ScottishPower

energy management

David Halldearn
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Office of Gas and Electricity Markets (Ofgem)
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Dear David,

BETTA consultation on the recovery of costs incurred as a result of the run-off of the Settlement Agreement for Scotland – An Ofgem/DTI consultation
November 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,

Alex MacKinnon
Regulation Manager
ScottishPower Energy Management Limited

BETTA CONSULTATION ON THE RECOVERY OF COSTS INCURRED AS A RESULT OF THE RUN-OFF OF THE SETTLEMENT AGREEMENT FOR SCOTLAND (SAS)

OFGEM/DTI CONSULTATION – NOVEMBER 2004

SCOTTISHPOWER UK DIVISION RESPONSE

1 General

ScottishPower UK Division agrees with Ofgem/DTI's view that the costs accruing in Scottish Electricity Settlements Limited (SESL) as a result of the introduction of BETTA which fall to SP Distribution Limited (SPDL) and Scottish Hydro-Electric Power Distribution Limited (SHEPDL) should be recovered.

We recognise the benefits from initially recovering these costs through the distribution price controls until their magnitude has been determined. However, we believe that all these costs should then be recovered from GB BSC parties over a period of 2 years through the proposed method of a notice issued to the BSC Panel by the Authority.

The reason the costs of the development of supply competition in Scotland in 1998 will not be fully recovered by 1 April 2005 is that cost recovery in Scotland was set to take place over a 7 year period as compared to the 5 year period adopted in England & Wales. This was in view of the higher costs per customer to be recovered in Scotland compared to England & Wales. Scottish customers have already paid more per head for the introduction of full GB supply competition than customers in England & Wales. Had 1998 cost recovery in England & Wales also been set at 7 years then cost recovery post BETTA would undoubtedly be set on a GB basis. The unrecovered Scottish costs should thus be recovered from GB from BETTA Go-live and will result in a minimal increase in GB charges.

The costs incurred in running down the staffing of SESL are a direct result of BETTA implementation. They would not have been incurred by Scottish customers if BETTA was not implemented and thus should be paid by all GB customers. Again this will result in a minimal increase in GB charges.

We agree with Ofgem/DTI that Scottish operational run-off costs and England & Wales run-off costs should both be recovered on a GB basis.

2 Areas of costs to be incurred

We agree with the categories of costs identified by SPDL and SHEPDL which will be incurred in relation to SAS run-off. It is our understanding that there will be no unbilled NETA costs to be recovered under BETTA since all such costs will have been recovered by 31 March 2005.

3 Recovery of costs

We agree with Ofgem/DTI's criteria for the costs to be recovered and that the costs incurred in running down the staffing of SESL and the operational costs of SESL under the SAS between BETTA Go-live and the termination of the SAS should be efficiently and prudently incurred.

The distribution price control is a suitable vehicle for the initial recovery of these costs until their magnitude has been determined when they can be recovered on a GB basis.

4 From whom should costs be recovered

<u>1998 costs</u>

Our view is unchanged from that set out in our response to the April 2003 Ofgem/DTI consultation on the recovery of costs under BETTA when it was still uncertain as to whether or not BETTA was to be implemented in 2004 or 2005. Had BETTA been implemented in 2004 there would still have been unbilled legacy NETA costs to have been recovered on BETTA Go-live.

Any outstanding legacy development costs in the England & Wales market or the Scottish market should be treated on a similar basis and all such costs should be included in the BETTA implementation costs and recovered over all GB following BETTA Go-live. This would place all GB participants on an equal footing when the GB market opens, be consistent with the proposed treatment of operational run-off costs and maximise implementation efficiency.

With BETTA implementation now planned for 1 April 2005 it appears that there will be no unbilled legacy NETA costs to be recovered. Nevertheless it is still appropriate to recover the outstanding costs related to supply competition in Scotland in 1998 on a GB basis from BETTA Go-live such that all GB participants will enter the new GB market with the same externally imposed costs, thereby ensuring fair competition.

The reason the costs of the development of supply competition in Scotland in 1998 will not be fully recovered by 1 April 2005 is that cost recovery in Scotland was set to take place over a 7 year period as compared to the 5 year period adopted in England & Wales. This was in view of the higher costs per customer to be recovered in Scotland compared to England & Wales. Scottish customers have already paid more per head for the introduction of full GB supply competition than customers in England & Wales. Had 1998 cost recovery in England & Wales also been set at 7 years then cost recovery post BETTA would undoubtedly be set on a GB basis.

<u>Staff run-down costs</u>

The costs incurred in running down the staffing of SESL would not have been incurred if BETTA was not implemented. They are a direct result of BETTA implementation and thus should be paid by all GB customers who will benefit from BETTA. They are not related to the benefit that Scottish customers have gained from the existing Scottish settlement system and thus it is not appropriate to charge them to Scottish customers. DTI included costs relating to the absorption of the existing Scottish settlement system in its final BETTA Regulatory Impact Assessment published in September 2004. These costs should not therefore be separated out from the other BETTA costs which will be recovered on a GB basis.

Operational run-off costs

Given that England & Wales operational run-off costs are to be recovered on a GB basis, we agree that it would not be equitable for Scottish consumers to fund a share of England & Wales operational run-off costs and also to fund Scottish operational run-off costs. It is not necessary to identify the costs involved in order to establish the inequitability, although we believe that the impact on England & Wales customers will be minimal given the size of the England & Wales market compared to the Scottish market.

These costs for administering the settlement runs relating to trades that occurred prior to BETTA Go-live for the separate England & Wales and Scottish markets are not directly related to BETTA implementation but are nevertheless incurred after Go-live. It is pragmatic to recover these on a GB basis and obviates the need for separate charging in the new GB market.

5 Mechanisms to effect recovery

Scottish recovery

We agree that the distribution price control is a suitable vehicle for initial cost recovery until the magnitude of the costs has been determined when they can be recovered on a GB basis. Provision of a mechanism to allocate the SAS run-off costs in a way that directly reflects the current process would be complex and costly. The principal parties from whom costs will be recovered through the distribution price control will be the same as those paying the current charges. The largest generator in Scotland, British Energy, does not currently pay SESL charges with the charges associated with its generation being paid by ScottishPower and Scottish & Southern Energy broadly in proportion to the relative size of their distribution customer bases in Scotland. Thus the major generators who currently pay SESL charges will continue to contribute towards cost recovery through their supply market share if recovery is channelled through suppliers' payments under the distribution price control.

GB recovery

We agree that the simplest method for effecting GB cost recovery is through the BSC and for the Authority to issue a notice to the BSC Panel specifying the sum to be recovered for each distribution licensee and the commencement date for such recovery. With potential costs to be recovered of some £7 million we believe that cost recovery should be over a period of two years.