Scottish and Southern Energy

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Our Reference:
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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 (SAS)

Thank you for the opportunity to respond to the above open letter consultation.

The issues around cost recovery of the run-off and termination of the SAS and SESL due to the implementation of BETTA have been discussed for some time. It is to be welcomed that we are nearing the end of this consultation process. However, we still do not agree with Ofgem's proposals for continuing to direct charges into the Scottish market. We consider the elements of the costs in turn below.

SAS operational run-off costs
We believe that the SAS operational costs should be recovered on a GB basis for two reasons:

i) given Ofgem's intention to charge E&W operational run-off cost out across GB it is the only equitable way to ensure Scottish participants are not encumbered with costs for both markets costs; and
ii) that the ratio of costs is a reasonable approximation for ensuring the costs are charged out in an equitable way to participants in both E&W and Scotland. We believe that it is reasonable to conclude in the way that Ofgem have that by charging out both E&W and Scottish run-off costs on a GB basis that this will result in an equitable share of each costs being picked up in the appropriate market.

We would highlight that now that Ofgem have concluded that the run-off should stop at R3, the budget for this is only some £2.1m.

SAS/SESL Termination Cost
We do not agree with Ofgem's conclusion that "as in relation to the costs of development of new arrangements, the costs of wind-up of such arrangements should be recovered from those

who have benefited from them. On this basis, such costs should be recovered from Scottish consumers."

We continue to believe that the termination costs of the SAS/SESL are not a continuation of development of the '98 arrangements, but are entirely a result of the introduction of BETTA and therefore that they should be treated as a legitimate BETTA cost to be charged out to the GB market.

1998 Capex
In a similar vein to our comments on Termination Costs, we continue to believe that the early crystallisation of the '98 Capex costs is as a direct result of the implementation of BETTA on 1st April 2005. Whilst it may have been appropriate for the costs of development of the arrangements to have been borne by Scottish consumers, these consumers would have anticipated that the arrangements would have lasted longer than five years. They may therefore rightly believe that they would be due compensation for their loss, rather than having to continue to pay for systems that have been replaced, in addition to having to pick up the costs for the new BETTA arrangements. It is also inappropriate for Scottish customers to pay for two systems at the start of BETTA when E&W customers will only pay for one. We continue to believe that these 1998 Capex costs should be charged out to GB.

GB Recovery
As indicated above, we continue to believe that all costs should be charged out on a GB basis. In doing this however, given that the bulk of costs are known, it should be possible to include these into the GB charging base at this stage rather than having to wait until the end of run-off when the exact costs are known. All that would be required would be a simple reconciliation of the costs recovered when the exact costs are known at the end of run-off.

Scottish Recovery
If Ofgem nonetheless proceed as proposed in the paper, it will be necessary to adjust the Scottish distribution price controls. In doing so, there could be two relevant issues. First, in order to allocate costs appropriately to the two distribution price controls, a simple ratio based on the historic size of the two market areas should be used. For example, this could be based on the previous years supply ratio. We understand this would give a ratio of 29:71, SSE to SP. As noted above, we believe that the bulk of costs are known at this stage, and therefore that it is appropriate that an allowance for these costs is made immediately under the price control, with a mechanism to reconcile costs with interest once the exact costs are known.

Secondly, it will be necessary to bring forward the appropriate price control licence modifications in time to be reflected in the distribution use of systems tariffs in 2005/06. If this is not possible, adjustments for 06/07 will need to reflect the extra year of financing costs for the distribution companies.

Yours sincerely

Rob McDonald
Director of Regulation