

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

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Date: 28th of March 2019

Dear Stakeholder,

Decision on Scottish Power Transmission Ltd.'s Output Measures Adjusting Event request and review of the Opening Asset Value for the South West Scotland Transmission Investment for Renewable Generation (TIRG) project.

The South West Scotland (SWS) renewables connection project is a multi-phase program of work to reinforce the network of Scottish Power Transmission Ltd. (SPT) in preparation for increased renewable generation.

The first phase of this project (Part A), further referred to as the SWS project, consists of the expansion of the existing grid substation at Coylton, a new substation at new Cumnock and a 400kV double circuit overhead line (OHL) from Coylton to the New Cumnock substation. This phase is funded through the TIRG Mechanism as set out in SPT's special licence condition 3J¹, which is outlined in Appendix A.

On January 25th 2019, we published a consultation² setting out our initial view on SPT's request for an Output Measures Adjusting Event (OMAE), the Opening Asset Value (OAV) for the post construction period and the options for addressing delayed delivery for the SWS project. This letter constitutes our final decision upon consideration of the consultation response. We received a single response to our consultation agreeing with our initial proposal.

We have decided to accept SPT's OMAE request to remove the Quad Booster at Tongland from the project scope. We have also determined that the OAV should equal the allowance set out in the TIRG Final Proposals³ published in December 2004, £42.55 million⁴. Further, due to delays in the project delivery, the post construction revenue allowances will be moved from a start date of 2015/16 to 2017/18. The general price control correction factor⁵ in SPT's licence will accordingly be applied to the gap between the adjusted revenue allowances and received allowances for the relevant years and a final correction will feed into the 2020/21 allowed revenue calculation.

¹ SPT Special Licence Conditions: <https://epr.ofgem.gov.uk/Content/Documents/SPTL%20-%20special%20conditions%20consolidated%20-%20Current%20Version.pdf>

² South West Scotland TIRG Consultation Letter: https://www.ofgem.gov.uk/system/files/docs/2019/01/sws_tirg_consultation_letter_final_2.pdf

³ TIRG Final Proposals: <https://www.ofgem.gov.uk/ofgem-publications/56481/9139-28804.pdf> Please note at this time the SWS project was referred to as 'Kendoo';

⁴ All revenues are stated in 2009/10 prices, unless stated otherwise.

⁵ SPT Special Conditions 3A Part E outlines the general price control corrections factor Kt Term.

Background and January Consultation

In 2017, following completion of the SWS project, SPT submitted the post construction reports accompanied by separate independent auditor statements as required by the TIRG licence condition 3J.10⁶. We have considered these reports and set out in our January consultation the following three key considerations for consultation:

1. Output Measures Adjusting Event

SPT submitted a request to remove an output from the project scope, namely the Quad Booster at Tongland Substation. We proposed to accept this OMAE request based on the view that a decision to install the Quad Booster would have increased the risk of asset stranding⁷. Our initial view was that SPT delivered the overall output that was required for the SWS project and for this reason we proposed to amend the output measures in Schedule C of the Special Licence Condition 3J to reflect that the Tongland Quad Booster was not required to be delivered.

2. The Opening Asset Value

The allowance determined in the TIRG Final Proposals for the SWS project was set to £42.55 million. The final expenditure was £43.7 million, indicating that there was a £1.15 million overspend against allowed expenditure, which includes the allowances for the Quad Booster.

In our consultation we outlined that this overspend, despite SPT undertaking a competitive tender process, was due to unforeseen increase in costs of the Overhead Line Works (OHL) against the original forecast. We noted that SPT entered multiple rounds of negotiation to minimise expenditure on the OHL works. Our initial view was that the costs have been efficiently incurred by SPT. Equally, we recognised, in our consultation, that this expenditure does not include delivery of the Quad Booster. Nevertheless, the decision not to deliver this output has mitigated any additional and unnecessary overspend. Our initial view was that on balance the outputs have effectively been achieved within the original allowances and therefore we proposed maintain the OAV at £42.55 million.

3. Delays in Delivery

Licensees delivering TIRG projects are initially funded based on the expected timescales of the project. The SWS outputs were delivered 16-months later than anticipated in the TIRG licence conditions, which we proposed to reflect as a two-year delay during the post construction period. This means that SPT's post construction revenue for the SWS project should start in 2017-18 rather than 2015-16 as set out in the current licence conditions.

In the past we have adopted one of two approaches in moving revenue allowances to reflect delays of outputs for TIRG projects. We took these two alternative options to consultation and asked stakeholders which in their view would be the most appropriate means through which to correct the revenues received early by SPT.

⁶ SPT Special Licence Conditions: <https://epr.ofgem.gov.uk/Content/Documents/SPTL%20-%20special%20conditions%20consolidated%20-%20Current%20Version.pdf>

⁷ SPT decided that the project did not require the Quad Booster to achieve the overall output, and had they delivered it the Quad Booster there was a risk of this asset not being utilised.

Option 1 would correct the revenues using the correction term that is applied through the general price control revenue model, whereas option 2 would apply the rate of return applicable to TIRG projects, which is a more penal adjustment.

We noted as part of our consultation that the delays in the SWS project were largely a result of their contractors going into liquidation and delays in obtaining planning consents. In addition, we recognised that the project was still operational during the delays, with SPT striving to comply with their licence obligations and continue construction works for the project. On that basis, our proposal was to favour option 1, which will restate incorrect historical allowances using the general price control revenue correction term.

Responses to the January Consultation

We received one response to our January Consultation which was from SPT. The response is non-confidential and is available on our website⁸.

SPT agreed with our initial view to accept the OMAE and remove the Quad booster from the project scope. Similarly, SPT accepted our proposal to maintain the OAV at £42.55 million on the basis that the project has met all of the criteria set out in the licence and has been delivered at an efficient cost.

SPT also agreed that the start of the post construction period should be shifted back to 2017/18 to reflect that the project was delivered 2 years late. SPT said that they consider option 1 to be the most appropriate approach in rectifying the allowances received two years early.

Reasons for the Authority's Determination and Next Steps

We recognise that SPT has agreed with all of our initial proposals in the consultation letter.

OMAE

Having carefully considered the information before us and the consultation response received, we are satisfied that the Quad Booster can be removed from the project scope. This letter constitutes notice for the purposes of 3J.12(e), and amends the Output Measures table for the SWS project in Schedule C to reflect the table in Appendix B.

OAV

Having reviewed the SWS project against the TIRG OAV assessment criteria, we have decided to maintain the OAV at £42.55 million. We have come to the view that on balance the costs incurred in the SWS project are efficient and in accordance with Special Licence Condition 3J.9. This will mean that the overspend of £1.15 million will not be shared with consumers during the post-construction period. We consider that the Regulated Asset Value Period – the 15-year period starting in 2022/23 - will be based on the total expenditure of the SWS project, £43.7 million, as per the TIRG Mechanism.

⁸ South West Scotland TIRG Consultation Letter:
https://www.ofgem.gov.uk/system/files/docs/2019/01/sws_tirg_consultation_letter- final_2.pdf

Delays

We have decided to apply Option 1 to correct the allowances received early by SPT. We recognise that the events that led to delays were largely due to planning consents and the circumstances of their contractor entering into liquidation. However, we note that during these delays, the project was still operational. We have also considered the delays in the SWS project in the context of other decisions that we have taken relating to delayed TIRG projects. Based on this review and noting the response that we have received to this consultation, it is our view that Option 1 is appropriate for this TIRG project and in keeping with our previous decisions specific to other TIRG projects.

Therefore, SPT will be required to complete the restatement of the historical allowed revenues⁹ for the SWS project as part of their annual submission for the year in July 2019. This will allow the correction factor to flow through to an adjustment to its 2020-21 revenue. We will validate that the adjustment has been made correctly as part of the November 2019 Annual Iteration Process (AIP) to ensure that the correct final adjustment feeds into the 2020/21 allowed revenue calculation.

Should you wish to discuss the issues raised in this document, please contact Eilidh Alexander at Eilidh.alexander@ofgem.gov.uk or on 0141 354 5453.

Yours Sincerely,

Min Zhu,
Deputy Director, Electricity Transmission

⁹ Within SPT's revenue reporting, the revenue adjustment will be applied specifically through the restatement of the average asset value during the efficiency period (*ETIRGC.it*) for the SWS project.

Appendix A- TIRG Mechanism

The TIRG mechanism¹⁰ was established in 2004 to fund transmission projects to connect renewable generation outside the price control process to minimise investment delays. It provides the three electricity TOs with expenditure allowances for specific transmission reinforcement projects. The various TIRG projects, including the SWS project, can be broken down into four distinct phases:

Pre-construction	Construction	Post-Construction period	Regulated Asset Value period
Period prior to construction.	Period of construction. The length of the construction period is set out in the Licence with an annual revenue allowance set for each year.	Period of 5 years which begins one year after output is delivered.	15-year period during which any savings are shared with consumers.

¹⁰ TIRG Final Proposals; <https://www.ofgem.gov.uk/ofgem-publications/56481/9139-28804.pdf>

Appendix B

The following amendments will be made to the Output Measures table in Schedule C of SPT's Special Licence Condition 3J.

Output Measures: South West Scotland

Project scope	Capability as at 31 March 2005			Forecast capability prior to construction start date			Forecast capability post construction		
	Circuit voltage (kV)	Winter rating (MVA)	Summer rating (MVA)	Circuit voltage (kV)	Winter rating (MVA)	Summer rating (MVA)	Circuit voltage (kV)	Winter rating (MVA)	Summer rating (MVA)
New Cumnock - Kilmarnock South	Circuit does not presently exist.			Circuit does not presently exist.			275	955	760
New Cumnock - Coylton	Circuit does not presently exist.			Circuit does not presently exist.			275	955	760
New Cumnock 275/132 'SGT1'	Circuit does not presently exist.			Circuit does not presently exist.			275/132	240	240
New Cumnock 275/132 'SGT2'	Circuit does not presently exist.			Circuit does not presently exist.			275/132	240	240
Fongland-Quad-Booster	132	90	90	132	90	90	132	190	190