

# **THE FORM OF TRANSMISSION OWNER REVENUE RESTRICTIONS AND CONSEQUENTIAL EFFECTS ON NGC'S REVENUE RESTRICTIONS**

## **SP TRANSMISSION RESPONSE**

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### **1 Introduction**

Thank you for the opportunity to comment on this consultation on the form of Transmission Owner revenue restrictions and consequential effects on NGC's revenue restrictions.

SP Transmission agrees that an important aspect of BETTA is the encouragement and reward of efficient behaviour between the transmission licensees and, in particular, between the GBSO and the Scottish TOs - SP Transmission and Scottish Hydro-Electric Transmission.

While incentivisation is a key part of the new arrangements, we would restate our view that the BETTA arrangements can only be fully evaluated when the complete package is comprehensively defined and available for assessment. Notwithstanding that, SP Transmission remains committed to working with DTI, Ofgem and the other Licensees to secure a satisfactory outcome for the entire Transmission sector. We are already supporting these objectives by committing considerable, and increasing, resources to expert groups to develop an efficient, low-cost TO-GBSO commercial and technical interface.

### **2 Timetable**

We note that Ofgem is also consulting on the extension of the existing price controls for the Scottish companies and is considering contingency measures to be implemented in the event that BETTA go-live is delayed beyond the planned date of 1 April 2005. We recognise that BETTA is being planned within a very uncertain environment but what is certain is that the existing price controls for the two Scottish companies was only intended to last until 31 March 2005 and key decisions need to be made well in advance of that date. We would therefore welcome the timely issue of relevant price control consultations.

### **3 Principles of TO incentives**

We agree with the statement in paragraph 6.3 that an ideal TO incentivisation arrangement would reward the GBSO and TO(s) for acting collectively in the same way that an integrated

TSO would have done in the same circumstances. We have three integrated TSOs in GB at present and we believe that customers are benefiting from the efficiencies brought about by combined system operations and asset ownership within the three licensed areas. However, by developing appropriate incentives we believe that splitting apart these functions within the Scottish companies will not bring about significant additional costs.

Our view is that we should not be trying to develop a perfectly defined solution. After all, as things stand just now the transmission sector manages with some imprecisely defined responsibilities and accountabilities and it must not be assumed that the rules in future, particularly in the early stages of BETTA, need to be exceptionally detailed.

Our principal aims for new incentive arrangements are that:

- Each company needs to know in advance how the mechanisms will be applied in order to reduce uncertainty in its decision making;
- Each company needs to be able to forecast the results of applying the rules easily and with confidence;
- Incentives should not compromise operational safety; and
- Security of supply must not be compromised.

We would therefore support the pragmatic approach taken in formulating these proposals for an initial incentive regime for BETTA go-live in April 2005. We agree with the conclusion of the discussion in paragraphs 6.7 and 6.8, that only the TOs' costs should be taken into account. That is the factor which would inform decisions in a combined TSO and that is the approach that would meet the initial criterion set out by Ofgem for an ideal TO incentivisation arrangement.

## **4 Proposed form of TO incentives**

### **4.1 Investment Planning**

SP Transmission has always held the view that the Scottish TOs should make the final investment decisions and accepts the accountability that goes along with that right. In doing so, we will welcome the views of the GBSO with respect to generation and demand backgrounds,

and strongly support the GBSO's right to challenge our decisions, but at the end of the day SP Transmission will be answerable to the Authority for its actions. That is the principle that has been accepted within the BETTA expert groups and is a principle which underpins the BETTA project, in draft licence conditions and also in SO/TO Code drafting. We have therefore considered the three approaches put forward in paragraphs 7.6 to 7.11 with that in mind.

We agree that adopting either of the first two options for investment planning incentive arrangements would be problematic. The first approach would require the development of a huge amount of data to analyse the costs and benefits to each party for each investment decision and would prove if not impossible as a task in itself, would certainly be impractical at this stage of the project. In any case, it would not be conducive to efficient decision making processes within the TO management. The second approach would undermine the role of planning standards which underpin the financing of the transmission sector. We envisage an important continuing role for these standards which have provided a high level of system security for customers.

We therefore endorse the third approach, which is consistent with current practice and is in keeping with the BETTA principles which have been adopted.

## **4.2 Outage Planning**

We agree with the key principle that the GBSO has the final say in granting an outage request. The plan agreed at Week 49 is therefore the GBSO's plan, albeit that it was produced from TO outage requests. Should the GBSO consider deviating from that baseline plan then we see it as essential that only by taking into account the actual cost of deviating can the GBSO decide efficiently whether or not the outage plan should be changed.

It is our understanding that the RPI-X incentive arrangements will continue. These arrangements incentivise the Scottish TOs to manage construction and maintenance outages in an efficient manner, creating cost reductions which are ultimately passed on to customers. As such, it would be unacceptable if a well developed plan was altered to the advantage of the GBSO but to the disadvantage of customers. Only by weighing up the costs and benefits can an efficient decision be arrived at.

We therefore support the proposal that the Scottish TOs should receive additional revenue if they incur additional costs as a result of the GBSO changing the agreed Week 49 plan. We would also support the proposal that TOs should be placed under an obligation to make declarations which accurately reflect reasonable and efficiently incurred costs. That would allow the GBSO to decide on the justification of an outage change.

Clearly the GBSO should be allowed to challenge any such costs. There will be an incentive on the TOs to declare a true estimate of costs in that doing otherwise will soon lead to disputes and Ofgem intervention. That is not in our interest.

We support the view that, rather than design a sophisticated incentive mechanism, the TOs should be subject to an obligation to use reasonable endeavours to comply with the outage plan.

#### **4.3 Transmission Switching**

We agree with the proposal in paragraph 7.31 that no additional incentives are required for the efficient switching following the GBSO's directions.

#### **4.4 Providing Transmission Services**

We anticipate that the Scottish TOs will continue to have an obligation to submit an annual report to the Authority which will provide details of the performance of the transmission system. That will allow the Authority to scrutinise the provision of transmission services. We believe that the provision of that report, along with the declaration of availability within the SO/TO Code, means that no further specific measures are required.

#### **4.5 New Connections**

SP Transmission has construction contracts in place at present which contain liquidated damages clauses for late completion of the works. These contracts are mostly fixed price contracts and we are therefore very used to accepting and managing construction and price risks associated with our new connections. We do of course pass on an appropriate amount of the construction risk to our contractors but we largely manage the price risk through market intelligence and careful analysis of tendered prices for previous contracts. Customers are still

required to bear some of the risk associated with planning permissions as these are largely outwith our control.

Since we, rather than the GBSO, are best placed to manage price and construction risks we take the view that the GBSO should be allowed to pass these risks on.

SP Transmission's LD arrangements are currently limited to the connections works. They operate as a percentage reduction on the contract price for each day/week that the connection is late. Under the CUSC customers are entitled to liquidated damages if the infrastructure works are late.

Slightly more problematic, as the paper points out, is the situation where one Licensee provides the connection and another is required to construct additional infrastructure. Should the connection works be complete but the customer's full capacity rights cannot be granted as the other Licensee has not completed the necessary infrastructure works the customer will feel entitled to claim liquidated damages from the GBSO.

Our view is that under BETTA any Licensee who is late to the programme in delivering infrastructure works should be liable for LDs. This of course is a new risk for the affected Licensee but our position is that risks should be allocated to the party best placed to manage that risk. A consequential difficulty is, of course, the calculation of the magnitude of the LDs. Should they be based on the connection price, the infrastructure cost or an arbitrary figure. Our view is that further discussion is required on this matter.

#### **4.6 New Connections as Excluded Services**

We agree that new connections should continue to be treated as excluded services. This can be managed through an offer of terms from the TO to GBSO to support an offer of terms from the GBSO to the customer.

This could lead to different payment arrangements between GBSO and the customer as compared to those between the TO and the GBSO. However, by harmonising the TO's offer of terms with the GBSO's offer to the customer we do not anticipate any difficulties.

Regarding the credit risk associated with new connectees, we do not see that this problem is any greater under BETTA arrangements and agree the Plug charging methodology diminishes the risk significantly.