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Date
1st October 2024
Contact / Extension
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By email:

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Dear Sai Wing,

Consultation on the RIIO-2 Re-opener Applications 2024 Draft Determinations – Electricity Transmission

This consultation response is from SP Transmission (SPT), which holds the transmission licence for central and southern Scotland. SPT is part of SP Energy Networks (SPEN) and the wider Iberdrola group. We welcome the opportunity to respond to the draft determination on RIIO-2 Re-opener Applications 2024. Our response is in relation to draft determination to SPT's Medium Size Investment Project (MSIP) applications.

We welcome the draft view to approve both the needs case and optioneering, for both the Constraint Management – Modification of Anglo Scottish Operational Tripping Scheme (OTS) and SPT-RI-237 Enoch Hill Collector Substation and Associated 132kV Circuit.

Detailed below is our position with regards to the proposed funding adjustments in relation to Risk and Contingency Allowance, the classification of Closely Associated Indirects (CAI) and Opex Escalator application.

Risk and Contingency Allowance

As expressed previously¹, we retain our position that Ofgem's use of an average value cap on risk provision is arbitrary, non-project specific and fails to consider the evidence presented on each project. This does not reflect the RIIO-T2 framework and Final Determinations (FDs), thus undermining the certainty provided in the price control framework.

The principle of applying an arbitrary and non-project specific cap fails to consider the project-specific evidence and is not consistent with industry practice. This was a key conclusion of the independent review of Ofgem's risk and contingency methodology provided by SPT in response to the RIIO-T2 Draft Determination. While elements of the methodology were changed at FD, the use of a portfolio average cap remains. We again urge Ofgem to consider the independent report provided².

We would like to highlight that the derivation of the cap is significantly flawed. The FD states that a bespoke approach to risk and contingency costs was required and that this differs for each TO. Therefore, the use of a cross-TO average of 7.5% uses non-comparable costs and does not reflect the RIIO-T2 framework and FD. If a portfolio average cap is to be applied, it should be based on the SPT data only and be consistent with the RIIO-T2 FD.

¹ Consultation: 3 SPT 2023 MSIP applications | Ofgem, November 2023

² Report provided after RIIO-T2 Draft Determination, conducted by Arcadis, RIIO-T2: Investment Plan – Engineering Risk Review, September 2020

Furthermore, the costs which are used as the basis for the calculation of the cap i.e. RIIO-T2 Business Plan costs contained contractors' indirect costs. Therefore, applying the same percentage to costs which do not contain contractors' indirects, will systematically award inadequate funding to TOs and is inconsistent with the basis on which the cap percentage was calculated.

In summary, we do not agree with the use of a portfolio-average cap approach to risk. The analysis to arrive at the cap percentage incorrectly relies upon non-comparable data from other licensees. Furthermore, if Ofgem retains the percentage cap approach to risk, the cap percentage needs to be applied to the project costs including contractors' indirects, not the costs which exclude them.

Classification of Closely Associated Indirects (CAI)

As per section 3.61 and 3.64 of this consultation, Ofgem's draft determination position is to adjust the allowances by removing the CAI costs from the requested direct costs. Ofgem have categorised surveys, project management and detailed functional design as CAI activities.

We disagree with Ofgem's view that all surveys (with the exception of flood related surveys) should be classified as indirects. As such, in our submission, we distinguish between "Functional Design" Surveys and "Asset Specific Design" Surveys, including only the later. Based on the content and purpose stated in the relevant contracts, all the surveys included as "Asset Specific Design"³, involve site works and activities involving physical contact with transmission network infrastructure assets, thereby, in accordance with Ofgem's guidance, these should be recognised as a Direct Cost.

Opex Escalator (OE)

We maintain our position regarding OE application, as previously stated within MSIP consultation response⁴. We continue engagement with Ofgem regarding the change in OE application and proposal to introduce the OE review mechanism. We have provided our detailed views on the proposed OE review mechanism within the response to the initial policy consultation⁵.

We are looking forward to the reinstatement of the planned working groups and continued collaborative approach to further the development of OE review mechanism.

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

Yours sincerely,



David Boyland

Head of Transmission Regulation & Policy *(Acting)*

³ Asset Specific Design activities are those which the licensee does not have direct control over and the decisions on how to meet the specification in function design are for the manufacturer/contractor to determine.

⁴ Consultation: 3 SPT 2023 MSIP applications | Ofgem, November 2023

⁵ Initial Policy Consultation on Proposed Opex Escalator (OE) Review Mechanism | Ofgem, September 2024

Appendix 1 – Consultation Questions – Responses are in relation to SPT MSIP applications only

ET.Q1 Do you agree with our assessment of the needs case for the 2024 MSIPs?

We agree with Ofgem’s draft view to approve the needs case for both SPT 2024 MSIP applications: Constraint Management – Modification of Anglo-Scottish Operational Tripping Scheme (OTS) and for SPT-RI-237 Enoch Hill Collector Substation and Associated 132kV Circuit (Stage 2).

ET.Q2 Do you agree with our assessment of the preferred option for the 2024 MSIPs?

We agree with Ofgem’s draft view to approve the preferred option for both SPT 2024 MSIP applications: the Constraint Management – Modification of Anglo-Scottish Operational Tripping Scheme (OTS) and for SPT-RI-237 Enoch Hill Collector Substation and Associated 132kV Circuit (Stage 2).

ET.Q3 Do you agree with our assessment of the efficient costs of individual MSIPs?

Risk and Contingency Allowance

We retain the position that removal of £0.03m for SPT Constraint Management – Modification of Anglo-Scottish Operational Tripping Scheme (OTS) and £0.14m for SPT-RI-237 Enoch Hill Collector Substation and Associated 132kV Circuit (Stage 2) to reduce the risk allowance to 7.5% of the direct costs is inappropriate. SPT maintain the view that risk should be assessed on a project-by-project basis and as such we do not agree that the risk allowance for this project should be assigned at 7.5%, which we understand is based on the average across the RIIO-2 portfolio.

The principle of applying an arbitrary and non-project specific cap fails to consider the project-specific evidence and is not consistent with industry practice. This was a key conclusion of the independent review of Ofgem’s risk and contingency methodology provided by SPT in response to the RIIO-T2 Draft Determination. While elements of the methodology were changed at FD, the use of a portfolio average cap remains. We again urge Ofgem to consider the independent report provided⁶.

We would like to highlight that the derivation of the cap is significantly flawed. The FD states that a bespoke approach to risk and contingency costs was required and that this differs for each TO. Therefore, the use of a cross-TO average of 7.5% uses non-comparable costs and does not reflect the RIIO-T2 framework and FD. If a portfolio average cap is to be applied, it should be based on the SPT data only and be consistent with the RIIO-T2 FD.

Closely Associated Indirects (CAI)

As per section 3.61 and 3.64 of this consultation, Ofgem’s draft determination position is to adjust the project cost in SPT’s allowance by removing the CAI costs from the direct allowance requested. Ofgem have categorised surveys, project management and detailed functional design as CAI activities.

We disagree with Ofgem’s view that all surveys (with the exception of flood related surveys) should be classified as indirects. In our submission, we distinguish between “Functional Design” Surveys and “Asset Specific Design” Surveys, including only the later. Based on the content and purpose stated in the relevant contracts, all the surveys included as “Asset Specific Design”⁷, involve site works and activities involving physical contact with transmission network infrastructure assets, thereby, in accordance with Ofgem’s guidance, these should be recognised as a Direct Cost.

⁶ Report provided after RIIO-T2 Draft Determination, conducted by Arcadis, RIIO-T2: Investment Plan – Engineering Risk Review, September 2020

⁷ Asset Specific Design activities are those which the licensee does not have direct control over and the decisions on how to meet the specification in function design are for the manufacturer/contractor to determine.