

Dear Stuart,

Ofgem Open Letter

Connecting the Scottish Islands- update (16 September 2008)

Introduction

Thank you for the opportunity to respond to your letter entitled "Connecting the Scottish Islands". The following are the views of Shetland Islands Council. These views should be read in conjunction with our response to the 'June 2007 open letter'. A copy of that response is attached.

Shetland Islands Council again welcomes Ofgem's ongoing, pro-active, contribution to seeking timely and cost effective transmission connections to Scotland's islands where the UK's renewable energy resources are at their most abundant.

SHETL advises that it is continuing its work in developing a transmission connection to Shetland in response to connection offers made by National Grid. That work has proceeded through initial design, survey and consultation work to a now advanced set of technical proposals. It is our understanding that SHETL will issue an invitation to tender to HVDC technology suppliers during November 2008. This should mean that the provision of a Shetland connection is subjected to a competitive supply process, albeit limited by the small number of potential suppliers within the market place. That competitive supply process is also set against a background of heavy worldwide demand for HVDC technology.

The following was stated in our response to the 'June 2007 open letter': "SHETL argues that it will deliver a cost effective, timeous connection to Shetland for the current applications by means of: a single circuit (through a relaxation of licenced security standards); HVDC Light technology; following the shortest subsea route, which allows the most cost effective point of connection on the Scottish mainland; following the most cost effective onshore connection routes at both ends; and use of the S.185 "cap" to bring island transmission charges down to an economic level. This assumes that the currently flawed NGET TNUoS methodology is amended to deliver a TNUoS tariff that is cost-reflective of the investment to provide the connection".

SHETL's current proposals should be scrutinised by Ofgem to judge their cost effectiveness. Any regulatory approach, beyond the current regulatory framework, must be capable of demonstrably reducing capital costs (and thus TNUoS charges) within existing timescales. A S.36 application for consent is expected to be submitted for Shetland's Viking Windfarm in January 2009. Whilst it is acknowledged the S.36 submission date has slipped considerably, there is now a clear expectation that this new date will be met.

SHETL expect to submit applications for consent(s) on a Shetland transmission connection in March 2009. It is expected that investment decisions on the Viking Windfarm project and on the transmission connection will need to be made in 2010. Key to those investment decisions will be a S.36 consent for the Shetland windfarm being obtained and clarity on transmission charges and grid access being achieved. Charging uncertainty remains an ongoing barrier to entry for island projects. Efforts, elsewhere, to obtain a fairer and more transparent transmission charging regime will continue.

Since our response to the 'June 2007 open letter,' the Government has conducted some further work on the S.185 "capping" power. This work is, in our opinion, seriously and fundamentally flawed and the Government has been made fully aware of our concerns. It remains Shetland Islands Council's position that a S.185 scheme should be developed and implemented by the Government to ensure that consented renewables projects in the islands can proceed.

#### Uncertainty

Shetland Islands Council welcomes Ofgem's 'September 2008 letter' and any specific work on a transmission connection to Shetland which seeks to break down the barrier to entry created by ongoing uncertainty and volatility in TNUoS charging predictions.

Concern needs to be expressed that investment in a transmission connection to Shetland potentially falls outwith the territorial scope of SHETL's (or another provider's) licence. We look forward to being kept up to date with progress on the consideration of the associated legal issues and solutions. Concern also needs to be expressed at the timing of the uncovering of this anomaly, with consents processes for island generation and transmission assets now fast approaching and consequent investment decision dates now fast approaching.

#### The Transmission Price Control Review (TPCR)

With both the Viking Windfarm proposal and SHETL's development proposals for a transmission connection to Shetland both close to submitting applications for consent, the biggest remaining hurdle (beyond planning) is the ongoing regulatory and transmission charging uncertainty.

Ofgem should examine SHETL's proposals for a Shetland connection, in detail, with a view to including that proposal in SHETL's agreed price control. To repeat a competitive approach, beyond the price control, should only be contemplated if it can see a Shetland connection delivered by 2013 and at reduced cost. We note that Ofgem states that such an alternative approach would represent "... a significant risk to the timely completion of the proposed connections to the Western Isles and Shetland". It is Shetland Islands Council's expectation that any such delay would prove fatal to existing island generation proposals.

#### Conclusion

The Scottish islands have this country's best renewable energy resources. Large scale, planning consented, projects should shortly be in a position to harness that resource for the benefit of the country as a whole, and for the benefit of electricity consumers. It is in everyone's interests to connect these rich sources of indigenous, secure, carbon-free and sustainable power as quickly and as cost effectively as possible. If mandatory renewable energy targets are to be achieved by 2020 then the islands must be allowed to make their significant contribution.

Regulation and transmission charging uncertainty represent a continuing barrier to entry to island projects. It is also worth restating our view that existing transmission regulation and charging methodology are at odds with European law, both existing and proposed. The January 2008 draft EU Directive

on renewable energy states that the costs of connecting new producers of electricity from renewable sources should be objective, transparent and non-discriminatory.

The issue of the territorial extent of legislative prohibition and transmission licences needs to be quickly closed down.

Realistically if transmission connected generation projects in Scotland's islands are to be achieved, prior to 2020, then SHETL's request for price control funding for its proposed connection to Shetland would need to be delivered under the existing regulatory framework. Shetland Islands Council looks forward to the speedy development and implementation of relevant incentives to enable this to happen. Consideration should be given to funding a Shetland connection via the European Investment Bank with any, cost of capital, benefits being translated into reduced TNUoS charges.

Within the existing regulatory process, there needs to be better communication between Ofgem and SHETL and clear pro-active scrutiny by Ofgem of all elements of SHETL's connection proposals in ensuring value for money.

Against the background of ongoing cost escalations and volatility there needs to be an additional backstop provided by a carefully developed, and implemented, S.185 "capping" measure from the Government to provide the required clarity and investor confidence which will finally enable ambitious island projects to proceed.

We look forward to the delivery of an affordable working connection to Shetland by 2013 and thereafter Shetland will become the country's top performing renewable energy asset.

Shetland Islands Council  
October 2008.