



Highlands and Islands Enterprise
Iomairt na Gàidhealtachd 's nan Eilean

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25/09/2009

Dear Ms. Fletcher

Response to Ofgem initial proposals for the Fifth Electricity Distribution Price Control Review (DPCR5)

Highlands and Islands Enterprise (HIE) along with its local partners, the democratically elected local authorities covering the north of Scotland; Shetland Islands Council, Orkney Islands Council, Comhairle nan Eilean Siar, Highland Council, Argyll and Bute Council and Moray Council, would be pleased for you to consider these comments on your initial proposals for the fifth distribution price control review (DPCR5) and your updated revenue allowances published on 21 September 2009.

The Highlands and Islands are home to world-class natural resources and valuable know-how required for the development and deployment of renewable energy technologies. HIE sees the careful exploitation of these resources as key to the future environmental, social and economic sustainability of the region as well as making valuable contributions to binding Scottish, UK and European carbon reduction targets.

Deployment of renewables technologies in Scotland is dependent on grid capacity to accept its output. The highly constrained nature of Scotland's electricity networks has led to the development of some ground-breaking solutions: these include the Registered Power Zone (RPZ) on Orkney, and research into hydrogen as a practical energy carrier in Shetland and the Outer Hebrides. HIE and its partners are proud of these developments and very keen to see further such schemes grow and develop in the region.

HIE notes that the general tone of the initial proposals is of Ofgem's support for transforming the distribution networks – both in providing for the physical infrastructure to connect new renewables generation and in incentivising the DNOs to explore and apply the smarter grid concepts. HIE commends this emphasis.

We cannot at this stage come to a firm view on whether the settlement that Ofgem is proposing is adequate to support DNOs in their crucial role for achieving a sustainable energy future. The details of the settlement are quite complex and lengthy, and in any event we note that at this stage it is a process of negotiation. However we do have some comments relevant to the framework and nature of the settlement, which we hope can be translated into the final details, as follows:

Provision for new infrastructure

HIE anticipates the need for new infrastructure investment at distribution level over the next five years, to accommodate a substantive increase in distributed generation. This includes for instance a probable rapid increase in small-scale projects responding to the UK Governments proposed new 2010 feed-in tariff; ongoing developments in both commercial and community-scale onshore wind; and marine projects in the Pentland Firth and Orkney waters and elsewhere.

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We appreciate the difficulty in predicting the volume and timing of these developments, and note Ofgem's proposals around flexibility and smoothing costs over longer time-frames to keep some stability for customer charges. HIE and Scottish Government along with other stakeholders, have been exploring options for marshalling grid applications to give the network companies some co-ordinated visibility of connections - work on this for the Crown-Estate leasing process for the Pentland Firth and Orkney waters is ongoing, and we would be pleased to speak to Ofgem about this work.

HIE believes that it is important that incentives on the DNOs strike the balance between appropriate reward and value for money. We note some anecdotal concerns we have heard on the reduction in the monetary incentive to connect distributed generation, (and the actual reduction of the distributed generation incentive) and hope that Ofgem and the DNOs can reach a realistic outcome on this.

Incentivising innovative or smart solutions

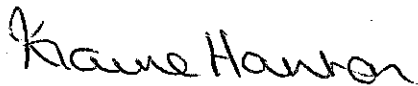
We are concerned that in such a fast-changing landscape for the DNOs, a fixed-in-stone five year settlement is too prescriptive, even with some flexibility and re-openers built in. We would support for instance moves to allow non-regulated income for new and innovative business ideas, and the opportunity for DNOs to pitch for discretionary regulated amounts throughout (as well as in advance of) the price control period.

Generally, in the fifth price control period, we support DNOs being rewarded for being dynamic and willing to push the confines of what is presently a very risk-averse business model - where this has the potential to contribute to green energy targets and aspirations.

HIE supports the provision made for the Low Carbon Networks fund and would be happy to share our views on project selection in our area.

I hope you find these comments useful and if I can provide clarity on any of the points raised, please don't hesitate to contact me. I look forward to viewing outcomes in due course.

Yours Sincerely



Elaine Hanton
Joint Head of Energy
Highlands and Islands Enterprise

In conjunction with
Shetland Islands Council
Orkney Islands Council
Comhairle nan Eilean Siar
Highland Council
Argyll and Bute Council
Moray Council