

SONI Price Control 2020-2025

NIE Networks' Comments on Utility Regulator's Draft Determination of 6 July 2020

11 September 2020

1. Introduction

NIE Networks welcomes the opportunity to respond to the Utility Regulator's consultation on its draft determination in respect of SONI's price control for the period 2020-2025.

NIE Networks is the owner of the electricity transmission and distribution networks in Northern Ireland and the distribution network operator. NIE Networks is responsible for developing, constructing and maintaining the transmission network. In its separate role as electricity transmission system operator (TSO), SONI is responsible for operating and planning the transmission network in Northern Ireland. SONI is therefore an important stakeholder for NIE Networks, with our ability to work in cooperation with SONI critical to the efficient delivery of electricity transmission infrastructure projects in Northern Ireland.

NIE Networks is already working positively with SONI on a number of key strategic areas including:

- inputting to the Department for the Economy's development of Northern Ireland Energy Strategy, with a Joint Working Group established;
- progressing amendments to the Transmission Interface Arrangements to make our working arrangements more effective for customers and the electricity market;
- progressing a framework for greater TSO-DSO co-operation;
- preparing for the North South Interconnector;
- engaging through the Connections Innovation Working Group;

as well as very active and important day to day operational interactions.

Going forward, both SONI and NIE Networks will continue to have crucial roles in delivery of the future transition of the energy system in Northern Ireland as an enabler towards a low carbon economy. This will aim to build on the early achievement of Government's 2020 target of 40% of electricity generated from renewable sources. In common with the increasing drive towards a sustainable 'whole energy' future across the UK and European Union, the future energy transition in Northern Ireland will bring the potential for new market models for electricity system services and much greater electrification of heat and transport.

In this context, NIE Networks and SONI will increasingly need to work in partnership to deliver outcomes that meet future Northern Ireland electricity system needs, as well as coordinating day to day operation of the distribution and transmission systems respectively.

Therefore, NIE Networks considers it important that SONI's price control arrangements should support and enhance arrangements in Northern Ireland aimed at:

- the timely and efficient delivery of transmission infrastructure projects;
- the evolution to a low carbon economy; and
- the best outcomes for Northern Ireland customers and stakeholders.

Our detailed response to the consultation is set out below.

2. Strategic approach

- Whole system collaboration and engagement

NIE Networks welcomes the identification by the Utility Regulator of the strategic importance of whole system collaboration and engagement in the context of the energy transition. Along with SONI, NIE Networks has already been fully engaged with the Department for the Economy (DfE) in its consideration of NI Energy Policy and supports the need for an integrated whole systems approach to the energy transition in order to deliver good outcomes for customers and wider stakeholders.

The Utility Regulator correctly identifies¹ that SONI can play a leading role as a whole system co-ordinator and NIE Networks agrees that this will become increasingly important in the 2020-2025 period and should be supported by regulatory arrangements during this price control and beyond. In that context, NIE Networks will also play a leading whole system role as Distribution System Operator (DSO) going forward and will need to work in partnership with SONI to achieve the right outcomes for customers. It is therefore important that SONI works closely with NIE Networks in its role as Transmission Asset Owner (TAO) and DSO to ensure the most efficient whole system solutions are identified and delivered.

The Utility Regulator sees² value in SONI developing strategy on how it will further take a whole system perspective, its approach to digitalisation and its approach to engaging stakeholders; and has proposed³ that SONI develop this strategy through involving NIE Networks and other relevant parties. NIE Networks is happy to fully support this initiative and agrees that this should provide greater clarity for stakeholders of SONI's roles and responsibilities, build a common understanding of whole system impacts and synergies, as well as the processes by which SONI collaborates with third parties and NIE Networks.

- Supporting SONI to deliver system change

The Utility Regulator recognises⁴ the benefits that SONI's services have brought to customers to date and welcomes its ambition to move 'beyond the status quo'. NIE Networks agrees with these sentiments and as a key partner of NIE Networks, we welcome the Utility Regulator's commitment to support SONI in building on its existing service proposition.

¹ Paragraph 3.6

² Paragraph 4.19

³ Annex 2, section 4

⁴ Paragraph 3.7

The Utility Regulator sees⁵ value in providing SONI with clearer service expectations for the 2020-2025 price control, particularly to reflect whole system considerations. The Utility Regulator recognises⁶ that the SONI price control regulatory framework is currently under-developed in respect of performance incentives and proposes the introduction of a new 'evaluative performance framework' to encourage and incentivise good performance from SONI across a range of services and outcomes.

NIE Networks is generally supportive of the Utility Regulator providing a stronger role for incentives to deliver high quality service within its regulatory frameworks; and agrees that there is a need for clarity and accountability for service performance within SONI's price control framework recognising SONI's role and influence on whole system costs and in pursuance of the energy transition.

The Utility Regulator proposes⁷ that the determination of SONI's performance for the purpose of determining the annual financial reward or penalty will be based on regulatory assessment of a range of quantitative and qualitative evidence, rather than mechanistic application against prescribed performance metrics.

Whilst recognising the particular nature of SONI's service offerings and the uncertainties of the energy transition, NIE Networks in general considers it best for customers as well as best regulatory practice, that incentives are based where at all possible on quantifiable metrics and ex-ante targets in order to provide a clear understanding for all stakeholders of both service expectations and the assessment criteria and approach that will apply. On the contrary, a highly qualitative assessment process risks a reduced level of clarity and real incentive, as well as presenting the potential for a heavy administrative burden for both regulator and company which risks at least a partial, yet significant shift of focus by the parties on to the out-workings of the assessment process at the expense of focus on improving the service offerings themselves.

3. Proposal directly impacting NIE Networks

- **TUoS Revenue Collection**

The Utility Regulator proposes⁸ to change the licence arrangements that determine SONI's role in relation to TUoS revenue collection so that cash flow risk lies with NIE Networks rather than the current arrangements whereby this lies with SONI. This is proposed in order that customers no longer need to pay SONI a risk margin on TUoS revenue collection.

NIE Networks understands the concept behind the Utility Regulator's proposals but would like further details of how the Utility Regulator envisages this operating in practice. It is our view that any changes should not be implemented until detailed proposals are developed by the Utility Regulator in conjunction with the parties, and fully consulted upon. Furthermore, it will be impractical to make any changes until at the earliest, the tariff year commencing October 2021.

⁵ Paragraph 3.8

⁶ Paragraph 5.3

⁷ Paragraph 5.4

⁸ Paragraph 8.11, Table 10

SONI is currently responsible for the setting and recovery of TUoS charges from transmission network users, as well as the underpinning contractual arrangements with these users. It is our view that these responsibilities are fundamental to current electricity market arrangements and should not be changed. Rather, it is our assumption that the cash flow issue referred to by the Utility Regulator relates only to timing and forecasting variances between (i) the TUoS revenue actually invoiced by SONI to users on a monthly basis; and (ii) the fixed monthly transmission service charge (TSC) that SONI is contracted to pay NIE Networks. On that basis, NIE Networks is open to discussion as to how that TSC payment may be profiled differently to minimise the cash flow impacts on SONI, without changing the fundamental market and contractual responsibilities of our respective companies.

- Telecoms Assets

The Utility Regulator proposes⁹ transferring responsibilities for certain telecom costs from SONI to NIE Networks.

Firstly, SONI and NIE Networks currently share the costs of the Operational Telecoms Network (OTN). The Utility Regulator proposes that this cost should fall fully to NIE Networks from RP7 (April 2024) onwards, and highlights the potential need to review agreements including the Transmission Interface Arrangements in advance of this change. NIE Networks is content with this proposed change and the need to work with SONI to review/amend any associated agreements regarding future use of the OTN.

Secondly, SONI has requested allowances to undertake the capital replacement of certain telecoms assets during the 2020-2025 period which the Utility Regulator has disallowed, taking the view that any physical assets operating in the field (outside of Castlereagh and the secondary control room) should fall within the remit of NIE Networks as the transmission asset owner. The Utility Regulator proposes that NIE Networks should use the D5 licence mechanism to seek allowances for such projects that fall due in RP6.

NIE Networks is content with this proposal and welcomes the clarity of roles that this provides. We would however wish to explore further with the Utility Regulator and SONI the practical implications of this change in responsibilities, including any implications for employees and other change management issues that might arise, as well as considering what is reasonable in terms of setting a target date for its implementation.

4. Regulatory Approach

- Transition from RPI to CPIH and impact on the RAB

The Utility Regulator proposes¹⁰ moving from indexation of the SONI RAB using the RPI inflation measure to using the CPIH inflation measure.

The example outlined in Table 8 of Annex 8 does not consider the longer term implications a move from RPI to CPIH regulation will have on the company; one of the key issues being lower

⁹ Annex 6, paragraphs 10.24f

¹⁰ Paragraph 9.20

depreciation allowances due to a reduction in the uplift applied to the RAB each year, as CPIH has historically been lower than RPI. Any drop in the regulatory return percentage to be applied to the RAB will exacerbate the reduction in allowances further.

Consideration should also be given to the impact a move from RPI-X regulation to CPIH-X regulation would have on annual productivity and RPE assumptions.

- Uncontrollable Costs

The Utility Regulator proposes¹¹ an ex-ante allowance for some uncontrollable but predictable costs such as licence fees¹², which would have the effect of exposing SONI to a possible windfall gain or loss for cost items over which it has no control. Likewise, electricity customers would face the converse exposure. NIE Networks considers it best regulatory practice to provide allowances for uncontrollable costs on a pass-through basis.

- Pensions

Deficit repair

SONI had indicated the intention to repair its pension deficit over 5 years, however the Utility Regulator has proposed that a 10 year period is appropriate to minimise risk to customers.

NIE Networks notes that this proposal by the Utility Regulator is against a backdrop of recent Pension Regulator guidance that schemes with strong employer covenants should generally have recovery plan lengths which are significantly shorter than the median recovery plan which is 7 years.

Although we are currently unaware of the strength of SONI's employer covenant, the Utility Regulator does not explicitly appear to have taken the Pension Regulator's recent guidance into consideration. NIE Networks considers therefore that the Utility Regulator should clarify its position in this regard.

Administration costs

The Utility Regulator has stated that it would expect to see the defined benefit administration expenses in the actuarial valuation to be in line with the previous valuation, adjusted for inflation.

However NIE Networks would note that there may be factors other than inflation which may impact on administration expenses, including market rates for administrators/advisers.

¹¹ Paragraph 7.28

¹² As well as the membership costs of ENTSO-E13 and CORESO14

Specific comments

We have provided other more detailed comments on the draft determination in the table overleaf based on a paragraph by paragraph review of the consultation paper and its various annexes.

Specific Comments

Paragraph/ Reference	Issue identified or proposed by the Utility Regulator	NIE Networks' Comment
Main Paper Para 3.6	SONI can play a lead role as a whole system co-ordinator	It should be noted that NIE Networks will also play a lead role as DSO going forward and will need to work in equal partnership with SONI to achieve the right outcomes for customers.
Main Paper Figure 2	Design and procurement of system services	NIE Networks agrees that a cost-based procurement/dispatch approach for system services will be an important enabler of the energy transition. This will be an important facilitator of NIE Networks' active participation in the system services market, as outlined in our 'DSO Vision'.
Main Paper Para 4.18	Financial incentives for bringing forward innovation	NIE Networks agrees that incentivising innovation should be an important part of the regulatory framework. It should be noted that the deployment of innovative solutions on the transmission network will require considerable input from NIE Networks.
Main Paper Para 4.19	SONI to develop strategy on whole system approach	It should be noted that any such strategy would require NIE Networks input.
Main Paper Para 5.13	Defines four high-level service outcomes for SONI: decarbonisation, grid security, system-wide costs and SONI service quality.	NIE Networks agrees that these seem the appropriate service outcomes for SONI to focus on during the 2020-2025 period.
Main Paper Para 5.13	Grid security/reliable electricity supplies	It should be noted that reliability of grid infrastructure is the responsibility of NIE Networks.
Main Paper Figure 6	Costs incurred by SONI and other costs it influences	The manner in which the different cost elements are depicted in Figure 6 may be misleadingly, if presenting DUoS as the larger outer band is misinterpreted by the reader as meaning that DUoS is the largest cost element in energy prices.

Paragraph/ Reference	Issue identified or proposed by the Utility Regulator	NIE Networks' Comment
Annex 3 Para 2.22	We are concerned that in many key areas SONI is presuming that it is best placed to undertake certain service activity without any demonstrable justification and consideration. We have particular concerns that SONI should not necessarily be undertaking activity which potentially fits within the DSO and TAO roles and that the potential role of other 3rd parties is very limited.	It is important that SONI works closely with NIE Networks in its role as TAO and DSO to ensure the most efficient whole system solutions. Moreover, proper consideration should be given as to which party is best placed to implement strategies and solutions which potentially impact on or involve the distribution network, and NIE Networks' evolving DSO role.
Annex 3 Para 2.23	Migration to IP to support SCADA (F4)	There is a need to ensure that the telecoms network is developed in the most efficient way. While IP may be the 'direction of travel' there should be no duplication of effort with NIE Networks.
Annex 4 Para 2.9	Grid security/reliable electricity supplies	It should be noted that reliability of grid infrastructure is the responsibility of NIE Networks.
Annex 4 Table 3	Outline design & consenting	It should be noted that a close working relationship is needed with NIE Networks to develop outline design.
Annex 4 Table 5	System Minutes Lost (SML)	NIE Networks would be concerned that using SML as a performance metric could hinder NIE Networks' legitimate access to equipment for maintenance purposes.
Annex 4 Table 5	Network Project Handover	NIE Networks agrees that the value of this metric is uncertain, however there is value in measuring speed of service to ensure that projects are forthcoming to NIE Networks without undue delay.
Annex 4 Table 5	Infrastructure Delivery	NIE Networks agrees that this metric should not be applied. It should be noted that once SONI has gathered consents, NIE Networks is responsible for the delivery timelines.
Annex 4 Table 7	Reference to Network Development	It should be noted that NIE Networks is responsible for Transmission Network Development. SONI is responsible for Transmission Network Planning which should be the 'service outcome' that is referred to in Table 7 to ensure clarity for stakeholder review.
Annex 4 Table 7	Independent Expert	NIE Networks notes that the weighting for this service item appears high in comparison to the importance of other areas such as system operation.