

15 February 2012

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Dear Sir/ Madam

Electricity transmission charging: assessment of options for change

The Scottish Council for Development and Industry (SCDI) is an independent membership network that strengthens Scotland's competitiveness by influencing Government policies to encourage sustainable economic prosperity. The membership of SCDI includes businesses, trades unions, local authorities, educational institutions, the voluntary sector and faith groups.

SCDI welcomes the opportunity to comment on the options for change developed by Ofgem as part of 'Project Transmit'. Ofgem has taken forward this review in an open and transparent way, as was demonstrated by its presentation to and participation in the discussion at the meeting which SCDI organised with Highlands and Islands stakeholders on this consultation.

The impact of the existing charging methodology on investment in energy generation in Scotland, above all renewable energy, and, therefore, Scottish and UK energy policies and targets has, for many years, been a significant concern to SCDI. Evidence gathered from generators for the Scottish Government has proven that the high levels of transmission charging in Scotland are a disincentive to projects. As Ofgem stated when Project TransmiT was launched, the UK is facing an "unprecedented challenge as it moves to a low-carbon energy system and new kinds of generators such as wind and wave power stations have less flexibility on where they are sited."¹ The existing locational charging approach is not designed to take this into account, and, as they are further from demand centres, discourages investment in those areas with the most productive sources of and greatest development potential for renewable energy. The "status quo" approach to locational charging, therefore, works against the grain of the transition to a more balanced, diverse and decarbonised mix.

SCDI has been supportive of the socialisation of costs. We note that this is modelled by Ofgem to support delivery of the UK's renewable energy target one and a half years early. It is important to note that the UK also has legally binding climate change targets for 2050 and that the UK Committee on Climate Change identified decarbonisation of electricity by 2030 as the most economic path towards them. The value of the greater certainty which

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socialisation would deliver in relation to the 2020 renewable energy target and the impact on this 2030 pathway, along with potentially wider benefits to consumers, do not appear to have been modelled by Ofgem. However, SCDI accepts Ofgem's conclusion that, because the socialisation of costs would be harder to deliver and create further upheaval in the industry alongside Electricity Market Reforms, and future EU policy is uncertain, that improvements to the current regime, compressing the locational variations, are the appropriate direction.

SCDI welcomes the recommendation to charge renewable generation according to output rather than capacity which better reflects the costs variable generators impose on the need for transmission investment. We note that Ofgem's modelling suggests that for the same level of low carbon support, its proposed Improved Investment Cost Reflective Pricing would increase the probability of hitting the 2020 renewables target, relative to the status quo, by increasing the deployment of onshore wind in Scotland. SCDI supports a balanced energy mix in both Scotland and the UK. We have also been concerned that the current methodology has disincentivised replacement base load capacity in Scotland and, therefore, security of supply. These proposals go some way to addressing this issue for all generators in Scotland.

SCDI is concerned that the modelling shows steep increases in transmission charges from 2020 due to the impact of the HVDC reinforcement projects. In the consultation, Ofgem has asked for views and SCDI would support socialisation of the costs of their converter stations.

Islands

At the meeting which SCDI organised with Highlands and Islands stakeholders, we focussed on the significant concern about the high estimated charges for island generators under the new regime. This will impact on the development of the high capacity, low carbon energy resources on the islands and of the strategically important subsea grid infrastructure. The effect would be that the differential between northern mainland Scotland and the islands would be even greater, which would potentially disadvantage the islands for investment. With these the location of much of the UK's marine energy industry, this would not be aligned with Ofgem's recognition of the need to reflect the lack of flexibility for wave power stations.

SCDI does not believe that a Section 185 cap would provide a suitable and timely solution. It would take 2-3 years to legislate for and introduce, and then it would only adjust charges in location for 10 years when investments are based on a certainty of returns over 20 years. There was an agreement by the partners that a solution should be arrived at through the Project TransmiT process. This is a transmission issue which requires a transmission solution.

SCDI has had sight of the proposals by Highlands and Islands Enterprise (HIE) and the islands, and has been briefed on the proposal by Scottish Renewables. HIE's proposal involves the extension of volume based charging to the islands and the introduction of anticipatory change of the treatment of the interconnectors as part of the wider Main Interconnected Transmission System. This relatively straightforward improvement to Ofgem's proposal would have the effect of reducing charges to levels where they would not be a disincentive to projects. HIE has shown that, with 50% of the cost of the three subsea links socialised, this could save the consumer £1.5bn in subsidies for the equivalent generation from offshore wind. Indeed, HIE have calculated that the entire cost of the interconnectors could be socialised and consumers would pay less than for offshore wind.

We believe that the proposals from both HIE and Scottish Renewables are potentially practical and achievable, within Ofgem's objectives for Project TransmiT and the improved framework which Ofgem has recommended in the consultation. We welcomed Ofgem's commitment to Highlands and Islands stakeholders to consider positively proposed options and we look to Ofgem, DECC and National Grid for a constructive, clear and joined-up response to these proposals and their further development and agreement along with industry.

SCDI hopes that these comments are helpful and looks forward to Ofgem's response.

Yours sincerely

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