

30th November 2009

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Dear Cheryl,

TAR – Enhanced transmission investment incentives – Initial proposals

The Renewable Energy Association is pleased to be able to comment on these initial proposals. As you are aware our members work on all types of renewable power and heat projects connected at both transmission and distribution levels in all parts of Great Britain. We have commented on all the previous consultations on this topic.

We are broadly supportive of the direction you are proposing. The priority must be to facilitate any work that can assist meeting government's CO₂ reduction targets. Having said that there is one matter that is central to assessing what reinforcements are necessary - the fundamental review of Security and Quality of Supply Standard (SQSS). We feel the SQSS is not being given sufficient urgency.

It is universally acknowledged the existing SQSS is not a suitable means of determining what transmission investment is required for the emerging pattern of generation, i.e. with the increasing penetration of wind and a higher ratio of installed capacity to peak demand. The fundamental review of the SQSS was therefore set up in June 2008, to look at a number of issues including this. It has not yet concluded, but in our view it needs to do so as soon as possible and in any event by the middle of 2010, so that all work from 2011/2012 onwards can be tested against its outcome.

Para. 2.16 of the proposals states that Ofgem's consultants are testing for "need" against a number of criteria, but are also questioning the use of the existing SQSS as the fundamental driver of the investment plan. In our view for the next year (2010/2011) there is no alternative to accepting the current standard (NGC would be in breach of its license if it did anything else) but if the consultants wish to look at the long term appropriateness of the standards then they should do so as part of the SQSS fundamental review.

We think that it is very unlikely that any expenditure planned for 2010/11 (and possibly for the following year) would be rendered unnecessary by any changes to the standard. However, it would be imprudent to justify new

commitments much further ahead, before the results of the SQSS review are known. We would therefore urge you to encourage NGC to bring this review to a conclusion as quickly as possible, with a suggested target of next summer. This would ensure that there is no risk of expenditure being committed after 2010/11 that would not be necessary under the revised standards.

We now address your specific questions.

CHAPTER: Two

Question 1: Do respondents consider we have appropriately summarised the views of respondents to our September consultation?

We can only comment on your representation of the REA's views, which we feel to be accurate.

Question 2: Do respondents have any comments on the initial findings of our consultants or views on the issues raised by the TOs?

We do not consider it appropriate for us to comment on specific projects. However it is clear that construction costs ramp up after 2010/2011 and this reinforces our view that it is imperative that a conclusion of the SQSS fundamental review is completed in 2010. The most significant construction costs envisaged for 2010/11 relate to two projects (links to Shetland and the Western Isles) and it is therefore appropriate that consultant / Ofgem effort over the next few weeks concentrates on these projects.

CHAPTER: Three

Question 1: Do respondents have any comments on our proposed funding framework for additional investment within TPCR4?

We are broadly supportive of the proposals with the exception of the proposed period of funding for construction which we explain in our response to question 3.

Question 2: Do respondents have any views on the appropriate funding mechanism for provision of pre-construction funding?

No, we think it is relatively low risk to fund all preconstruction work to the end of 2011/2012 to keep as many options as possible open. If the price control period is extended to 2012/2013 then we think that funding for preconstruction work in 2012 / 2013 should be considered as part of the working up of the roll over arrangements.

Question 3: Do respondents have any views on our proposed approach to identifying projects eligible for construction funding?

Construction funding is by its nature more substantial and whilst it is important not to delay any work, it is also necessary to provide greater protection against unnecessary expenditure.

We suggest that during the remainder of this price control period, construction funding should only be provided for one year ahead at a time. I.e. during 2009, funding should only be committed to for construction work taking place during 2010/2011. This would allow further construction expenditure to be stopped if, in a year's time, the project was no longer considered to be required in that timescale, taking account of course of the construction costs already sunk.

It is recognised that this is not an ideal way to provide construction funding, and should not be contemplated as part of a normal price control period. However acting in this way this year in particular would allow projects to be reassessed for need following the completion of the SQSS review. Whilst this may have no effect on the need for the project and we would not advocate delaying the start of construction, we think that this is a necessary "safety" device that should not be ruled out.

Question 4: Do respondents have any views on our proposal to fund construction costs up to the end of TPCR4 for specific projects? Do respondents agree that it may be appropriate to provide funding up to an earlier end date for projects in certain circumstances?

See above. We think that for this year construction costs should only be funded for the amount that needs to be committed in 2010/2011.

Question 5: Do respondents agree that the same rate of return should apply as for other investment undertaken within TPCR4?

Yes

Question 6: Do respondents have any views on the appropriate treatment of projects beyond TPCR4 or on any interaction with our decision on the timing of TPCR5?

The funding of those costs to be incurred during TPCR5 should be dealt with under TPCR5. If it is decided to roll over TPCR4 for a year the expenditure committed during 2012/2013 should be considered as part of the arrangements for the roll over. One possible way forward for TPCR5 could be that enhanced investment returns on network investments based on TO forecasts of need could be later reduced or disallowed altogether if the investment turns out to be under-utilised. Whilst this may sound attractive to some, it is likely to add risk to TOs/DNOs. Given that these are traditionally risk-averse businesses, this may lead to under-investment unless the additional returns are at a sufficiently attractive rate in which case the overall cost to customers may be increased. Alternatively, project-specific reviews could form the enduring way forward for projects where user commitment is not possible.

We have not come to a conclusion on this and will consider carefully the arguments put forward for enhanced incentives when the main TPCR5 starts, following the conclusion of the RPI-X@20 project. If project-specific reviews are carried out, with or without consultation, it is important that the review process does not result in delay to critical projects.

Question 7: Do respondents have any comments on any other aspect of our Initial Proposals?

No

CHAPTER: Four

Question 1: Do respondents have any views on our proposed approach for taking forward our work on TO incentives to facilitate further investment within the current transmission price control?

We are happy with the process going forward with the exception that we think that in the case of construction funding the need for individual schemes ought to be reconfirmed following the completion of the SQSS fundamental review. In practice, assuming that this is completed in the first half of 2010 (which NGC should be encouraged to do), it may mean an additional exercise to reconfirm the need for work in 2011/2012 in the autumn of 2010.

If the price current price control period is extended for one year the expenditure to be incurred during 2012 / 2013 should be dealt with during the consideration of the roll over.

Question 2: Do respondents have any views on our proposed consultation process going forward?

No

We hope you find these comments useful. If you would like to discuss them further please feel free to get in touch.

Yours sincerely

Gaynor Hartnell
Director of Policy