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Your Ref: 26/12

Our Ref:

Date: 18 December 2012
Contact: Alan Michie
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Dear Ian,

Open Letter: Update on the Integrated Transmission Planning and Regulation Project – request for further views and evidence

This response is from SP Transmission Ltd (“SPT”) as the onshore Transmission Owner (“TO”) for the south of Scotland.

We support the ITPR project objective to ensure the GB regulatory regime for electricity transmission facilitates the most efficient and economic investment planning and delivery over the long-term. Delivering UK energy policy is heavily dependent on appropriate and effective regulatory arrangements which facilitate the delivery of essential network infrastructure. We therefore believe that it is important that all stakeholders can contribute and that this is possible if a pragmatic approach is taken, as set out in more detail below.

Onshore Competition

This response primarily focuses on offshore. However, we also recognise that ITPR includes considering competition onshore. On this point, we would again comment that we do not believe that the anticipated benefits for consumers of onshore competition have been sufficiently demonstrated.

Effective separation has governed the onshore systems since BETTA and has delivered an effective onshore integrated transmission system. We have well-developed skills and expertise across both pre-construction and construction activities, as for example demonstrated by our strong track record for the cost-effective and timely delivery of essential system reinforcements.

If there must be onshore competition, there must be clarity over accountabilities between the incumbent and third party TOs and the NETSO. We also believe that third parties should be responsible for the entire project, including pre-construction and pre-engineering activities.

Approach to Offshore Development

SPT is heavily involved in developing offshore solutions in order to meet our licence obligations. The Western HVDC link, as a joint venture National Grid, is now in the construction phase. We are also fully engaged with National Grid and Scottish Hydro-Electric in scoping an Eastern HVDC link. Our direct involvement in these projects has highlighted the practical difficulties in connecting offshore wind farms and transmission assets on a common system. We believe that it is important that windfarm developers, OFTOs and onshore TO's have a common understanding of the difficulties in integrating offshore generation, interconnectors and onshore and offshore transmission reinforcement.

Given that there is a risk that uncertainties around the regulatory frameworks could delay offshore wind, we recommend that in addition to aiming to create a coherent regulatory framework, the ITPR project should also apply a pragmatic approach to expedite individual onshore / offshore works. This would apply where there is a clear need case and where an appropriate, cost-efficient technical solution (that works in the longer term) has been identified. Once the solution has been identified, the ITPR project should support addressing any regulatory changes, or perhaps one-off dispensations, to allow all interested parties to take part on an equitable basis. Such an approach would complement any new or amended regulatory arrangements identified by the ITPR project.

Our point around being pragmatic is that, at least in the short to medium term, the distinguishing factor between on onshore TO's requirements and offshore wind requirements is likely to be technical around the onshore TO's requirement to maximise capacity through 600kV HVDC links while the building block for offshore windfarm connections will either be a 220kV AC or a 320KV HVDC connections, dependant on the distance to the shore. The interface point could be an onshore or offshore hub, and could be clearly defined.

Strategic Direction and Coordination

The challenges that we face going forward, and our experience over recent years, have highlighted the importance of strong strategic direction and coordination. We recommend that a structure based around the ENSG, acting as a high-level design authority providing strategic direction and coordination, co-chaired by DECC and Ofgem, and working very closely with National Grid as the NETSO, is a model that has worked to date and should be seriously considered. This would be a good model for coordinating offshore transmission as it would allow for a longer term view and support the involvement of all stakeholders.

Optimising System Costs

We are acutely aware of the scale of constraints in and from Scotland and, like Ofgem, we expect that the implementation of the Network Access Policy will help optimise these costs.

In Scotland, high constraints are due to the scale of renewable generation that has connected over recent years. It is notable that the scale of constraints across the Cheviot boundary (i.e. from Scotland to England) has recently reduced while constraints within Scotland have increased. It should come as no surprise that the reduction across the Cheviot boundary is due to the completion of the joint network reinforcement to increase the Cheviot boundary capacity from 2200MW to 2800MW.

Our point here is that although it is absolutely right to optimise short-term constraints, the priority must be to reinforce the network through the ENSG agreed projects as quickly as possible, and accept that there may be higher constraints until these reinforcements are complete. In addition, it is important to note that the GB onshore TOs also need to refurbish and replace existing assets as they reach end of life, and that this work will have to be carefully coordinated to limit system impacts and minimise constraints. The Network Access Policy will help by setting out principles to ensure that the right decision is taken when assessing the economics of short term versus medium and longer term system costs.

It is important to note that Ofgem has strongly incentivised the onshore TOs to deliver their system reinforcement outputs as part of their RIIO T1 package. Failure to deliver these outputs could lead to substantial penalties of up to 10% of allowed revenue.

Conflicts of Interest

We would refer Ofgem to their open letter of 19 June relating to SPT's EU certification in which it stated "*the Authority considered that SP Transmission Limited's arrangements as of 3 September 2009 guarantee more effective independence of SP Transmission Limited than the provisions of the Independent Transmission Operator model set out in Chapter V of the Electricity Directive*". For the avoidance of any doubt, we would stress that we have NO conflicts of interest, as may have been implied by certain stakeholders.

The RIIO T1 pre-construction funding referred in the open letter is to commence the detailed design and pre-construction tasks for an east coast offshore reinforcement necessary to ensure compliance with our licence obligations.

The issue of conflicts of interest for onshore and integrated design is an understandable concern where competition is being encouraged. However, effective separation has governed the onshore systems since BETTA and has delivered an effective onshore integrated transmission system.

The following appendix provides our views on some of the questions raised.

Yours sincerely,



Alan Michie
Head of Regulatory Policy and Commercial
SP Energy Networks

Questions

1. Do you think that the key issues, as described above, should be considered? What is the materiality of the issues identified?

System Costs

As part of their RIIO T1 package the TOs are incentivised to complete agreed system reinforcements in line with their plans. In this open letter there appears to be an emphasis on minimising short-term constraint costs. We would comment that the ability for TO's to manage short term operational costs to minimise constraint costs is hindered by the lack of visibility of constraint costs.

However, the priority must be to reinforce the transmission network through the ENSG agreed projects as quickly as possible, and accept that there may be high system costs until these reinforcements are complete. It is important to note that Ofgem has strongly incentivised SPT to deliver its system reinforcement outputs as part of their RIIO T1 package and failure to deliver these outputs could lead to substantial penalties of up to 10% of allowed revenue.

Rather than a lack of incentive on short term operational planning, it is important to consider the economic impact of system costs in the short, medium and longer term. Like Ofgem, we expect that the implementation of the Network Access Policy will help optimise whole system costs over the full time-period.

Connection Offers

Connection offers for potential grid connections in SPT's area are always delivered in line with licence timescales. At times, this focus can limit our ability to identify the most economic solution, particularly in situations where multiple developers seek connection in a constrained area.

It is difficult under the current regulatory arrangements to fund anticipatory investment. To mitigate the risk of stranded assets a regime that encourages co-ordination of developers would be of benefit. From our perspective more coordination between developers could help us achieve more economic and efficient network outcomes, and possibly also accelerate the planning and consenting process. We have raised this point in our recent connection stakeholder forums in July and September however there was limited support from developers who operate in a very competitive environment.

Coordination and Integration

The ENSG has developed onshore integration effectively. Working closely with the NETSO, we believe that it would be a good model for co-ordinating offshore transmission as it allows a longer term view and involvement from all interested parties. Ofgem and DECC should consider establishing this group as the basis for any future regime to encourage offshore integration.

The issue of data sharing is a significant hurdle in the design and development of an offshore regime where new parties are becoming involved. Currently this works effectively onshore as each of the TO's have access to the GB system model to facilitate system design. We agree that a suitably independent design authority is required to manage this information exchange to all parties responsible for transmission system design and construction.

2. Are there any other issues to be considered in this area?

The current TO - SO model in the UK for onshore transmission system ownership and operation is effective and has been endorsed by the recent European unbundling derogation.

However current European Code drafting does not seem to consider the GB regime and is at risk of placing responsibilities on TO's and OFTOs that can only be fulfilled by the NETSO currently. It is essential Ofgem do all they can to ensure the new codes align with our regulatory regime, or consider what changes will be required to allow TO's and OFTO's to operate as system operators for their assets.

The issue of conflicts of interest for onshore and integrated design is an understandable concern where competition is being encouraged. However, effective separation has governed the onshore systems since BETTA and has delivered an effective onshore integrated transmission system.

The focus on competition could drive short term behaviours and risks the achievement of an effective, coordinated integrated offshore transmission system. Ofgem must consider whether the focus on competition will achieve effective offshore integration as the cooperation of interested parties is essential to achieve anticipatory investment, shared risk and long term perspective.

3. How effective are the current arrangements in representing all GB transmission entities' interests within ENTSO-E?

The current TO - SO model in the UK for onshore transmission system ownership and operation is effective and has been endorsed by the recent European unbundling derogation. As noted previously, current European Code drafting does not seem to consider the GB regime and is at risk of placing responsibilities on TO's and OFTOs that can only be fulfilled by the NETSO currently. It is essential Ofgem do all they can to ensure the new codes align with our regulatory regime, or consider what changes will be required to allow TO's and OFTO's to operate as system operators for their assets.

In terms of our particular role as a member of ENTSO-E, we have tried to get the right balance between our representation, and allowing National Grid as the GB NETSO, to take a lead role for GB. We have recently had discussions at a senior level with National Grid to ensure that we provide the right level of representation to ENTSO-E, and for National Grid to provide appropriate communications back to us on relevant matters.

4. How material is the impact of these arrangements on representation of the GB transmission system developments in the TYNDP and other related European activities?

Please note our answer to 3.

5. How effective are the current business separation arrangements the transmission entities are subject to?

The current TO - SO model in the UK for onshore transmission system ownership and operation is effective and has been endorsed by the recent European unbundling derogation. Our model is more unbundled than the ITO model with critical market functions being kept entirely separate. It is governed by proven and effective licences, codes and procedures which ensure that independence is guaranteed and all users operate on a level-playing field.

6. How material is the impact of the current arrangements on efficient network development?

Effective separation has governed the onshore systems since BETTA and has delivered an effective onshore integrated transmission system. We have well-developed skills and expertise across both pre-construction and construction activities, as demonstrated by our strong track record for the cost-effective and timely delivery of essential system reinforcements.

In terms of our direct involvement in offshore both in terms of reinforcement/s to increase boundary capacity and to connect offshore wind developments, we believe that the current arrangements have not hindered connection timescales or cost. Our view is that in terms of the projects we are involved in, efficient network solution/s will be achieved which address both system and connection requirements. It should be possible to have regulatory arrangements what allow for our full participation without compromising ITPR objectives.

7. Where networks are increasingly integrated, are there other areas where the question of conflicts should be considered?

In the short to medium term the distinguishing factor between onshore TO's requirements offshore and parties directly involved in offshore wind development will be the capacity of the network requirements, with onshore TOs looking to maximise capacity through 600kV HVDC links.

Hence the distinguishing element, at least initially, is likely to be technical. In order to assess the full potential of integrated offshore transmission networks it will be necessary to understand both from a technology and timeframe basis how and when the offshore developer and offshore (and onshore) transmission infrastructure will interact.

It is acknowledged (TNEI Offshore Coordination report P7098-03-R3) that the building block for windfarm connections will either be a 220kV AC or a 320KV HVDC connections dependant on the distance to the shore. However transmission networks will always want to operate at the highest voltage possible to maximise capacity and minimise system losses. The Western HVDC link demonstrates that 600kV 2GW interconnection is possible within the pre 2020 time scale and it is highly likely that as we progress through the 2020's offshore windfarm connections will trend towards 600KV (or even higher).

More work and understanding is required with both the windfarm developer community and the TO's to ensure that there is a common understanding of the difficulties integrating offshore generation with offshore transmission reinforcement to ensure that both are optimised and that neither is disadvantaged by being forced to accept, for example, the voltage level of the other party.

8. Do you agree that these issues associated with multiple purpose projects should be considered? What is the impact of the issues you identify as relevant? In particular how do they affect multiple purpose projects?

We acknowledge that the issues listed in this open letter are relevant. Planning, regulatory and market arrangements need to allow for the involvement of all stakeholders.

9. Do the issues capture all the potential regulatory barriers? Are there any other issues to be considered in this area?

The issue of data sharing is a significant hurdle in the design and development of an offshore regime where new parties are becoming involved. Currently this works effectively onshore as each of the TO's has access to the GB system model to facilitate system design. A mechanism may need to be established to provide for the sharing of data to all parties responsible for transmission system design and construction.

In order to assess the full potential of integrated offshore transmission networks it is necessary to understand both from a technology and timeframe basis how and when the offshore developer and offshore (and onshore) transmission infrastructure will interact. Greater work and understanding is required with both the windfarm developer community and the TO's to ensure that there is a common understanding of the difficulties integrating offshore generation with offshore transmission reinforcement to ensure that both are optimised and that neither is disadvantaged by being forced to accept, for example, the voltage level of the other party.