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Dear David

**Price controls and incentives under BETTA
October 2003**

Thank you for the opportunity to respond to this consultation. This response is submitted on behalf of ScottishPower UK Division which includes the UK energy businesses of ScottishPower, namely ScottishPower Generation Ltd, ScottishPower Energy Management Ltd and ScottishPower Energy Retail Ltd.

ScottishPower UK Division continues to support the introduction of BETTA on the basis that it includes satisfactory proposals for transmission charging and losses in a GB market, and the division of responsibilities between the GBSO and the Transmission Owners (TOs).

The consultation proposes to use NGC's current two-part revenue restriction as the basis for developing the transmission price control and incentive arrangements for BETTA. Ofgem/DTI propose to adjust NGC's revenue restrictions to allow recovery of the aggregate GB allowed revenue by the GBSO through charges on users, and to introduce TO incentives. Although we await more detail on these proposals in the January 2004 consultation, we wish to highlight that the arrangements should ensure there are no perverse incentives on or double payments to NGC, as a result of interactions between incentive schemes on the TOs and GBSO and user payments through BSUoS, to the detriment of non-affiliated TOs, users and the end customer. On this basis we believe that there must be explicit equivalence in the arrangements applying to all three TOs, including NGC's TO function, and that clarity of cashflows is required. We believe that NGC's current price control and incentive arrangements should be reviewed in more detail, in the context of the split-transmission model for BETTA, and with these issues in mind.

Under the proposed model in which the GBSO is the sole contracting party with users, we believe that the relationship between the GBSO and users should be completely decoupled from the relationship between the GBSO and the TOs. Currently, each transmission licensee sets transmission charges to recover their allowed revenue from users of their own network; however it is proposed that under BETTA, NGC as GBSO will carry out this function on behalf of all transmission licensees by setting the transmission charges for all GB users to recover the total allowed revenue for all three licensees combined, and will pay the TOs their allowed revenues under the STC. We believe that consistent with this model in which GBSO acts as intermediary, the specification of each licensee's revenue restriction agreed under their price control should be decoupled from the specification of the target revenue to be recovered from transmission charges;

the former would be present in all transmission licences, the latter in the GBSO's licence only. As such, the Part 1 provisions in NGC's licence should specify the revenue restriction in relation to its own TO price control for the England & Wales network, separately from the aggregate target revenue for the GBSO, on which GB transmission network charges are based. Further, given that the GBSO will assume responsibility for GB charge-setting it must also be fully responsible for any over or under recovery from those charges, with its payments of TO allowed revenues remaining unaffected. However, any over or under recovery by the individual licensees in the year before BETTA Go-live should be reconciled by network as soon as possible after Go-live, directly with the network users affected, hence should be dealt with outwith the Kt mechanism.

The above provisions would ensure that the TO-related revenue restriction for each licensee is specified on the same basis. We also believe they should be aligned in terms of start dates and duration, be based on consistent underlying assumptions as to future connections and infrastructure requirements across GB, and subject to equivalent regulatory reporting requirements. Further, any TO incentive arrangements introduced for the Scottish TO's should also be applied to NGC's TO activity, such that the associated internal cashflows within NGC are similarly identified. Without such equivalence, it is difficult to see how any comparative analysis can be carried out.

A further consideration under the proposed split-transmission model for BETTA is the allocation of transmission costs between the TO-related and SO-related revenue restrictions, and hence between TNUoS and BSUoS charges. We note that in setting NGC's current price control¹ there was a review of the allocation of costs between revenue restrictions in terms of the split between the SO and TO functions within NGC under NETA. Given that this split will deepen under the proposed BETTA model, the allocation of NGC's internal costs between its Part 1 and Part 2 revenue restrictions should be reviewed for BETTA. Further, any costs associated with the GBSO's intermediary role should be allocated to Part 2.

We believe that, consistent with above approach to TO-related revenue, the aggregate of any BETTA implementation costs to be recovered from users should be included in the GBSO's Part 2 revenue restriction for recovery through BSUoS; the amounts to which individual licensees are entitled should be specified separately within their respective licences, and covered by the STC.

ScottishPower UK Division welcomes the socialisation of the Anglo-Scottish interconnector under BETTA, and notes Ofgem/DTI's intention to consider the associated impact on the transmission licensees' revenue restrictions within the April 2004 consultation. We would ask Ofgem/DTI to commence consideration of these issues in the January 2004 consultation so that the outcome can be incorporated as soon as possible into the development of the GB transmission charging methodologies.

A further consideration in the development of GB transmission charges is the need to take account of differences in standards across GB, which was explicitly recognised in Ofgem/DTI's conclusions document on "Planning and operating standards under BETTA" in June 2003. We are disappointed that while this consultation (paragraph 5.15) provides a summary of the conclusions of the standards consultation, there is no explicit reference to this interaction with the charging methodologies, and this was similarly absent from the August 2003 consultation on "Transmission charging and the GB wholesale electricity market". Network charges must be commensurate with the standard of service which is offered, and this principle must be incorporated into the licence conditions for charging and reflected in the charging methodologies.

¹ "The transmission price control review of the National Grid Company from 2001, Draft proposals", Ofgem, June 2000

"The transmission price control review of the National Grid Company from 2001, Transmission asset owner, Final proposals", Ofgem, September 2000

Finally, we note the consultation document indicates that Ofgem intend to introduce revised SO incentive arrangements in England & Wales before BETTA, although no indication is given of when Ofgem will commence consultation on their proposals. We remain of the view stated in previous ScottishPower responses that it is highly inappropriate to introduce further new initiatives at this time. We believe that any changes to the structure of NGC's current price controls and incentives arrangements must be considered in a BETTA context from the outset, and in particular in terms of the split-transmission arrangements to apply under BETTA.

I hope these comments are helpful. Please contact me should you wish to discuss further.

Yours sincerely

Mike Harrison

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