

Transmission licensees,  
generators, suppliers, consumer  
groups and other interested  
parties

Date: 18<sup>th</sup> December 2013

Dear Stakeholder,

**Consultation on SP Transmission Ltd's opening asset value for the England-Scotland Interconnector – a Transmission Investment for Renewable Generation project**

SP Transmission Ltd ("SP") has completed construction works required to increase the capacity of the electricity transmission network on the England-Scotland border. This project is known as the "England-Scotland interconnector". The project qualifies for potential cost recovery under the Transmission Investment for Renewable Generation (TIRG) mechanism. This was put in place in 2004 to accommodate investment in the transmission system resulting from increased demand for connections from renewable generators. We have received all of the relevant reports from SP to enable us to consider and determine the opening asset value<sup>1</sup> for the project. This consultation sets out our initial views and invites comments from interested parties to inform our final determination.

Our initial view is that SP's expenditure on the England-Scotland interconnector met all of the necessary criteria for post construction allowances in 2010-11. This includes increasing the capability of the transmission network on the England-Scotland border to the level specified in SP's electricity transmission licence. Based on this, we propose an opening asset value of £76.7 million in 2009-10 prices<sup>2</sup>, subject to consideration of the responses from this consultation.

We invite responses to this consultation by 14<sup>th</sup> February 2014. Subject to consideration of the responses, we intend to publish a determination in March 2014.

**Background**

The England-Scotland interconnector is a Transmission Investment for Renewable Generation ("TIRG") project. We put the TIRG mechanism in place in 2004<sup>3</sup> to provide funding for transmission investment projects not forecast at the time the relevant price controls were set<sup>4</sup>. Each licensee was given expenditure allowances for specified transmission reinforcement projects.

The provisions governing SP's revenue allowances for TIRG projects, including the England-Scotland interconnector, are set out in Special Condition 3J of its electricity

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<sup>1</sup> This determines the revenue allowances for the five year incentive period under the TIRG mechanism.

<sup>2</sup> All values in this document are in 2009-10 prices unless otherwise stated.

<sup>3</sup> For more information on the TIRG final proposals, see: <https://www.ofgem.gov.uk/ofgem-publications/56481/9139-28804.pdf>

<sup>4</sup> The electricity transmission price control review preceding the TIRG final proposals was TPCR 3. This was undertaken in 1999 for SPTL and SHETL and in 2000 for National Grid Electricity.

transmission licence ("the TIRG condition"). Full details of the TIRG condition can be found in SP's transmission licence<sup>5</sup>. The TIRG final proposals and the published guidance note for the mechanism<sup>6</sup> provide further background on the intention behind the five year incentive period. This commences the year after the project is commissioned. The Transmission Operators ("TOs") can earn a return above costs incurred for a project during this five year period if they deliver the project for less than forecast costs. This provides an incentive for the TOs to deliver projects efficiently. At the end of this period, any cost savings are shared with consumers.

The England-Scotland interconnector works were designed to increase the capability of the boundary<sup>7</sup> between England and Scotland from 2200MW to 2800MW by upgrading both of the west and east coast circuits. The project was identified in the TIRG final proposals in 2004 as one of four that would be funded through the TIRG mechanism.

The project required works in the transmission areas of both National Grid Electricity Transmission plc and SP. Each party was responsible for the works within its own area with the works being carried out in a co-ordinated manner.

SP commenced its works for the England-Scotland interconnector in 2006. The scheme was completed and put into full service in 2010. On 21 January 2013, SP submitted its post construction technical and expenditure reports for the project to us. As required by the TIRG condition, the post construction expenditure report was accompanied by an independent auditor's statement. The post construction technical report was accompanied by a construction completion certificate from independent technical advisors. It set out the actual capability of the project and the extent to which this complied with the output measures set out in Schedule C of the TIRG conditions<sup>8</sup>.

### **Initial consideration of opening asset value**

The opening asset value for SP's revenue allowance to be determined by the Authority is described as "SAFTIRG" in the TIRG conditions.

The TIRG Condition sets out that we will have regard to the following in determining the term "SAFTIRG":

- "Whether the final aggregate transmission investment expenditure set out in the post construction expenditure report has been efficiently incurred;
- The extent to which the licensee has complied with the output measures specified in Schedule C of the TIRG condition for the transmission investment project under consideration;
- Whether an adjustment has been made to the average asset value for the transmission investment project during the construction period;
- Whether an adjustment has been made to the depreciation value for the transmission investment project during the construction period;
- Any other information the Authority considers to be relevant to the determination."

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<sup>5</sup> A copy of SPs licence can be found here: [<https://epr.ofgem.gov.uk/Document>]

<sup>6</sup> A copy of this guidance note can be found here: <https://www.ofgem.gov.uk/ofgem-publications/56420/12320-27505.pdf>

<sup>7</sup> Boundaries are used to split the transmission system into different areas in order to assess and report on system capability

<sup>8</sup> A copy of the post construction technical report accompanies this letter

In reaching our initial view of SAFTIRG in respect of the England-Scotland interconnector works carried out by SP, we have considered the following:

- The final aggregate transmission expenditure set out in the post construction expenditure report: The final aggregate expenditure incurred by SP is £79.0 million, compared to £86.6 million originally forecast. As the final expenditure is below the level originally forecast, our initial view is that the level of expenditure is appropriate to deliver the output measures.
- The post construction technical report submitted by SP: We note that the construction completion certificate states that SP have completed all construction activities necessary to fulfil its output measure obligations specified in Schedule C of the TIRG condition. The data gathered and technical review carried out by the independent technical advisor confirms that the output measures have been fully delivered for all elements of the England-Scotland interconnector works carried out by SP.
- No adjustment has been made to the average asset value or to the depreciation value during the construction period.
- We have reviewed all other relevant information, including the reports submitted to date by National Grid Electricity Transmission plc in respect of the completion of its works for the England-Scotland interconnector.

We have also considered the guidance note on the TIRG condition and the TIRG final proposals. These state that during the five year incentive period, the licensee will be able to recover an allowance based on the forecast opening asset value for each transmission investment project. Where a TO is able to deliver a project for less than the forecasted level of costs, this creates what is known as the incentive payment<sup>9</sup> in the TIRG final proposals. These cost savings are then shared with consumers at the end of the five-year incentive period.

### **Our initial views**

Having considered all the relevant information discussed above, our initial view is that all relevant criteria and requirements set out in the TIRG licence condition have been met. In particular we consider that SP achieved the output measures set out in Schedule C in 2010/11. In line with our policy, we therefore propose that the opening asset value for the project should be set equal to the forecast level of costs so that the benefits of delivering the project below the forecast are shared between SP and consumers.

Our initial view therefore is that the opening asset value (SAFTIRG) for the England-Scotland interconnector for the five year incentive period should be £76.702 million. This is the original forecast of the opening asset value set out in the TIRG condition.

This consultation does not consider the value of the revenue allowances after the end of the 5 year incentive period. We will determine these by 2015/16 in accordance with our policy for TIRG projects that allows recovery of efficiently incurred costs.

### **Next Steps**

We welcome views from any interested parties regarding the issues raised in this letter. We will use these to inform our determination of the opening asset value which, subject to consultation, we anticipate publishing in March. Unless marked confidential, all responses will be published by placing on our website [www.ofgem.gov.uk](http://www.ofgem.gov.uk).

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<sup>9</sup> The incentive payment is equal to the value of the allowances based on forecast opening asset value less the value of allowances based on actually incurred costs.

Respondents may request that their response is kept confidential<sup>10</sup>. Any respondent who wishes its response to remain confidential should clearly mark the response to that effect and give its reasons for confidentiality.

Any responses should be made in writing on or before 14 February 2014 to the following email: Catherine.Williams@ofgem.gov.uk.

If you have any questions regarding this letter, please contact Catherine Williams on 0141 341 3979 or at her email address above.

Yours faithfully,

Geoff Randall  
**Head of Networks Policy, Electricity Transmission**  
**For and on behalf of the Authority**

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<sup>10</sup> Ofgem shall respect such requests subject to any obligations to disclose information, for example, under the Freedom of Information Act 2000 or the Environmental Information Regulations 2004.