4th February 2011

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Dear Hannah

Strategy for the next transmission price control

The Renewable Energy Association gives below its response to this consultation. As you know our members work on all types of renewable power and heat projects including many electricity generation projects that are dependent on the transmission system. Whilst some of our members are involved in the injection of renewable gas into gas distribution networks this response concentrates on the electricity transmission price control strategy.

We do not propose to comment separately on the subsidiary documents but have reviewed those on outputs and incentives and uncertainty mechanisms and our comments on those are incorporated into our response on the main document below.

Our overall comment is that whilst there are many good ideas proposed we remain disappointed and perplexed that you have failed to recognise that the outcome of the fundamental review of the SQSS should be the starting point for the business plans to be developed for the price control. The review does therefore need to be brought to a timely conclusion and / or the timing for the business plan submission needs to be delayed until after that milestone.

We note that despite our previous comments you have neither included the completion of the SQSS review as a milestone on the RIIO –T1 process (for electricity) nor given any reasoning as to why this should not be the case.

Response to specific questions asked

CHAPTER: One

Question 1: Do you have any comments on the proposed process and timetable for the review?

We are not convinced that the provision for a fast track process is appropriate for the first time application of RIIO. The downside of having provision for this is that it is forcing the important initial stages of the review to be completed more quickly than would otherwise be necessary.

CHAPTER: Two

Question 1: Do respondents consider there are any interactions with other policy areas that have not been highlighted in this chapter?

The Electricity Market reform work has not been mentioned. Whilst this is a very fundamental piece of work we think it is unlikely to have any first order impact on the transmission price control.

Whilst the interaction with the fundamental review of SQSS has been mentioned that interaction has been described in what we can only describe as precisely the wrong way around. It is the result of the fundamental review of the SQSS that should be the starting point for RIIO-T1. Whatever emerges from the review will define how much expenditure is required to meet any "demand" for transmission capacity. How therefore can the SQSS review outcome can be anything other than the starting point for the price control review?

Question 2: Do respondents consider that the transmission and gas distribution price control periods should remain aligned for future review periods?

We have no view on this but cannot see any reason why the periods should need to be aligned.

CHAPTER: Three

Question 1: Do you have any comments of the overall approach to stakeholder engagement?

It may be useful for some of the questionnaires being used by TOs to be discussed by a small stakeholder group before being launched. Fundamentally the value in obtaining transmission customer feedback is to establish how much they value different services and what their views are on paying more or less for different levels of service. It is therefore important for meaningful questions that ask about how particular services are valued and give an indication at the same time about how the levels would be expected to change if more or less resource was spent on them.

Apart from general issues of reliability levels this would establish for example how highly valued quicker levels of response to connection requests would be.

Question 2: Do you have any views on how our engagement process and that of the network companies could be made more effective?

See the response to the previous question.

CHAPTER: Four

Question 1: Do you consider the proposed outputs and associated incentives, along with the other elements of the proposals, will ensure companies deliver value-for money for consumers and play their role in delivering a sustainable energy sector?

All incentives can do is encourage certain behaviour, they cannot ensure it. In terms of value for money we reiterate our view that the core of establishing what constitutes value for money in transmission would entail a timely completion of the fundamental review of the SQSS. Without this it will be impossible to determine whether whatever is promised will be delivered or has actually been delivered is the best possible value for money.

Question 2: Do you consider that the proposed outputs and incentive arrangements are proportionate?

Generally yes. We agree that it is not appropriate to have incentives related to the achievement of safety. This begs the question of what is the point of having safety as an output as such. Clearly it is a very important outcome that has to be delivered in exactly the same way as compliance with all statutory obligations.

Question 3: Do you have any views on the proposed outputs or incentive mechanisms?

We agree with you that the current level assumed for the value of lost load for incentivising transmission system security is too high. Establishing an appropriate lower level should be a priority as it should be an important input to work to develop the SQSS, which itself should determine the level of transmission expenditure required for any level of "demand" for transmission.

We think that there should be an incentive related to the achievement of a lower carbon generation mix. Because how much low carbon generation wishes to connect and use the system is outside the control of the TOs a double negative type of incentive is probably the most appropriate i.e. TOs should be incentivised not to prevent low carbon generation from connecting and using the system. We think that this has some advantages over the proposals for a positive incentive scheme but would be supportive of whichever type of scheme Ofgem considers better. For the avoidance of doubt the above should be taken to mean that we do support a scheme that encourages the TOs to support as appropriate the connection and access of low carbon generation.

CHAPTER: Five

Question 1: Is our proposed approach to cost assessment appropriate?

We think that benchmarking total expenditure as well as capital and operating expenditure is probably a satisfactory method of cost assessment, together of course with seeking independent advice.

Question 2: Do you have any views on our proposed process for proportionate treatment?

We think that the proposal for fast tracking some companies is fraught with difficulty. You have noted the possibility of fast tracked companies being worse off and propose to take measures to avoid this. The possibility arises because of additional information becoming available after the fast tracked company's price control has been set. The possibility must also arise that information becomes available that shows that the company got a price control settlement that was more generous than it ought to have been. This illustrates just one issue with trying to compete the price control for some companies almost a year earlier than the process requires.

Question 3: Do you have any views on the criteria for assessing business plans? Are any of the criteria highlighted inappropriate? Should any additional criteria be added?

We do not believe that any of the criteria proposed are inappropriate. Companies should also be invited to consider innovative ways for coping with uncertainty, both in their network development strategy and in how it might be treated financially. The latter is mentioned here notwithstanding its fuller discussion in the next chapter.

Question 4: Do you have any views on the proposed role for competition in third party delivery?

Providing the proposals for third party delivery do not lead to a material delay to any projects (which is an important and not insignificant proviso) we welcome them cautiously as another tool to give best possible value for money. Major projects such as the direct current offshore bootstraps may be candidates for such treatment given their similarity in many ways to offshore transmission work which is already open to owner / operator competition.

CHAPTER: Six

Question 1: Do you have any views on the uncertainty mechanisms identified?

We think that they cover most possibilities. We note that you have not covered the possibility of disapplication of the price control mechanism because required expenditure becomes significantly lower than that envisaged when the price control is set and this arises in a manner that is not compensated for by the volume or other identified adjustment mechanism.

Question 2: Are there any additional uncertainty mechanisms required that we have not identified?

We think that approval of any significant changes to the SQSS should trigger a review of the price control as this may have a significant effect in either direction on the expenditure required to meet any set of volume driven requirements. It is for this reason that we feel that the fundamental review of SQSS should be completed in 2011 (and ideally before the first business plan submissions are made).

Question 3: Are there any mechanisms that we have included that are not necessary and, if so, why?

See above.

CHAPTER: Seven

Question 1: Do you have any views on the role of innovation in RIIO-TI?

Clearly companies should have incentives to innovate in order to deliver more at a lower cost in the future. However many innovation projects may not deliver the anticipated savings or may deliver them at a point in the future when there is no certainty about whether the TO will be permitted to make a reasonable return on the investment in innovation. As electricity transmission is not expected to have the same risk / reward profile of for example drugs companies that spend vast sums on innovation, most of which produces no return but some of which leads to breakthroughs on which large profit margins are available, that "free market" method of incentivising innovation is not appropriate. It is therefore an "administered" approach that is required that allows additional funding for "approved" projects but then may not allow the cost savings from successful ones to be completely kept by the company that developed them. We therefore feel that a scheme of the type proposed is appropriate.

Question 2: Do you have any views on the time limited innovation stimulus?

We are slightly curious as to why the transmission package is time limited. We understand that the electricity distribution LCN fund will be reviewed or absorbed into the overall distribution price control in 2015 as RIIO was not available for that price control. It is however for the electricity transmission control so the innovation incentives may be as embedded into the main price control arrangements as they will ever be.

CHAPTER: Eight
In this chapter we have only responded to question 2

Question 2: Do you have any views on our proposed approach to depreciation?

In our view depreciation should reflect the anticipated economic life of the assets which should in a period of rising demand be similar to the technical life of those assets. Although the advent of "smart grids" may lead to the widespread uses of equipment (for example electronic control systems and wide area communication networks) that have a shorter technical life than primary transmission hardware, we do not consider that this should be used as an argument for general shortening of the depreciation period. Would it not be possible to have different depreciation periods for different types of equipment, better reflecting reality? It is acknowledged that this would increase the complexity of the price control but the option should surely be considered.

We hope that you find these comments useful. Please let me know if you would like to discuss them further.

Yours sincerely

Gaynor Hartnell

Chief Executive, Renewable Energy Association