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Hannah Nixon,
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Dear Hannah,

Project Transmit: approach to electricity transmission charging work.

Thank you for the opportunity to respond to your letter of 27th May 2011.

As you will be aware from our previous responses to the Project Transmit open letter consultations in September 2010 and January 2011, we broadly welcome this review of electricity transmission charging. We believe it is both a timely and appropriate way to proceed on this important matter.

Ofgem has commissioned a number of pieces of work from the academic community and has received responses from stakeholders (which have included additional work from the academic and consultancy community commissioned by stakeholders) in writing or via the roundtable and/or face to face meetings. It seems to us appropriate that Ofgem, having reflected on this evidence, have put forward the emerging options as set out in your letter of 27th May.

The initial conclusions that Ofgem has come to, namely that the wider changes should not proceed further at this time is, in our view, both sensible and pragmatic. We concur with the assessment that these wider changes should be outside of the scope of Project Transmit and that by so excluding them will enable further consultation on charging recommendations to take place broadly in line with the original timetable (and scope) of Project Transmit and thus provide greater certainty for the industry.

The other conclusion reached is that the focus of Project Transmit going forward should be on TNUoS charging changes alone. This too is an appropriate position to reach having reflected upon the body of evidence to date.

We note that there are three broad options still 'on the table', ranging from a socialised (or "postalised") charge, through the 'status quo' ICRP to Improved ICRP. We understand the socialised option to be broad in nature and it should include, as part of your deliberations, a very flat 'postage stamp' model as well as our postalised proposal.

Mindful of the need for brevity, we do not repeat here the details of our proposed postalised approach, nor do we repeat why we consider ICRP (be it in the form of the 'status quo' or Improved) inappropriate for electricity transmission charging - we refer you to our previous comments. However, we note that there was no support for ICRP among the academics, and that some were particularly scathing of this approach. We therefore do not believe that a credible solution to transmission charging can be based on the current ICRP methodology, and that any "improved" ICRP can only be similarly flawed. If you require further clarification please do not hesitate to contact me.

Having come to these conclusions on the emerging options it is right, as Ofgem has done, to consider the appropriate way to proceed from here in terms of developing and assessing the options for charging under Project Transmit. We welcome the intention to initiate detailed modelling work to identify the likely impacts of the different potential options for change and to take forward this work in an open and transparent way.

It is imperative however, that the modelling work takes account of the wider impact of the options, including the impact on existing plant (both renewable and conventional), the meeting of renewable and climate change targets, and security of supply as well as the practical constraints that affect location of generation facilities. It should not simply be about the cost of transmission infrastructure. We look forward to contributing to this endeavour in due course, be that via focused work groups and/or written consultations over the coming weeks and, in particular, we welcome your suggested involvement of industry in the specification of design features and appropriate assumptions that feed into the analysis. We also look forward to responding to your proposed October 2011 consultation on the outcome of this work.

We welcome the intention to implement changes in 2012 whilst recognising that to have arrangements in place for April 2012 is ambitious. Nevertheless we would urge Ofgem to progress these TNUoS changes as quickly as possible. As noted in the letter, changes may be required to NGET's licence and to the CUSC. With respect to licence changes, it may well be necessary to undertake these prior to the TNUoS charging methodology changes and we would suggest Ofgem starts the preparatory work on the licence changes sooner rather than later. In our view such preparatory work would be a pragmatic use of the time between October this year and January next year and would not, for example, fetter the position of either the Authority or National Grid.

With respect to the practicality and timeframe for implementation, there is still the matter of the associated IT system changes required of National Grid (and, potentially, stakeholders). This is especially the case with the most complex option, namely Improved ICRP. In this regard we note that similarly complex recent charging change proposals, namely those associated with the TAR CUSC changes, were, according to National Grid, likely to require a 17-24 month lead time for its IT system changes. This would clearly breach the original timescale for the project.

Turning to the matter of the detail of the SCR, we broadly welcome the suggested way forward. We note that when the SCR approach was introduced as part of Ofgem's Code Governance Review, stakeholders were advised that the use of the SCR power would be limited both in terms of the number raised each year and the topic area. In our view undertaking an SCR to address electricity transmission charging is in this instance appropriate and proportionate at this time. We therefore concur with the conclusion that there is a need for this piece of work to be undertaken and that the SCR route is appropriate (as the stated SCR criteria are met in this case).

In relation to the scope of the SCR, again we agree with the assessment that the focus of the SCR should be on the potential short term changes to the current TNUoS arrangements and thus the SCR should focus on the previously noted options, ranging from a socialised (or "postalised") charge, through the 'status quo' ICRP to Improved ICRP.



In terms of the scale and timetable of the SCR we concur with the suggested launch date of July 2011 and should it be decided to proceed with an SCR then we look forward to contributing to the process over the coming months to the potential conclusion of the SCR in January next year.

As noted in your letter¹ the SCR process could “*result in changes being brought forward to more than one code*”. In addition, in your letter of 11th March 2011 it is stated that “*the way transmission losses are allocated interacts with how other costs incurred in transmission are charged out*”. We agree with these statements. It goes on to state: *We consider that there may well be interactions between some of the issues that we will consider in the context of an impact assessment on P229 [zonal transmission losses], and the issues that we are considering in Project Transmit*. We concur with this statement as well. You also note in that letter that you consider it “*may be prudent totake into account any relevant interactions [with P229]*”. Again, we wholeheartedly agree with this.

In our view it would therefore be remiss of Ofgem to make any decision on (P229) zonal transmission losses on a different timescale to the conclusion of Project Transmit SCR. As you will see in our response to the Ofgem (P229) zonal transmission losses regulatory impact assessment consultation for 4th July 2011 we foresee significant problems with the P229 assessment to date. We believe that these problems render the analysis (on which that RIA is based) flawed. We believe that this and the use of the SCR process provide the opportunity to align the timescales for decisions on TNUoS charging and Zonal Losses and that the opportunity to do so should be taken.

To conclude, we welcome the initial conclusions reached to date and the suggested way forward outlined in your letter of 27th May 2011. We hope you find these comments helpful and if you wish to discuss them further then please do not hesitate to contact me.

Yours sincerely

Angus MacRae
Head of Electricity Strategy

¹ Your footnote 2 on page 1