

David Halldearn
BETTA Project
Office of Gas and Electricity Markets (Ofgem)
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18 June 2004

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Dear David,

**Transmission price controls and BETTA - Update
May 2004**

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 Energy Management Ltd, ScottishPower Generation Ltd and ScottishPower Energy Retail Ltd.

I hope that you find these comments useful. Should you have any queries on the points raised, please feel free to contact us.

Yours sincerely,

Mike Harrison

Commercial Manager, Trading Arrangements
ScottishPower Energy Management Limited

TRANSMISSION PRICE CONTROLS AND BETTA - UPDATE

SCOTTISHPOWER UK DIVISION RESPONSE

1 General comments

1.1 ScottishPower UK Division welcomes this opportunity to comment on Ofgem/DTI's latest proposals for transmission price controls under BETTA. We are generally supportive of these proposals. However, we note that some areas are still under development, and it will be important that they are sufficiently far progressed in time for Ofgem/DTI's followup consultation on Draft Proposals, currently planned for June/July 2004, to enable them to be incorporated into other areas, in particular the development of GB transmission charging. It will also be important to ensure that there is consistent treatment of the three transmission licencees, particularly in determining appropriate adjustments to their respective revenue restrictions in relation to interconnector socialisation and any redesignation of assets from connection to infrastructure. We believe that such arrangements should follow a principle of allowing each licensee to continue to receive the same overall revenue streams as they do under the pre-BETTA contractual arrangements.

1.2 The above matters are discussed in more detail below.

2 Specific comments

Revenue adjustments in relation to interconnector socialisation

2.1 We support the proposal to amend the regulatory asset values for NGC, SP Transmission and SHETL at 1 April 2005 to ensure that each continues to receive the same overall income stream from their interconnector assets that they currently receive under the present contractual arrangements.

2.2 As a generator in Scotland with access to the interconnector we currently pay capacity charges for the use of the interconnector assets and also a cross border exit charge for leaving the Scottish system and a cross border entry charge for entering the NGC system. These 'pancaked' exit and entry charges solely imposed on Scottish exporters are a barrier to competition and inconsistent with European legislation. Removal of these charges will not change SP Transmission's and NGC's allowed price control income as the charges would be spread across system users under the agreed charging methodology.

2.3 It is important that each of the three transmission licensees is treated on the same basis recognising that the investments required for the upgrade of the interconnector post vesting were undertaken, as a result of licence obligations, by all three companies following commercial negotiations in a privatised environment. Shareholders who have invested in the parent companies of the three transmission licensees have done so on the basis of anticipated future overall income streams, of which the income streams from the interconnector assets are a constituent part.

Socialisation of the interconnector income streams would be consistent with shareholders' expectations and reduce investor uncertainty.

- 2.4 Post BETTA we do not consider that it would be appropriate to separately identify for each transmission licensee a rate of return to be made on its interconnector assets and also the costs of operating and maintaining these assets. The appropriate interconnector assets should be fully incorporated into each licensee's regulatory asset base in such a way that separate identification is not required and the licensee is incentivised to operate and maintain these assets efficiently and effectively on the same basis as it is incentivised for the rest of its transmission network. This can be achieved by adjusting the regulatory asset value at 1 April 2005 by an amount which at the cost of capital set for the price control will deliver the same income stream for each licensee as under the present contractual arrangements.
- 2.5 Under BETTA all GB generators will be able to compete directly in the GB market and with single GB transmission charging arrangements there will no longer be a separate interconnector charge to disincentivise trades between Scotland and England & Wales. It is, however, important that the new GB transmission charging arrangements do not act as a disincentive for generators to locate in Scotland, particularly as it is now widely recognised that the UK Government's environmental targets cannot be achieved without a significant contribution from new Scottish renewable generation.

Revenue adjustments in relation to connections

- 2.6 If implemented, NGC's current proposals for the GB connection charging methodology would lead to a redesignation of assets from connection to infrastructure due to the redefinition of the connection boundary over the Scottish networks under the "Plugs" model. This raises similar issues to the implementation of "Plugs" in England & Wales in April 2004, hence the treatment of the Scottish transmission licensees should be consistent with that previously followed for NGC. We agree therefore that under any such redesignation there should be consequential changes to the regulatory asset bases and adjustments to the revenue restriction where necessary in order to ensure that each transmission licensee is no better or worse off in terms of overall revenue as a result of the change in connection boundary. These revenue restriction adjustments should also provide the Scottish transmission licensees with any additional funding necessary to address legacy issues as appropriate.

Interaction with development of GB transmission charging

- 2.7 The above revenue restriction adjustments in relation to interconnection socialisation and any redesignation of assets from connection to infrastructure clearly affects the calculation of GB transmission charges. Uncertainty as to the level of these adjustments, and also the further adjustments in relation to transmission investment for renewables, compounds uncertainty as to the level of transmission charges to which users will be exposed under BETTA. It will be useful if Ofgem/DTI's draft proposals on price controls and transmission investment for renewables, both of which are currently planned for June/July 2004,

were sufficiently far advanced and in sufficient detail to provide NGC with reasonable estimates of the additional revenue to be recovered from GB transmission charges, for incorporation into the calculation of indicative tariffs for their next consultation on GB transmission charging methodologies, currently planned for September 2004.

- 2.8 The use of accurate target revenue assumptions is particularly vital if NGC continue to propose a methodology which incorporates a G:D split adjustment in order to eliminate negative demand tariffs, since the target revenue will clearly affect that adjustment. However, as stated in our recent response to NGC's GB Initial Methodologies Consultation, we do not support NGC's methodology proposals nor do we believe that G:D split adjustment is an appropriate or robust means of addressing the issue of negative demand tariffs in an enduring manner.
- 2.9 We note that charging implications of part year price controls in the event of mid-year BETTA implementation will be taken forward as part of the transitional arrangements for BETTA. It will be important that a consistent approach is followed in considering the charging arrangements over each individual network pre-BETTA and over the GB network post-BETTA.

TO incentives

- 2.10 We agree that the compensation payments to TOs in relation to outage planning should not be included in incentivised balancing costs, however it is not clear from this consultation how it is proposed that such payments would be funded instead. We would ask Ofgem/DTI to clarify such matters in their next consultation, and also demonstrate how their proposed arrangements follow the principle that the impact both on NGC and on users' charges should be the same on whichever network the outage is changed. We also believe that to the extent that NGC is required to report on the compensation payments to the Scottish TOs, it should similarly report on the costs incurred by its TO function in deviating from the agreed week 49 outage plan over the England & Wales network.
- 2.11 In terms of new connections we are not convinced that the currently proposed BETTA arrangements ensure that applications to the GBSO for new connections to non-affiliated TO networks can be progressed as efficiently as those to the England & Wales network. We believe that this creates an inherent disadvantage to Scottish users, particularly in instances of interactive applications or a shortage of transmission capacity. While we agree that specific TO incentives may not be appropriate in this area, we believe that further consideration should be given to the need for a specific obligation or incentive on the GBSO to ensure efficiency and equitability in the applications process for connection and use of system, so that no applicant is disadvantaged by the complexity of the industry contractual framework.

Costs recovery mechanisms

- 2.12 We agree that BETTA implementation costs should be recovered through BSUoS charges, similarly any TO costs in undertaking SO-related activities. We also

believe that BSUoS is the most appropriate mechanism for recoverable costs in relation to transmission activities carried out by the GBSO only. This would ensure that the GBSO revenue restriction on which TNUoS charges are based would cover the aggregate GB costs of equivalent TO-related activities carried out by the three transmission licensees over their respective networks.

SO incentives

- 2.13 We note that this consultation does not cover SO external cost incentives, on which Ofgem/DTI intend to carry out a separate consultation in June/July 2004. We would urge Ofgem/DTI to issue that consultation as soon as possible in order to give the industry a more complete picture of their overall proposals for the transmission price controls and incentives arrangements under BETTA.