

Northern Ireland Electricity Limited

Transmission and Distribution Price Controls

2012-2017

Final Determination

23 October 2012

APPENDIX H – FUND 3 CONSULTATION RESPONSES

- 1.1 Our consultation on the draft determination for the approvals methodology and criteria for Fund 3 closed on 27 September 2012. We received non confidential responses from the following organisations:
- | | |
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| Northern Ireland Renewables Industry Group (NIRIG) | 2 |
| Energia | 3 |
| Gaelectric | 3 |
| Renewable Energy Systems Limited | 4 |
| ESBI..... | 4 |
| SONI..... | 4 |
| NIE T&D | 5 |
- 1.2 In the pages overleaf we have summarised the principal points made in each of the responses, and our response in turn to each of these.

Comments from respondents other than NIE

In the section below we address the responses including NIE's.

| Ref | Organisation | Topic | Comment | Our response |
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| 1 | Northern Ireland Renewables Industry Group (NIRIG) | <i>Process.</i> | NIRIG recognises the need to ensure appropriate governance for a regulated business such as electricity transmission and distribution; however, the process as outlined is convoluted and has the potential to introduce significant additional delays into an already complex area. | Legislation and the licensing regime place duties on both UReg and NIE T&D. Any requests for funding must be made and analysed in the context of the legal framework. We will strive to ensure that we discharge our duties in a timely manner, while ensuring that we subject NIE T&D's request to an appropriate level of scrutiny to ensure best value for customers. |
| | | <i>Legal responsibility.</i> | NIRIG believes that, in considering the development of new infrastructure to facilitate renewable generation, NIAUR needs to give more weight to the legal imperatives placed on the UK government by the RES-E and IME3 Directives. | Our analyses will comply with the green book (http://www.dfpni.gov.uk/index/finance/eag.htm). The green book outlines the appraisal, evaluation, approval and management of policies, programmes and projects. This limits options being considered to those that comply with legislation. |
| | | <i>Strategic development.</i> | NIRIG believes that the consultation fails to recognise that grid development is a strategic process and that the sum of the whole will be greater than the contribution from any individual component. Justification for development on a piecemeal basis is difficult when set outside the context of an overall strategic framework. Furthermore, NIRIG believes that it is fundamentally incorrect to include two major projects (North/South interconnector and Coolkeeragh/Magherafelt refurbishment) within this process - while both benefit renewable generation, both would be necessary even if renewable development ceased immediately | At the time of writing, NIE T&D has not produced a strategy for network development. Until this is available, we are limited to assessing individual schemes. In the draft determination, we state our preference for considering as many schemes together as possible. We also note the statutory duty on NIE T&D to ensure that the network is developed and maintained in a coordinated manner. We disagree with the statement that it is 'fundamentally incorrect' to include two major projects within the fund 3 process. We are intending to include both North/ South interconnector and Coolkeeragh/ Magherafelt refurbishment projects within Fund 3. This |

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| | | | | allows approval once NIE T&D is able to provide the detailed costs and scope required. |
| | | <i>Best Practice.</i> | NIRIG does not believe that proposals as outlined represent best regulatory practice and would recommend that the decision-making framework for infrastructure development in Northern Ireland should include wider strategic and sustainability considerations, as well as a longer-term price control and greater use of monitoring, as opposed to approval processes | <p>We consider the process we are proposing will allow us to consider strategic and sustainability criteria in our analyses, and we will need to include them to be able to demonstrate compliance with our statutory duties.</p> <p>The current level of uncertainty around the need for investment of renewables and the timing of construction of these projects means that they cannot be included in the current price control. Fund 3 means that they do not have to wait RP6 for approval.</p> |
| | | Role of SONI. | NIRIG is of the view that the consultation paper has not taken into account the existing role of SONI in terms of auditing new grid development proposals. | We will work with NIE T&D and SONI to confirm roles and responsibilities. |
| | | Role of a Reporter and rate of return. | NIRIG has previously commented in some detail on the proposals to introduce a Reporter and to introduce a reduced rate of return for renewable generation infrastructure. We would wish to reiterate our concerns on both proposals as they apply to this consultation. | <p>In our final determination for RP5 we reviewed the WACC applicable to Fund 3 and can confirm that it is the same as that for Funds 1 and 2.</p> <p>We consider the reporter to be essential to ensure that network development is progressed in an efficient manner and that generators can be assured that the capacity is delivered in accordance with our approvals.</p> |
| 2 | Energia | general | This respondent wrote in support of NIRIGs' response | No further comments required |
| 3 | Gaelectric | general | This respondent wrote in support of NIRIGs' | No further comments required |

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| | | | response | |
| 4 | Renewable Energy Systems Limited | general | This respondent wrote in support of NIRIGs' response | No further comments required |
| 5 | ESBI | general | This respondent wrote in support of NIRIGs' response | No further comments required |
| 6 | SONI | | It is important however that this cost benefit framework can adapt to the current level of uncertainty in the evolution of the Northern Ireland network and Northern Ireland generation portfolio. | We will base our analyses on the NI "green book". The green book outlines the appraisal, evaluation, approval and management of policies, programmes and projects. This limits options being considered to those that comply with legislation. We will also undertake sensitivity analyses to cover uncertainty related to the assumptions made. We will undertake these sensitivity analyses based on the issues, concerns and assumptions made at the time the analyses are undertaken. |
| | | | SONI raised concerns about the fact that the planning and development roles are carried out by two parties in NI. The interaction between NIE T&D and SONI is determined by the TIA. If the framework as suggested by the Authority in this paper were to be implemented it would be incumbent upon the Authority to bring forward the necessary changes to the basic architecture of the arrangements to support it. | We accept the need to ensure that roles and responsibilities are clearly defined and that both parties have access to the information required to discharge their statutory and licence obligations. We will request a review of the TIA in this context. This will be done following the completion of the TSO certification process. |
| | | | SONI flagged that the assessment should be undertaken at a societal level. | We will base our analyses on the NI "green book" methodologies, and best regulatory practice, in accordance with our statutory duties. The green book outlines the appraisal, |

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| | | | | evaluation, approval and management of policies, programmes and projects. This limits options being considered to those that comply with legislation. |
| | | | As with all investment decisions the decision to build transmission infrastructure should be made with the best information available at the time. The framework as proposed appears to suggest that there will be an <i>ex post</i> assessment also to determine whether the events forecast have actually transpired and incentives and returns calibrated accordingly. It would appear to SONI that such an approach has the potential to increase risk and therefore also to increase the cost of capital for the regulated utility investing. | The assessment will be made against the incentives defined in the approval letter. These criteria will be related to physical outputs such as available capacity at a certain point in time. For the avoidance of doubt, they will not related to utilisation, as that is outside NIE T&D's control. |
| 7 | NIE T&D | | <p>It is not clear from the consultation paper whether the Utility Regulator is suggesting a review of the Planning Standards or whether it believes a different approach may be appropriate. It would be helpful if the Utility Regulator clarified this.</p> <p>The consultation paper states that NIE has started a review of Planning Standards in respect of transmission. Whilst NIE has initiated some work, this is not intended to be a review of all of the Transmission and Distribution Planning Standards or to reflect a fundamental change to the methodology currently adopted. The focus of this review is the security arrangements associated with the connection of new generation to the transmission system, including bulk supply point design requirements (e.g. single busbar</p> | We can confirm that we expect the Planning Standards to be reviewed. |

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| | | | versus double busbar). | |
| | | | The paper includes the statement that customers “should not pay for transmission assets before they are providing a benefit to them” (paragraph 2.15). This suggests that costs for any given project may not be allocated to the RAB until after its operational date. If this is indeed the intent, an appropriate alternative mechanism is required for the recovery of the funding costs that NIE will incur in the preceding period. This point requires clarification. In any case, it is not apparent why a different treatment should apply for transmission assets provided under the Fund 3 mechanism than for capital expenditure on other network assets. | <p>This statement related to the construction of assets before they are required for network operation. It relates mostly to the order of development.</p> <p>We can confirm that the treatment of assets during construction should be the same for all funds.</p> |
| | | | Whilst it is reasonable and beneficial to include the prospective costs of extended market constraints within the scheme assessment process, it is not reasonable to have incentivisation measures that require NIE to accept risks associated with the delivery of reduced constraint costs, since these are outside the control of NIE and may change significantly with the passage of time and a changing mix of generation and demand. | We will strive to ensure that we only incentivise aspects of the project that are substantially with NIE T&D's control. |
| | | | For the avoidance of doubt, as no provision for asset replacement of the Coolkeeragh to Magherafelt line was included elsewhere in the Utility Regulator's RP5 draft determination, NIE understands that the entire costs of the upgrade to the Coolkeeragh to Magherafelt line, whether driven by asset replacement or other investment drivers, are | We can confirm that the entire project is reallocated to Fund 3. This is to remove the cost risk associated with any increase in capacity on the line, and to ensure that this would not impact on resources available to the business as usual capex programme. |

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| | | | to be considered under the Fund 3 mechanism. | |
| | | | Once the project is approved, NIE would see its role is to implement the network development specified in the approval. On that basis, “specified functionality” would therefore be defined, for example, in terms of the network capacity or rating specified in the approval of the investment, as implemented through physical development of the network. | For the avoidance of doubt, specified functionality can only refer to physical characteristics of the assets being installed and the timing of that installation. Operation of the assets is not within NIE T&D’s control. |
| | | | Paragraph 2.19 also proposes that “costs beyond the ceiling price will only be considered if they could not have been reasonably foreseen by a competent network developer”. NIE does not consider this to be the appropriate criteria to apply because it could imply that NIE should bear the risk for cost increases beyond its reasonable control. For example, while the potential for delay in obtaining planning consent could be reasonably foreseen, its impact on cost could vary considerably due to events that are beyond NIE’s reasonable control. This would leave NIE exposed to potential uncontrollable cost increases exceeding the approved “ceiling price”. NIE has instead proposed that the Utility Regulator be kept fully apprised of pre-construction development progress, and that additional allowances will be sought if and when the circumstances prove them to be necessary and reasonable. | <p>We would encourage NIE T&D to improve its estimation of pre-construction costs to ensure that our Board has the full information available to it when approving pre-construction costs.</p> <p>We would expect similar standards of governance to apply to NIE T&D’s own board.</p> |
| | | | NIE does not consider renewables-driven investment is less risky than investment in other transmission and distribution assets and has set out its objections to a reduced WACC | As stated on our final determination, the same WACC will be applied to all 3 funds. |

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| | | | in Chapter 12 of its 19 July response to the RP5 draft determination. | |
| | | | This “cost report” is presumably to be prepared and submitted as part of the process for seeking construction approval, at which point the pre-construction outturn costs will be known and the construction costs will have been determined. However, the proposed timing of this report should be clarified by the Utility Regulator. | We can confirm that this cost report is required for construction approval purposes. |
| | | | NIE T&D has requested that the baseline allowance for preliminary development of schemes should be reviewed. The company has also asked if the “50% rule” for staff allocation applies to RP5. It seeks clarification that costs of staff who are also working on preliminary development of projects can be charged to pre-construction or construction activities if they work on these projects also. | We can confirm that NIE T&D can reallocate staff between preliminary development and other activities, however we would require the company to be able to demonstrate that preliminary activities are not being compromised and that there is no double payment. |
| | | | It will be crucial for the Utility Regulator to commit to a timely process with defined milestones for consideration and response to approval submissions, so that the approval process can operate efficiently and transparently. | We will work with NIE T&D to agree timescales for approvals. These will be discussed at future meetings of the Renewables Grid Liaison Group. |
| | | | Reference is made in paragraph 3.6 to cost benefit analysis: it is not clear whether it is proposed that this analysis be undertaken by the Utility Regulator or NIE. This should be made clear. NIE stated that it would be normal for delegation of authority for approval of projects of lower value to avoid the need for the Board to consider approval of every submission. | The cost benefit analysis will be undertaken by UReg, however we would also expect the board of NIE T&D to consider similar information to be able to demonstrate compliance with its statutory duties in accordance with good corporate governance. |
| | | | In circumstances where approval is not granted, NIE would like an assurance that it | We will share our analyses and reasoning with NIE T&D. |

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| | | | will be provided with adequate reasons for any such decisions made by the Utility Regulator. | |
| | | | <p>NIE does not believe it is appropriate that incentivisation should be based on outcomes that may vary because end-users or market participants do not make use of the asset in the way or to the extent that was initially envisaged. Such deliverables are outside NIE's control and therefore should not form part of the incentives associated with its development of the network. Rather, NIE's incentivisation should be established and measured by reference to the key deliverables that are more readily under NIE's control, which are principally the final cost and schedule for delivery of the specified network development project.</p> <p>It is NIE's view that the Utility Regulator's assessment of performance against incentives should follow immediately after construction is complete and all costs have been confirmed, with any incentive payment made as soon as practical thereafter.</p> <p>NIE notes that the consultation paper does not specify the process by which incentives or performance criteria are to be agreed. This requires clarification.</p> | <p>We will endeavour to ensure that the aspects of the project that we incentivise are within NIE T&D's control.</p> <p>We will assess the incentives after one year of operation to ensure that the full functionality has been delivered.</p> <p>The items to be delivered under each incentive will be specified in each approval.</p> |
| | | | NIE would request that the Utility Regulator considers the merits of including an appeals mechanism to help ensure the Fund 3 process is in line with transparent, consistent and accountable decision making. | We would consider our fund 3 processes to be subject to the same appeals processes as our non-price control decisions. |
| | | | Under paragraph 4.4, NIE would have | We will not introduce a limit of 40% |

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| | | | expected some reference to DETI's Strategic Energy Framework as a consideration in the Utility Regulator's assessment of need for network investment to support the connection of renewable generation. | renewables to our approvals process. |
| | | | NIE remains of the view that the Reporter is not required or appropriate and that the terms of reference for his work in respect of Fund 3 will only serve to increase costs and to reduce the overall efficiency of the process. | We consider the reporter to be essential to ensure that network development is progressed in an efficient manner and that generators can be assured that the capacity is delivered in accordance with our approvals. The presence of a reporter will also reduce regulatory risk for NIE T&D. |
| | | | It is therefore important to establish the principle that NIE shall not be obliged to proceed with construction and delivery of any given project without agreement of terms. | We accept this principle. |
| | | | For the avoidance of doubt, while outsourcing of these works may be required in many cases, NIE reserves the right to employ its own resources (including NIE Powerteam) when appropriate in carrying out construction works. NIE has set out its position in respect of NIE Powerteam in Chapter 3 of its 19 July response to the RP5 draft determination. | We note NIE T&D's concerns, however as Powerteam is separate legal entity; we would expect NIE T&D's board to require some sort of binding agreement between the two limited companies to ensure that the directors can produce the certificates required with respect to availability of resources under NIE T&D's licence. All procurement must comply with NIE T&D's licence and statutory duties. |
| | | | NIE proposes that the overall balance of risk and return should instead be a fundamental part of each construction assessment by the Utility Regulator, with each project being taken on its merits at the time. | We will work with NIE T&D to agree an appropriate method for assessing and allocating the risks associated with each project. |

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| | | | <p>Whilst NIE would expect to justify the nature and extent of any proposed “contingency” provision, we would suggest that it is unwise, impractical and inappropriate to require a prescriptive approach to the calculation of contingencies</p> <p>NIE T&D also raised concerns about the mechanisms that could be used to allocate risk to 3rd parties.</p> | |
| | | | <p>NIE acknowledges the Utility Regulator's need to understand what is referred to in paragraph 5.19 of the consultation paper as the "directly measureable financial costs and benefits" of a project and notes the statement (paragraph 5.21) that the Utility Regulator “expects [NIE] to have considered the impact on the wholesale market“ in any submission for approval of a project. However a requirement on NIE to consider the impact of network development on the wholesale market should not be regarded as falling within NIE's duty to ensure that the T&D system is efficient and economic.</p> | <p>We will work with NIE T&D and SONI to ensure that the TIA provides the company with sufficient information to ensure that it can comply with its statutory duties.</p> <p>NIE T&D have a legal obligation to ensure that the network is economic, efficient and coordinated. The consideration of the impact of the network on the wholesale costs to consumers is therefore a requirement in its decision making.</p> |
| | | | <p>NIE T&D raised the issue of information flows between itself and SONI with respect to wholesale market costs, and how these are not covered by the TIA at present.</p> | <p>We will request a review of this aspect of the TIA, following the TSO certification process.</p> |
| | | | <p>At present the process chart in Figure 1 indicates that non approval simply results in a “rerun” of the approval process. However, it should be incumbent on the Utility Regulator to define to NIE and SONI the basis upon which the approval submission needs to be modified to make it acceptable.</p> | <p>We will ensure that any non approval contains the reasons why the request has failed. The subsequent actions will be dependent on these reasons. Having an overall strategy for network development will help (e.g. Network 25).</p> |