Network Planning & Regulation

Network Price Controls
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Dear team

RIIO-2 Sector Specific Methodology Decision and further consultation - Electricity System Operator

SP Transmission plc (SPT) welcomes the opportunity to respond to this decision and consultation. As a GB onshore Transmission Owner, SPT has a strong relationship and engagement with the ESO to make our network available, allowing the ESO to balance the GB electricity system. We also provide key services in respect of network connections and investment planning. These arrangements are defined in the System Operator/Transmission Owner industry code (the "STC"). As we already submitted a detailed response, dated 5th July 2019 to the earlier consultation, on this occasion, rather than address each of the consultation questions, we have instead highlighted our views on some key aspects of the proposals below.

Decision on the ESO Funding Model for RIIO-T2

The decision to implement "model 1" as presented in the May consultation still leaves some questions unanswered. It also introduces some new proposals that could significantly impact our business as a Transmission Owner, as well as the GB energy system as a whole.

The proposed model 1 precludes an efficiency incentive on expenditure. The pass through approach, in principle, should reduce risk for the ESO but could impose higher costs on consumers, if costs escalate above forecast. The disallowance measures Ofgem have retained are common to networks companies but present a more significant risk to the ESO under this model. The efficiency incentive in place for other network companies, acts as a buffer to mitigate risk to both consumers and the network companies from the disallowance mechanism.

In contrast, the ESO are exposed to higher risk because they do not have a clear view of what will constitute inefficient costs and therefore could be subject to disallowance in any ex-post assessment. This could result in a more conservative approach to investment by the ESO which could limit the progress of the energy system's transition to support a net-zero economy.

We do not support the proposal that the ESO's revenue collection function could be more efficient if Transmission Owners bear TNUoS revenue collection risk, associated with the onshore transmission networks. This is a significant new consideration at this stage in the development of the ESO funding model. The scale of these charges is significant. The Ofgem consultation (para 3.49) indicates SPT would be exposed to 13% of overall TNUoS charges which are forecast at £2.8 billion for 2019/2020 presenting approximately £364 million of additional risk exposure to us.

If this proposal is to be progressed further, the Transmission Operators affected will have had no opportunity to build this considerable additional risk exposure into their RIIO-T2 business plans, which are due to be submitted in December of this year. The practical implications of adopting this role are also significant for network companies, not least the contractual requirements that would need to be established, which are currently precluded under BETTA arrangements.

Ofgem need to give time for any such change to be properly assessed, understood and implemented. As a potentially affected party, we would also expect a detailed consultation exercise to be undertaken by Ofgem with the ESO and affected network operators, before any final decision on this proposal is reached.

The incentives package for the ESO is not yet defined and the early thinking presented by Ofgem in this consultation (para 4.20) is fairly broad brush and process orientated, with no quantitative parameters incorporated. There is no clear view of the potential for outperformance that the ESO may have. This exacerbates the risk proposition for the ESO as there is limited ability for the ESO to balance off risk with reward. In the year 2018/19 under the existing incentive framework, which is unlikely to change significantly for RIIO-T2, the ESO was rewarded less then £1million. This would not give much scope to balance risk of any disallowance that could be applied.

It is possible that the solutions to the risk areas the ESO have laid out in Appendix 2 of the consultation could be mitigated by a strong and targeted incentive package.

Finally, in relation to the proposed incentives evaluation criteria, it appears there may be too much scope for subjective assessment by the Panel in the current approach. Incorporating a set of deterministic financial metrics to reduce the extent of the Panel's evaluation could be an improvement to current arrangements.

Yours sincerely

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