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Dear Hannah

Open letter consultation on Transmission Price Control Review 5 (TPCR5) – the way forward

SSE welcomes the opportunity to respond to this early consultation on the application of the RIIO model to TPCR5.

In general, we support the amendments to the regulatory framework that are proposed in the 'Regulating energy networks for the future: RPI-X@20 recommendations' consultation. In particular, enhanced stakeholder engagement, outputs-led regulation and a greater focus on innovation represent timely and sensible developments to the GB regulatory approach. However, we continue to strongly disagree with Ofgem's proposals to change how it assesses the financeability of network licensees. If implemented, it is our view that these proposals have the potential to seriously undermine investors' confidence in the sector.

Accordingly, this response should be read in parallel with our recent response to the 'Regulating energy networks for the future: RPI-X@20 recommendations' consultation, and our specific response on the financeability proposals.

TPCR5 key issues: network investment

In terms of the key issues that need to be considered at TPCR5, we agree that uncertainty over future network investment remains the biggest challenge for the electricity transmission companies. However, from the perspective of Scottish Hydro Electric Transmission Limited

(SHETL), we can be reasonably confident that the volume of installed renewable energy generation in the north of Scotland will continue to grow as the industry contributes to meeting the 2020 targets. Furthermore, we can be confident that the suite of network investments that have been developed by SHETL (in collaboration with our stakeholders) over the past decade continues to represent the efficient future development of the network.

Consequently, the key uncertainty for SHETL is largely the timing of investing in the network. Determining the 'right' time for grid investment is always difficult, not least because of the 'chunky' nature of transmission upgrades. Following the Transmission Access Review, this issue has been addressed through the Enhanced Transmission Investment Incentive mechanism that assesses proposed reinforcements against a number of "readiness" criteria. We support this approach, which has worked well to date for both SHETL and consumers; hence, we believe that consideration should be given to continuing with this mechanism during the TPCR5 period for the small number of very large transmission investment projects for which the timing of investment is uncertain.

The forecast level of investment required by SHETL over the next price control period is unprecedented, particularly when compared to the current size of the business. Accordingly, Ofgem's policy in respect of future network investment, and the associated approach to financeability, makes this by far SHETL's primary TPCR5 policy issue.

Outputs-led regulation

SSE supports the move towards outputs-led regulation; away from 'bottom-up' micro regulation. We believe that a focus on a small number of clear, non-technical outputs will make licensees' activities and achievements more visible to their stakeholders.

We welcome Ofgem's approach of using the next six months, prior to issuing the final business plan guidance, to establish the primary outputs for each industry sector. We set out our views on the primary outputs for the five output categories proposed for electricity transmission in an annex to this letter.

We note that it is Ofgem's intention to set out in the final business plan guidance the required level of primary outputs, while allowing companies to make the case for an alternative level for one or more of the primary outputs in their business plans. To avoid any confusion and the possible appearance of a contradiction in this position, we would favour allowing as much flexibility as possible in the final business plan guidance and templates on the level of primary outputs the networks are required to commit to. Without such flexibility, innovation might be stifled and companies might struggle to justify delivering outputs that are prescribed by Ofgem but not supported by their stakeholders.

The initial business plan guidance emphasises throughout that the onus is on the companies to engage with their stakeholders and, from this, present a well-justified business plan. In electricity transmission, where the three licensees have businesses of very different size and scope, the opportunity to prepare ‘bespoke’ business plans is one of the key benefits of the RIIO model. However, we do also recognise that there are central components that should be common to all business plans, and we therefore suggest that development of the business plans is a further area for stakeholder engagement over the coming months.

The opportunity for bespoke business plans is welcome given, for SHETL in particular, the scale of required network investment and the impact of this on the business. It will be important to recognise the potential effect of uncertainty over future network investment on the proposed primary outputs – this will need to be taken into account when the required level of primary outputs is set. However, it would not be appropriate to try to use the primary outputs targets as a means to somehow resolve the anticipatory network investment issue. Future network investment requirements is the key TPCR5 policy issue and should be treated as such.

Timetable and process

We welcome the early sight of the key milestones for TPCR5. In the period before the initial strategy consultation document in December 2010, we agree that work to identify potential primary outputs is a priority. In addition to the further group considering financial issues, we would support the establishment of a workstream focusing on developing the final business plan guidance and templates. In parallel with this, we note that the licensees have already commenced formal stakeholder engagement.

In the early part of 2011, prior to the publication of the strategy decision document, the focus should turn to integrating stakeholders’ views into the further development of primary outputs and any associated incentive regimes.

We hope that you find these comments helpful.

Yours sincerely

Aileen McLeod
Regulation Manager

TPCR5 Primary Outputs

The following sections provide a summary of SHETL's view on the primary outputs for the five output categories proposed for the electricity Transmission Owners (TOs).

Safety

In our view, there are three potential areas where primary outputs could be identified:

1. Public safety – all TOs already have an active programme of engagement with the public on safety issues; however, this is not currently reported on. Hence, we believe that there is merit in developing a new form of annual report that would provide information on safety related public stakeholder engagement activities. This would provide additional and new information on companies' activities in this area and, therefore, add further value to stakeholders on the licensees' safety related activities.

2. Asset condition – asset health indices. Asset condition is a key factor in asset safety and, hence, we consider this to be a relevant output measure. This information is already collated and reported under the TO network output measures and is proposed as a secondary output indicator under the Reliability output measure outlined below.

3. TO staff safety during network activities – all TOs currently collect key performance indicators for safety; for SHETL this is Total Recordable Injury Rate (per 100,000 manhours). These indicators could be adopted as meaningful primary outputs. It will be important to align the reporting for staff safety with existing annual company reporting procedures to ensure the continuation of a clear and simple measure of safety that is accessible to staff and stakeholders.

The above three outputs consider both internal and external factors and would use quantitative information to present an overview of the TO's safety performance. Consistent with Ofgem's view, we do not believe it is appropriate to apply incentives to future safety primary outputs.

Reliability

We agree that the number of unplanned supply interruptions and the associated measure of energy not supplied (ENS) are the key output measures that are of interest to consumers and should be considered under this category as primary outputs.

The development of an associated reliability incentive regime will depend on the views of our stakeholders as to the current level of performance, and their expectations of future levels of performance. Accordingly, if targets and/or incentives are to be set they must be set relative to the historic performance of each specific network (that is, SHETL's target would be set using historic SHETL performance). Furthermore, the definition of a "relevant loss of supply event" will be critical in order to ensure only controllable events are targeted and/or incentivised. So, the definition must take account of a number of issues including, but not limited to, extreme weather; the network design criteria used for each network; customer choice of security, and events triggered by other users/networks.

Under the existing price control settlement, common TO network output measures have been developed and are in the process of being implemented. We see merit in continuing to use this framework as a secondary output under the reliability output category. The suite of network output measures are leading indicators of asset health and, hence, network reliability. That said, a wide range of factors are taken into account as part of a robust asset management strategy – not just asset health. Given this, it is our strong view that the network output measures do not constitute a meaningful parameter for an incentive mechanism. This is particularly the case given the large and uncertain (in terms of timing) load related transmission investment requirements that will have a significant effect on the consequential health of the asset base.

Environment

Environmental primary outputs should target the environmental impacts that can be directly and controllably attributed to the relevant network business. As such, we believe the key primary outputs should be focussed around a continuation of the existing SF6 emissions incentive; business carbon footprint reporting (consistent with that developed and agreed under DPCR5); and, for the Scottish companies with 132kV transmission assets, an output that relates to the length of 132kV overhead line that is undergrounded (again, consistent with the treatment of equivalent 132kV lines in DPCR5).

Connections

There are two key areas associated with the connections process which, in our view, lend themselves to being developed into meaningful and relevant output measures. These being: the time taken to provide a quotation upon receipt of a fully competent application (the quotation process); and the time taken to provide the physical connection assets once the quotation has been accepted (the delivery process). In either case, it will be necessary to accommodate "clock stops and starts" during the process. There is a wide range of reasons for "clock stops and starts" including, for example, additional information or changes to the requirements of the user, the planning consents process, and restrictions on network outage scheduling/cancellations.

Customer Satisfaction

Electricity transmission is, in some regards, at 'arms length' from the customer given the structure of the industry (specifically, the role of the system operator) and the small number of directly connected customers. Hence, it will be important in developing a primary output for customer satisfaction to ensure that any measure can be clearly attributable to the actions of the relevant TO and that the customer is aware of exactly who the service provider is that they are being asked to appraise. This is a particular issue for the Scottish networks where the direct relationship with the customer is with the system operator and not the TO.

Given this, we believe that for the Scottish TOs the customer satisfaction output measure should be based upon a continuation of the stakeholder engagement process. This might take the form of an annual report providing information on activities undertaken and the feedback that has been received. This approach would, in our view, be more meaningful than a 'point of contact' survey given the relatively few direct customer interactions a TO has (compared with the SO or DNO) – resulting in statistics that could be misleading if a customer satisfaction metric were to be developed.