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Contact / Extension
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Dear James

Hinkley-Seabank – Consultation on Final Needs Case and potential delivery models

SP Distribution plc, SP Manweb plc, and SP Transmission plc. ("the network companies") are the "asset-owner companies" holding Scottish Power's regulated assets and distribution and transmission licences. Scottish Power operates along divisional lines, and together, the activities of these companies fall within the Energy Networks division "SP Energy Networks" (SPEN). This response is from SP Transmission plc (SPT) the onshore Transmission Owner (TO) for the South of Scotland. As a TO we must ensure that we develop an economic, efficient and coordinated onshore transmission system. We therefore welcome the opportunity to comment on this consultation.

SPT has nothing to fear from competitive process and potentially much to gain given our core skills and relative scale compared to other industry players. However, it should not be assumed competition will yield a better result compared to effectively regulated licencees delivering the investment. Recent experience for consumers with respect to the cost and delivery of smart meters serves to illustrate this. It is important to note a regulated solution may well ensure consumers continue to enjoy a cost effective solution and secure quality of service. It is worth remembering that Ofgem's GB model of incentive based regulation has yielded a 25% improvement in network reliability¹, dramatic improvement in customer service alongside a 17% reduction² in real terms in prices for the consumer.

It is therefore vital for Ofgem to ensure that the proposed alternative delivery models for introducing competition will deliver material net benefits for the consumer. Our view is that Ofgem have not sufficiently demonstrated the merits of applying the SPV or competitive proxy models and the project should continue to be developed under the established strategic wider work (SWW) process. The risk of implementing an alternative untried, untested and potential one-off regulatory framework, for assets that provide connection for critical national infrastructure of the significance and sensitivity of a nuclear power station is not justified by the scale or probability of any potential cost savings.

¹ <https://www.ofgem.gov.uk/press-releases/ofgem-requires-electricity-network-companies-deliver-more-less>

² <https://www.ofgem.gov.uk/publications-and-updates/david-gray-s-speech-utility-week-congress>

Notwithstanding our overall view, we also need to highlight certain issues regarding the proposals for both delivery models being consulted on. We have therefore provided responses to each of the questions set out in the consultation in the attached Appendix.

In respect to the needs case submission itself we agree with Ofgem's view that that HPC connecting to the transmission system creates a need for investment in transmission infrastructure in the South West and that connecting HPC using an additional 400kV double circuit is appropriate.

Yours sincerely,



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Appendix 1: Response to Questions

Chapter 1: Regulatory framework for Hinkley-Seabank and other similar projects

Question 1: Do you agree with our initial views on the appropriateness of the new, separable and high value criteria for the SPV and Competition Proxy models?

Response: SPT agree with Ofgem's view that all the criteria for competition would need to be applied when considering whether to apply the SPV model, but that both the 'separability' criterion and the 'new' criterion, is not required for the Competition Proxy model. This is one justification for the Competition Proxy model being a more suitable framework than the SPV

Question 2: Do you think the criteria for identifying projects suitable for delivery through models intended to secure the benefits of competition should be the same, irrespective of which delivery model is used?.

Response: SPT does not consider alternative delivery models for introducing competition should be applied without an assessment to demonstrate this would deliver material consumer benefits over existing arrangements. Implementing an alternative model could undermine the status of the CATO regime as the enduring solution, if Ofgem intend to continue with this option.

Chapter 2: SWW Final Needs Case assessment

Question 3: Do you agree that there is a technical need for the HHSB project and that the proposed connection is compliant with SQSS requirements? If not, please give evidence.

Response: SPT agrees with Ofgem's view that that HPC connecting to the transmission system creates a need for investment in transmission infrastructure in the South West and that connecting HPC using an additional 400kV double circuit is appropriate.

Question 4: Do you agree with our initial conclusions?

Response: In general SPT agrees with Ofgem's initial conclusions.

Question 5: Are there any additional factors that we should consider as part of our SWW Final Needs Case assessment?

Response: SPT suggests that the use of alternative visual mitigation factors instead of undergrounding should be considered.

Chapter 3: Assessment of suitability for competition and potential delivery models

Question 6: Do you agree with our assessment of HSB against the criteria for competition, including our view on potentially re-packaging the project so that it meets all the criteria?

Response: In principle SPT agrees the criteria for competition developed for the CATO regime is appropriate to apply the project as Ofgem propose.

Question 7: Do you agree that the SPV model or Competition Proxy model would deliver a more favourable outcome for consumers relative to the existing status quo SWW delivery arrangements under RIIO?

Response: SPT does not agree with Ofgem's view that consumers will benefit from these delivery arrangements compared to RIIO. Although it is possible that a lower cost of capital may be achieved, the risk of implementing an alternative untried, untested and potential one-off regulatory framework, for assets that provide connection for critical national infrastructure of the significance and sensitivity of a nuclear power station is not justified by the scale of the potential cost savings.

We note from the consultation that Ofgem accept, , that they haven't quantified the savings which this model is intended to provide. We also believe that licence modifications will be required to deliver both models and the detail of those licence modifications has not yet been provided.

Question 8: What are your thoughts on the SPV model, including:

- (a) The structure of the model and length of revenue term?
- (b) Should construction funding start during construction, or once it has completed?
- (c) The contractual and regulatory arrangements?
- (d) The identified benefits?
- (e) Any potential downsides or implementation risks?
- (f) Any other considerations?

Response: SPT consider the SPV Model is complex and would be difficult to implement. The proposals are very high level at this stage and in order to properly assess the model, SPT considers that the following key points should be addressed by Ofgem. The proposal for the SPV model is also very high level and there are a number of points of detail which need to be considered as follows:

- Tender exercise – it is not clear who will bear the responsibility for the tender exercise and compliance with the applicable procurement regulations. If NGET is to be responsible for the tender (and therefore responsible for compliance with the applicable procurement regulations) this will require further consideration.

We would expect provision to be made to keep NGET whole against any procurement challenge which arises from an Ofgem direction.

- Cost uncertainty – we understand that the “cutover” from NGET to the SPV will follow high level design and consenting, with the SPV carrying out the detailed design. We think this could be an issue for bidders and in particular could lead to cost uncertainty on the basis it will not be possible for fixed bids to be submitted given unknown risks. This could mean that the Invitation to Tender (ITT) stage does not result in fixed price bids or even in comparable bids.
- Funding – we assume that the SPV will need to be funded from multiple sources. As such, funders will likely require both step-in rights and security over the SPV’s revenue stream. Provisions for this should be considered for this model
- Payment start date – payment only after construction completion is likely to be difficult to achieve. Funders are likely to expect payment in advance of completion.
- Regulatory responsibility – we understand that NGET will retain overall responsibility and operational control for the SPV and the assets. As such, any acts or omissions by the SPV will be attributed to NGET. More detail on NGET’s recourse against the SPV is required.
- Risk allocation – although Ofgem’s starting point is that the SPV should bear as many risks as possible that NGET bears, we note that Ofgem also say that there are some “high impact/low probability” risks which should remain with the NGET TO or consumers. We consider that these risks should only sit with NGET if it is clear it can manage them. It would also be helpful if Ofgem could provide some examples of these “high impact/low probability” risks.
- Benefit sharing – how can NGET share in the benefits of the SPV in light of the it will retain
- Transfer of Section 37 Consent - there is an outstanding issue from the CATO consultations in relation to the differences in the planning regime in Scotland and the transferability of a Section 37 Consent. We note from the consultation that a Development Consent Order (DCO) can be transferred to a third party. In Scotland, consent under Section 37 of the Electricity Act 1989 (Section 37 Consent) is obtained rather than than a DCO. The transfer of a Section 37 Consent is largely untested. If the Section 37 Consent will require to be transferred to the SPV under the SPV model then primary legislation might be required before this model could be implemented in Scotland.

Question 9: What are your thoughts on the Competition Proxy model, including:

- (a) The structure of the model and length of revenue term?
- (b) Should construction funding start during construction, or once it has completed?
- (c) How we identify comparable benchmarks?
- (d) The identified benefits?
- (e) Any potential downsides or implementation

Response: SPT consider the Competition proxy model would be difficult to benchmark and identify a justifiable cost of capital. In forming an assessment of the competitive level of project cost, Ofgem will need to select appropriate comparators to ensure the project is deliverable which will be challenging to achieve.

For example, offshore transmission owners (OFTOs) bid for transmission connections post construction and therefore the associated cost of capital excludes construction risk. Using OFTOs as a proxy for cost of capital is therefore unlikely to be sufficient for a project involving the construction and commissioning of an onshore transmission asset, in addition to its operation and maintenance.