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Date

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Contact / Extension

David Boyland

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Dear Sai Wing,

Statutory consultation on proposal to modify the special conditions of the electricity licence held by SP Transmission plc ("SPT") to give effect to Ofgem's decision dated 28 February 2024 in respect of three SPT 2023 Medium Sized Investment Project ("MSIP") applications

This consultation response is from SPT, which holds the transmission licence for the south and central Scotland. SPT is part of SP Energy Networks (SPEN) and the wider Iberdrola group.

We welcome the opportunity to respond to Ofgem's current Statutory Consultation in relation to SPT's 2023 MSIP re-opener applications ("the Statutory Consultation"). We note that:

- In October 2023, Ofgem consulted on its assessment of SPT's three MSIP applications for Coalburn SGT4; Constraint Management Pathfinder (CMP) – extension of LEO and Overload Protection Scheme (OTS) Modifications and Wishaw-Eccles-Torness-Smeaton OTS (the "2023 SPT MSIP Application Consultation");
- SPT submitted a response to that consultation on 6 November 2023 (the "6 November SPT Response");
- Ofgem issued its decision<sup>1</sup> on 28 February 2024, which purported to take account of the points raised by SPT in the 6 November SPT Response (the "2023 SPT MSIP Application Decision"); and
- Ofgem's current Statutory Consultation is intended to reflect the 2023 SPT MSIP Application Decision.

We would like to take this opportunity to respond to several areas raised within the 2023 SPT MSIP Application Decision document, which are reflected within the proposals set out in the current

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<sup>1</sup> [Decision: Three SP Transmission's 2023 MSIP applications | Ofgem](#)

Statutory consultation. In our 6 November SPT consultation response we raised several issues which remain to be addressed by Ofgem.

### **Opex Escalator**

As outlined in the 6 November 2023 SPT response, and as communicated throughout our engagement with Ofgem on this matter, SPT maintains the view that Ofgem's proposed application of the Opex escalator (OE) represents an error and will result in underfunding across the portfolio of MSIP projects.

We welcome the introduction of Ofgem's proposed OE review mechanism to address this issue, but still have significant concerns with the mechanism's proposed parameters. We remain committed to working with Ofgem on the development of the OE review mechanism and looking forward to the reinstatement of OE closeout mechanism working groups, but reserve our rights to appeal under the Electricity Act 1989 should SPT consider the OE review mechanism is not fit for purpose.

### **Staged approach to MSIP application**

We retain our position, as set out in the 6 November SPT Response, regarding the need for a staged approach to assessment of MSIP applications and strongly urge Ofgem to reconsider retaining the staged approach to the applications.

As set out in our 6 November SPT Response, the approval of needs case and optioneering not only aids risk management but also enables more timely planning and consenting processes, which is crucial for project delivery as well as achieving Net Zero targets. We would welcome further engagement with Ofgem to fully explore their rationale of the adoption of the single stage approach which has not been outlined in the 2023 SPT MSIP Application Decision.

It should be noted that the ESO, within the code administrator consultation for STC CM094: Amendment to Bi-annual estimate provisions<sup>2</sup>, is seeking to allow TOs not to pass on costs associated with specific funded Transmission Reinforcement Works that have received Authority approval, meaning that Users would no longer require to securitise for the projects with needs case approval. Removing the staged application from the MSIP process will result in Users of applicable (HND related) MSIP projects having to securitise until the full application for MSIP is complete, despite the changes in the CM094.

### **Risk Allowance**

While the definition of the activities for contractor indirect costs has been clarified and more defined. We retain the view that application of a 7.5% cap for risk remains arbitrary and non-project specific. Even if the 7.5% did reflect the total average risk of RIIO-T2 baseline projects, it should be noted that the direct costs within RIIO-T2 baseline included defined contractor indirect costs within direct costs – excluding the contractor indirect costs prior to the application of the risk cap further diminishes the risk allowance. Hence, the statement included within the Ofgem's decision that *"it aligns with the position set out by us in RIIO-ET2 FDs"* is not entirely correct given the changes to the direct cost definition associated with treatment of contractor costs.

The application of the cap for risk allowance results in downward bias and fails to assess project specific evidence provided in the MSIP applications.

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<sup>2</sup> [CM094 - Amendment to Bi-annual estimate provisions | ESO \(nationalgrideso.com\)](#)

We would like to note that Figure 1 within Ofgem's decision document, which explains the relation between Totex Incentive Mechanism (TIM) and risk allowance, does not accurately reflect what TOs require risk allowance for and its relationship with TIM:

(i) the figure assumes that risk expenditure is overspend, meaning that the direct cost allowance would cover all efficient costs required for the project, however the funding request for direct costs includes only efficient certain costs with risk allowance covering costs which may materialise;

(ii) TIM is an incentive mechanism, deeming that risk allowance beyond 7.5% would result in consumers paying additional money with no benefit is misleading. The Totex allowance should be set to reflect efficient and justified costs, with TIM acting as an incentive mechanism for efficient costs where both TOs and consumers would benefit from further efficiencies.

### **Treatment of survey costs**

It is important to recognise that SPT has applied a generic meaning to the term of 'survey' for many years to describe a wide range of activities, and that the fundamental purpose of these activities has not changed. Survey activities are integral to the process to develop and deliver projects, ensuring electrical assets are installed in accordance with our quality standards and will perform their function safely and reliably for their design lives.

The amendments made to the RIGs in recent years – which have amended the definition of direct and indirect activities - may have caused some confusion in the use of the term "survey". It is our contention that the nature and function of an activity, rather than its title, should determine whether it is classified as direct or indirect costs. This is clearly illustrated in the current RIGs where, under the definition of Direct Activities, it is stated, "In addition, includes, for the purposes of flooding, site surveys and non-site-based costs."

In light of the above, it is not clear what rationale lies behind Ofgem's decision to disallow the costs associated with surveys and treat these as indirect costs. In the context of the works undertaken for specific project there will be a much clearer rationale for the assignment of different 'surveys' to direct or indirect activity (depending on the nature and function of the specific survey).

### **RIIO-T1 expenditure**

Where there is no mechanism in place to address the development of overarching projects within different price control periods, Ofgem should ensure that the total efficient project expenditure is funded.

SPT incurred initial costs within the RIIO-T1 period associated with Coalburn SGT4 and Wishaw-Smeaton-Torness-Eccles OTS, however these costs were disallowed despite not having an appropriate mechanism in place within the previous price control to fund the efficient costs associated with the development of MSIPs.

Please do not hesitate to contact me should you wish to discuss any of the points raised within this response.

Yours sincerely,

A handwritten signature in black ink, appearing to read "David Boyland".

David Boyland

**Head of Transmission Regulation & Policy** *(Acting)*