

# Transmission Price Control Review

## Draft Licence Modifications

### Response from Scottish & Southern Energy (“SSE”)

#### 1. Introduction

- 1.1. We have set out below SSE’s view on the draft licence amendments proposed as a result of the new transmission price controls to be introduced in April 2007.

#### 2. Gas Entry – NGG NTS Obligations

##### *Approach to gas entry licence drafting*

- 2.1. We are disappointed that Ofgem has continued to pursue the complex incentive arrangements that were introduced at the time of the last price control review rather than reverting to a more traditional approach of network regulation in terms of capex approval. Notwithstanding this point, we support the carving up of the existing, single NTS price control licence condition into its various constituent parts to aid usability of these price control terms.
- 2.2. However, we do not support the proposal to simplify the licence conditions by removing the calculation of many of the detailed terms from the licence and instead making them subject to annual reporting requirements for NGG NTS. We believe that terms of a price control formula that are directly relevant to customers should be transparent and in the public domain which would clearly not be the case under the proposal set out in paragraph 2.9 of this consultation paper. Annual reporting requirements would be in addition to the detailed drafting within the licence.

##### *Draft legal text – Capacity reallocation obligation*

We note that much of the proposed draft legal text presented in Appendix 6 is expressing the sentiment of the discussion contained within the main document, rather than precise drafting and will therefore be subject to further change. We have therefore provided comments at a fairly high level at this stage.

- 2.3. Capacity substitution obligation. We believe the information provided in the proposed statement should also include where the capacity has been substituted from and the exchange rate that has been applied. We also believe that this statement should be made public. Transparency is extremely important when considering substitution, as are the exchange rates used by NGG, and Users would need to be reassured that, for example, a consistent exchange rate has been applied in NGG’s calculation of substitution to those given to Users requesting capacity transfers.

#### 2.4. Capacity transfer facilitation obligation.

- We believe that there should be a prescribed timescales by which, having received a request for a transfer rate, the NTS should respond to such a request.
- We not sure whether the capacity transfer facilitation obligation is restricted to unsold baseline entry capacity and unsold obligated incremental entry capacity.
- For ease of reading, we suggest the obligation to act in accordance with the methodology established should come after the requirement to establish a methodology.
- There should be a prescribed timescale within which the Authority is able to direct NGG not to implement the revisions to the methodology.
- We do not believe that a change should be made for the provision of exchange rates. NGG would be calculating exchange rates to enable it to consider and comply with its substitution obligations and therefore we do not believe additional calculations would be required to warrant making a charge to shippers.

#### 2.5 Capacity trade facilitation obligation

- We assume the obligation for shippers to confirm in writing that they wish to proceed with a capacity trade will be met by the notification of trades through the by use of Gemini.
- We assume that the drafting will be extended to include equivalent paragraphs from paragraph 1.6 onwards in the Capacity transfer facilitation obligation.

2.5. The incentive on NGG NTS regarding incremental Buy-back. Although specific drafting has not been provided for this incentive scheme, we are concerned that the wording used in paragraph 2.43 could suggest that the incentive is not solely related to the late delivery of obligated incremental capacity. The words used would suggest that it could also relate to subsequent operational issues associated with this capacity (ie greater than baseline capacity) following its delivery which was not our understanding.

2.6. Investment lead time extension. We are opposed to the proposed permit arrangement to allow NGG NTS to extend its investment lead times. In particular we believe it is inappropriate to allow NGG NTS to delay projects if it delivers others on time. In our view this would allow NGG NTS to arbitrage between project delivery to the detriment of Users at specific entry points. Furthermore, we believe it would be a form of undue discrimination between Users at different locations for NGG NTS to behave in this manner.

### **3. Electricity Transmission**

#### ***Revenue Restriction for SHETL***

3.1. The current format of the revenue restriction contains a number of terms that were designed to capture the change in circumstances for SHETL, and indeed the other transmission licensees, as a result of the introduction of BETTA. As

such there is an opportunity to consolidate and simplify the revenue restriction for these aspects. This is particularly important given the new incentive schemes being introduced that will add to the complexity. The specific terms and our views on them are set out below:

- 3.2. “ $R_t$ ” is the core regulated revenue and would be retained.
- 3.3. “ $KK_t$ ” is the correction factor for any over or under recovery of allowances the previous year and would be retained.
- 3.4. “ $LF_t$ ” is the term that currently allows pass through of licence fees (which National Grid now pays) and rates and would therefore be retained.
- 3.5. “ $EI_t$ ” is the rolling incentive term from the earlier price control and would need to continue to be consistent with Ofgem’s commitment in regard of this incentive.
- 3.6. “ $BI_t$ ” allows for recovery of BETTA implementation costs in 2005/6 and 2006/7. As the costs have now been audited, we believe that this term can now be removed.
- 3.7. “ $EC_t$ ” was an adjustment to reflect the change in role of SHETL post BETTA. Going forward, the basis revenue requirement of SHETL will be captured in the  $R_t$  term, so the “ $EC$ ” term can be removed.
- 3.8. “ $CC_t$ ” was a specific adjustment to capture connection contribution repayments. This term can now also be removed as the actual values have been incorporated into the RAV for setting the new price control.
- 3.9. “ $IAT_t$ ” covers specific adjustments for an income adjusting event and would remain.
- 3.10. “ $IAAC_t$ ” is a correction in 2006/7 to reflect actual customer contribution repayments compared to the allowance “ $CC_t$ ”. Since this has now been completed, we believe this term can also be removed.

### ***Condition J3***

- 3.11. This condition refers specifically to the adjustments required as a result of capital contribution repayments. As noted above, these have now been concluded for SHETL and in our view condition J3 can be removed.

### ***Regulatory Reporting***

- 3.12. In general, we would support the proposals to capture all reporting requirements into a single new condition B16. We comment on the range of specific licence conditions in section 4 below.

### ***Transmission Investment for Renewable Generation (TIRG)***

- 3.13. Ofgem has not proposed any changes to the licence conditions for the TIRG funding mechanism. However, the September TPCR update document proposed a change to the depreciation period for these schemes. Specifically, in paragraph 8.39, Ofgem states that “Given the proposals for accelerated depreciation, we now consider that it is appropriate to adopt a 20 year depreciation period in respect of the approved TIRG schemes.”

- 3.14. This would imply that the  $DEP_t$  term in the schedules for the specific TIRG projects would need to be doubled, since this was set with a 40 year assumed depreciation.

### ***New Special Conditions***

- 3.15. New special conditions are envisaged for various new incentive arrangements under the TPCR. These include Revenue Driver, SF6 and Innovations Funding incentives. While we recognise the policy initiatives driving these proposals, we are concerned that much of the detail remains to be resolved.
- 3.16. We are also concerned that little further information has been provided on the interruptions incentive. This is a particular concern given that Ofgem is proposing a “penalties only” incentive. A further concern is that it has become apparent that the three transmission licensees report interruptions differently. More specifically, SHETL has not historically reported short duration interruptions, whereas the other licensees do.
- 3.17. We would agree that the information presented in the GB system performance report should be on a consistent basis. However, we do not believe such short duration interruptions should form part of the incentive as they reflect, in general, automatic reclosure after transient faults.

### ***Revenue Drivers***

- 3.18. Discussions have been going on for some time about the details of the revenue driver mechanisms to fund transmission infrastructure for new renewable generation. There are a number of outstanding issues of detail and we are concerned to ensure that the policy is properly set out in the final proposals document so that licence conditions can then be drafted.

### ***Innovations Funding***

- 3.19. In the discussions regarding innovations funding, we have proposed that there is a deminimis level of funding that should be available for small companies such as SHETL where a small percentage of allowable revenue would not support a meaningful level of innovation. As currently drafted, there does not appear to be any such deminimis term.

### ***SF6 Incentive***

- 3.20. The proposed drafting appears to work adequately for the mechanism proposed in the September update document. However, whether this is a meaningful incentive depends upon the level of reward available to consider investment in improved facilities.

## **4. Revised Regulatory Reporting Requirements**

- 4.1. Ofgem have proposed a number of changes to standard licence conditions B1, B2, B6, B7, B9 and B10. The majority of these proposed changes are to ensure consistency and, in principle, we agree with the proposed changes.

- 4.2. Changes to condition B1 relate to the content and timing of regulatory accounts. As currently drafted, there may be some overlap between the information reported under this condition and that reported under the proposed new condition B15 (Price control review information). We believe that the condition should be clarified to avoid the potential for reporting the same information in two different formats in one year.
- 4.3. No changes are proposed to standard licence conditions B3, B4, B5, B8, B11, B12 and B14. We agree that these conditions do not need to be revised. Further, we agree that condition B13 (BETTA implementation) should be removed.
- 4.4. New standard conditions B15 and B16 are proposed for price control review information and revenue reporting respectively.
- 4.5. The purpose of condition B15 would be to require licensees to report, on an annual basis, information about the transmission business that Ofgem would use to monitor performance and set price controls. While we accept the rationale behind the introduction of this condition, particularly given the number and complexity of proposed new regulatory mechanisms, it is important that the information requirements set out in the RIGs are proportionate – particularly for a business of the size and scope of activities of SHETL.
- 4.6. We note that the draft licence condition does not state the date at which the licensee must deliver the price control review information to the Authority. As we have stated in response to previous consultations, we believe that this should be in September, consistent with the accounting timetable.
- 4.7. We would anticipate that the requirement for annual reporting would result in a reduction in the information requirement from licensees at the time of the next periodic review.
- 4.8. The purpose of condition B16 would be to consolidate all the existing revenue reporting requirements. We agree that this is a sensible approach particularly given the likely complexity of the new price control formula. However, as with condition B15, we believe it is important that reporting requirements remain proportionate to the size of the business.

## **5. System Operator Standard Conditions**

- 5.1. We agree that, while determinations under Condition C18 are outstanding, it would not be appropriate to remove the condition from the licence.

## **6. Transmission Owner Standard Conditions**

- 6.1. Section D of the licence contains a number of conditions that were specific to the introduction of BETTA and have now served their purpose. We therefore agree that Condition D12 (Scottish Settlement Agreement) and Condition D15 (Obligations relating to TO offers during the transition period) should be removed from the licence.
- 6.2. In this respect, we agree that condition B13 (BETTA implementation) should also be removed.

## **7. Transmission Special Conditions**

- 7.1. A number of the special conditions for SHETL could also be removed as a result of changes since the introduction of these conditions. This would improve readability and simplify the structure of the licence. In particular, Condition G: Requests for transit could be removed as that Directive has now been repealed. Condition H: Change coordination for the Utilities Act could be removed as that Act is now fully in force. Condition I: Definitions could be consolidated into Condition A: Interpretation. Condition J3: Capital contribution repayment adjustment could be removed as this has been completed. Finally, Conditions L, L1, L2 and P should be incorporated into the new B16 since they relate to reporting requirements.