

This response is submitted by SP Transmission & Distribution, which owns and operates ScottishPower's three network businesses in GB - SP Transmission Ltd, SP Distribution Ltd and SP Manweb plc.

We do not propose to comment on the details of the proposed price control extension for NGET. In general, we found it difficult to follow the reasoning underlying the detail of these initial proposals. Nevertheless, there are a few issues, which will be important for the forthcoming main transmission price control review, where we wish to express our concerns.

First, we remain concerned that the proposed treatment of NGET's non-load related capital expenditure, in particular, could deter network owners from replacing equipment at the appropriate time, contrary to the interests of present and future customers. We do not consider that Ofgem have clearly demonstrated that NGET's expenditure was not legitimately incurred. In particular, there remain concerns about Ofgem's consultants' modelling of non-load related capex, especially with regard to overhead line expenditure, which now seem unlikely to be satisfactorily resolved in the remaining time available. Ofgem have previously set out its thoughts on the treatment of capex overspends for gas and electricity distribution which state that only if there is clear evidence of wasteful and unnecessary spending should this not be included in the RAV.

As a matter of regulatory principle, where investment has been efficiently incurred and can be justified in terms of planning or security standards, safety or other legitimate driver then that investment must be allowed into the RAV. In this case, should the interim RAV be subsequently adjusted, during the main transmission price control review, to take into account expenditure which was initially disallowed, then that adjustment must take into account the financial effect of the delayed recognition of that expenditure.

Second, although we agree with Ofgem's proposal to again use the approach to setting the cost of capital (i.e. in post-tax terms with a company specific tax allowance) which was developed during DPCR4, at this stage we do not consider that there is sufficient evidence to justify reducing the cost of capital below that recently set for DPCR4. At a time of rising investment requirements in energy networks, it is essential that the network operators are able to attract and retain equity funding and maintain an investment grade credit rating.

While we recognize that a one year price control extension warrants only a less rigorous review process than that required for a main price control review, care must be taken to avoid setting inappropriate precedents which could have unintended consequences, such as deterring necessary investment in energy networks. We would also welcome a clearer justification of Ofgem's proposals, in future.

Finally, we have concerns that it is becoming increasingly likely that a number of complex issues relating to NGET will need to be revisited, as part of the main price control review. This must not be allowed to divert resources in a way which would compromise the main review of the Scottish TOs. Equitable treatment of all parties must be assured.