy was bearing the risk of under-recovery itself. Not only has GEMA removed this but it has also removed the penalty term in the ESO's licence for under-recovery. Moreover, the incentive framework that GEMA has introduced for the ESO during RIIO-2 is so weak, indirect and ill-defined that it is possible for the ESO to materially under-perform in its TNUoS forecasting role and yet earn a reward of at least £2m, if it performs well in other areas. SSEN Transmission is therefore fully justified in its concern that the ESO's performance will likely deteriorate during RIIO-2 as a result of GEMA's decision, a risk that GEMA clearly acknowledges.[153]

(e) **GEMA's enforcement record does not create sufficient incentives for the ESO.** GEMA seeks to position its recent £1.5m fine of the ESO for inaccurate forecasting as evidence of the incentives on the ESO to improve its performance in RIIO-2.[154] Yet GEMA glosses over the fact that the fine related to inaccuracies in seven-day ahead demand forecasts, not its annual forecasts relating to TNUoS. In fact, GEMA did not fine the ESO at all in respect of the forecasting errors leading to the massive TNUoS under-recovery between 2013/14 and 2019/20. There is no basis for believing that this fine will do

[146] GEMA's Response on Finance Issues and TNUoS, **Para. 500.**

[147] See **Alkirwi-2 / Para. 2.3.**

[148] GEMA's Response on Finance Issues and TNUoS, **Para. 508.**

[149] **Alkirwi-2 / Para. 31 et. seq.**

[150] GEMA's Response on Finance Issues and TNUoS, **Para. 507.**

[151] See **Alkirwi-2 / Para. 4.1 et seq.**

[152] **Wilde 2 / Para. 71.**

[153] See **Alkirwi-2 / Para. 5.1 et seq.**

[154] GEMA's Response on Finance Issues and TNUoS, **Paras. 520-521.**

anything to encourage the ESO to improve its performance during RIIO-2.[155] GEMA's decision does underscore and support SSEN Transmission's submission that such forecasting errors in the charging regime are a material issue for licensees.

(f) **GEMA's claims regarding the effects of the Targeted Charging Review are speculative at best.** GEMA is wrong to suggest that the changes that it may implement as part of its Targeted Charging Review will do anything to improve the ESO's performance.[156] Moreover, the letter that GEMA has solicited from the ESO to support this view should be given little if any weight. Irrespective of the proposed changes (which do not focus on TNUoS), charge setting still requires reliance on data, oversight and forecasted usage. The in-year data which the ESO claims in its heavily caveated letter "may" improve and mitigate future reconciliations is a smaller and secondary aspect of charge setting and collection of revenue.[157]

6.3 **SSEN Transmission has not been adequately remunerated for the cash-flow risk.** Mr Alkirwi explains why GEMA is also wrong to suggest: (i) that SSEN Transmission has been adequately remunerated for the cash-flow risk in its RIIO-2 price control; and (ii) that the issue is in any case immaterial.

(a) **SSEN Transmission's equity beta is under appeal.** GEMA is wrong to claim that the TNUoS cash flow risk is captured in SSEN Transmission's assumed equity beta.[158] The errors that GEMA made in estimating the beta mean that it does not reflect an appropriate level of risk for the TOs and it therefore cannot capture the TNUoS cash-flow risk.[159]

(b) **The time value of money adjustment in SSEN Transmission's licence is lower than GEMA's cost of debt**. GEMA is also wrong to claim that any revenue shortfalls are funded through a time value of money adjustment.[160] While it is correct that the Kt correction term in SSEN Transmission's licence contains a term for the time value of money, this amounts to only 1.2% whereas SSEN Transmission's assumed cost of borrowing during RIIO-2 is 3.6%. Therefore, SSEN Transmission cannot fully recover the funding costs of the cash-flow risk in the way that GEMA suggests.[161]

(c) **The RCF that SSEN Transmission has been funded for was not intended to cover TNUoS under-recovery**. GEMA's claim that its allowance of £0.9m per annum for an RCF to cover the TNUoS risk (amongst other things) is incorrect.[162] The RCF in question was to fund 10% of SSEN Transmission's notional 55% gearing of its RAV during RIIO-2 (which was due to grow during the period as a result of the capital investment envisaged by SSEN Transmission's Business Plan). Any borrowing to cover TNUoS under-recovery would be in addition to this 55% gearing, meaning that SSEN Transmission would either have to borrow more than GEMA assumed in the price control (raising financeability concerns) or scale back its investment programme during RIIO-2.[163]

(d) **GEMA treats the ESO and onshore TOs inconsistently.** GEMA has historically funded the ESO in its revenue collection role and indeed continues to do so in RIIO-2 despite the ESO no longer carrying the TNUoS cash-flow risk. GEMA's reliance on the size of the ESO's RAV relative to the TOs' to justify its decision to award no such funding to the latter cannot be sustained – the determining factor of the costs to the party bearing the risk is its credit rating, and the respective credit ratings of the ESO and the onshore TOs are not materially dissimilar. For the reasons explained by Mr Alkirwi, SSEN Transmission has not been adequately remunerated for such risk.[164]

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[155] See **Alkirwi-2 / Para. 7.2.**

[156] **Wilde 2 / Para. 44.**

[157] See **Alkirwi-2 / Para. 10.3.**

[158] GEMA's Response on Finance Issues and TNUoS, **Para. 509.1.**

[159] See **Alkirwi-2 / Para. 10.7.**

[160] GEMA's Response on Finance Issues and TNUoS, **Para. 509.2.**

[161] See **Alkirwi-2 / Para. 10.8.**

[162] GEMA's Response on Finance Issues and TNUoS, **Para. 509.3.**

[163] See **Alkirwi-2 / Para. 10.7.**

[164] See **Alkirwi-2 / Para. 11.1 et seq.**

(e) **GEMA's comparison with other licensees is invalid.** GEMA has conceded that the position for the TOs following its TNUoS decision is different from the distribution sectors where each network is responsible for collecting its own usage tariffs.[165] Accordingly, GEMA is wrong to suggest that its decision aligns the transmission and distribution sectors.[166] Moreover, GEMA's comparison of the scale of the cash-flow volatility with RAV (and the equivalent metric in other sectors) does not provide any justification for its conclusion that the costs to the industry will be lower as a result of its decision nor justification for its decision more generally.[167]

(f) **The costs of bearing the cash-flow risk are plainly material to SSEN Transmission.** GEMA's £0.3m estimate of the annual cost to SSEN Transmission of bearing the cash-flow risk significantly under-estimates the materiality of the issue.[168] Assuming the best-case scenario that the ESO's performance is no worse than it was between 2013/2014 and 2019/20 and that SSEN Transmission does not seek any further sums via re-opener mechanisms, these costs could be in the region of £8m-£10m (not including arrangement fees). In view of the weakening of the ESO's accuracy incentives and the need for SSEN Transmission to seek at least £1.3 billion of additional funding to stay on track to meet Net Zero, these costs are likely to be significantly higher due to the increasing revenue over the period as a result of the investment in line with the regulatory formula. These costs exceed (the portion relating to SSEN Transmission's charges of) the reduction in the ESO's financing costs that GEMA considers to have resulted from its decision. Moreover, GEMA fails to take into account the potential perpetual nature of the under-recovery, which would plainly be material to SSEN Transmission. In any case, GEMA's decision is material on the basis that it concerns a radical change to the industry that raises points of economic and regulatory principle.[169]

6.4 For all of the reasons explained above, it remains the case that **GEMA's decision puts SSEN Transmission at risk of breaching Standard Condition B7 of its licence.**

6.5 Despite GEMA's inadequate attempts to supply reasons in support of its decision after the fact, it remains the case that **there is no compelling evidence for GEMA's conclusion that the costs to the industry will be more efficient.**

(a) **GEMA's credit-rating analysis does not support its position.** In an attempt to shore up its position after the fact in the face of SSEN Transmission's claim that GEMA relied only on a simplistic comparison of the ESO's and the TOs' respective RAVs, GEMA claims in its Response that the ESO's credit rating has increased as a result of its decision.[170] However, GEMA's cost of debt allowance for the ESO and TOs was based on a Baa1 credit rating (i.e. the rating of the ESO prior to the increase) meaning that there has been no cost reduction to the industry as a result of GEMA's TNUoS decision.[171]

(b) **GEMA's submissions indicate that the cost to the industry may have risen as a result of its decision.** As noted above, the potential costs to SSEN Transmission of funding the TNUoS shortfall during RIIO-2 is higher than the equivalent costs to the ESO even in the unlikely best-case scenario. This is consistent with the fact that GEMA's notional cost of debt for the ESO is lower than that for the TOs and evidences that the costs to the industry may have risen as a result of GEMA's decision.[172]

(c) **GEMA wrongly attempts to put the burden of proof on SSEN Transmission.** GEMA's Response contains numerous references to SSEN Transmission not having produced evidence to rebut its conclusion that the costs to the industry would be lower as a result of its decision.[173] However, the fact

[165] GEMA's Response on Finance Issues and TNUoS, **Para. 562.7.**
[166] GEMA's Response on Finance Issues and TNUoS, **Para. 527.**
[167] See **Alkirwi-2 / Para. 12.1.**
[168] GEMA's Response on Finance Issues and TNUoS, **Para. 512.**
[169] See **Alkirwi-2 / Paras. 13.4-13.6.**
[170] **Wilde 2 / Paras. 25 and 31.**
[171] See **Alkirwi-2 / Paras. 14.3-14.5.**
[172] See **Alkirwi-2 / Para. 14.6.**
[173] For example, **Wilde 2 / Para. 124(e).**

that (in GEMA's view) SSEN Transmission did not present evidence that disproved the basis for its eventual decision obviously does not, in itself, mean that the decision was justified.[174]

6.6 For the reasons outlined above, **GEMA is wrong to say that its decision would not have a significant impact on market participants** – and accordingly that it did not have to carry out an impact assessment in line with its statutory obligations.[175] Moreover, GEMA's position is inconsistent with its justification for the recent fine of the ESO, in which it recognised the principle that inaccurate forecasting could have a significant detrimental impact on market participants. In any case, GEMA's decision was significant in the sense that it constituted a radical change to the industry, raising complex issues of regulatory and economic principle. An impact assessment was therefore plainly required.[176]

6.7 Finally, **GEMA is wrong to claim that it consulted fully or adequately on its decision.** Even a cursory examination of GEMA's statements in the consultation documents shows that GEMA did not consult on *whether* the TNUoS cash-flow risk should be transferred to the TOs but *how* this could be achieved. This is wholly inappropriate for any consultation, let alone one concerning a decision that may radically alter the industry and cause significant harm to industry participants.[177]

6.8 In view of the foregoing, SSEN Transmission respectfully requests that the CMA uphold Ground 4 of its Notice of Appeal and grant the requested relief.

[174] See **Alkirwi-2 / Para. 14.7.**

[175] GEMA's Response on Finance Issues and TNUoS, **Para. 552.**

[176] See **Alkirwi-2 / Para. 15.3.**

[177] See **Alkirwi-2 / Para. 16.2.**

Statement of Truth

The Appellant believes that the facts stated in this Reply are true.

[CONFIDENTIAL]

Signature of Authorised Representative

[CONFIDENTIAL]

Name of Authorised Representative

10 May 2021

Date

for and on behalf of SSEN Transmission