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Dear Colleague,

**NOTIFICATION UNDER SPECIAL CONDITION J3 PARAGRAPH 6(C) - EXTENSION
OF THE DEADLINE FOR NOTIFICATION OF A TIRG ASSET VALUE ADJUSTING
EVENT FOR TRANSMISSION INVESTMENT PROJECT BEAULY-DENNY IN RESPECT
OF TIRG RELEVANT YEARS $T=1$ to $T=N$**

Introduction

The Beauly-Denny transmission line is a major reinforcement running from northern to central Scotland, and was funded by Ofgem through the Transmission Investment for Renewable Generation (TIRG) mechanism in December 2004. However, the project has been subject to a planning inquiry, and has only recently received consent from the Scottish Government to proceed, subject to a number of key consent conditions. When Ofgem approved funding for Beauly-Denny, it set out in the transmission licence the anticipated spend for the project from $t=0$ - being the first year of construction - to $t=n$, the last year of construction.

As a consequence of the Scottish Government's decision, SHETL intends to change the profile of spend in the construction period, and will conduct a significant amount of consenting work in the first construction year, $t=0$. SHETL will not know what changes will need to be made to the funding in the licence for the second year of construction onward, $t=1$ to $t=n$, until it has completed this consenting work in the first year of construction. However, the provisions of the transmission licence in Special Condition J3, paragraph 6(c)¹ specify that if the licensee considers an Asset Value Adjusting Event has occurred, or is expected to occur, it must provide the Authority with a notice for the full construction period, in advance. SHETL considers that it will not be able to finalise the overall scope of works, and hence capital cost for years $t=1$ to $t=n$, of the Beauly-Denny project until it undertakes the work necessary to satisfy the key conditions of consent. It has therefore asked the Authority to agree to submit this information at a later date than stipulated in the licence. SHETL has asked the Authority to agree to a submission date of 31 December 2010 for this information.

¹ Which can be found at Ofgem's electronic public register at:
http://epr.ofgem.gov.uk/document_fetch.php?documentid=14832

SHETL argues that if it were to wait to undertake all of the work to satisfy the consent conditions, such that the construction programme and forecast cost were known before commencing construction, it considers there would be a delay to the completion of the project until 2015.

Annex 1 provides more background to the Beaulieu-Denny project. Annex 2 sets out in more detail the relevant provisions of the transmission licence.

The Authority's notification

The Authority takes the view that it is in network users' and consumers' best interests to allow SHETL an extension to submit updated cost information for Beaulieu-Denny once consenting works have been completed. As a result, and in accordance with the provisions of Special Condition J3, paragraph 6(c), the Authority agrees to extend the timetable to permit SHETL to submit a TIRG asset value adjusting event notice for $t=1$ to $t=n$ by 31 December 2010.

If you have any queries in relation to the issues raised in this letter, please feel free to contact David Hunt on 020 7901 7429 or via email at david.hunt@ofgem.gov.uk.

Yours sincerely,

Hannah Nixon

Partner - Transmission and RPI-X@20

For and on behalf of the Authority

Annex1 – Further information on the Beaully-Denny project

Special Condition J3 of SHETL's Electricity Transmission Licence sets out restrictions in relation to the revenue allowances associated with Transmission Investment for Renewable Generation (TIRG). The TIRG mechanism provides funding to connect a large volume of renewable generation that was not forecast at the time that the relevant price controls were set for the transmission licensees. TIRG provides explicit revenue allowances and associated output measures (in Schedule C: "Supplementary provisions to Special Condition J3" in the transmission licences) for each of the transmission projects covered by the mechanism.

When funding for TIRG was approved in December 2004, it was based on project-specific allowances for four discrete reinforcements². We recognised, however, given the inherently uncertain volume and nature of the new connections that it was appropriate to provide funding allowances that could be amended subject to Authority approval, in case the allowed TIRG revenue proved inadequate.

On 28 September 2005, SHETL applied for planning consent to install a double circuit 400 kV overhead transmission line from Beaully to Denny. The new line would replace an existing 132 kV line: one circuit to operate at 400 kV to provide a high capacity circuit between Beaully and Denny and the other circuit to operate at 275 kV to provide a circuit into which much of the generation in the area between Beaully and Denny could be connected.

The Beaully-Denny line passes through a number of cultural and historical sites and, due to strong local opposition, became subject to a planning inquiry. After two years of deliberation, the inquiry reporters submitted their final report to the Scottish Government on 19 February 2009.

After consideration of the report, the Scottish Government granted consent to the project on 06 January 2010 with conditions imposed in relation to mitigation of the visual and environmental impact of the transmission line. Moreover, Scottish Ministers considered that the terms of the consent could be varied every six months in order to meet unanticipated issues that may arise.

In order to meet the Scottish Ministers' conditions of consent, SHETL has adopted a two-fold approach to avoid further delays on the Beaully-Denny project. Consequently, SHETL has requested a TIRG average asset value adjusting event in respect of TIRG relevant year $t = 0$ (2010-11) and a later date for notification of a TIRG average asset value adjusting event in respect of TIRG relevant years $t=1$ to $t=n$. Indeed, SHETL is not able to finalise the overall scope of works, and hence capital cost, of the Beaully-Denny project until it has undertaken the work necessary to satisfy the key consent conditions.

² Several other projects were not considered to be sufficiently certain at the time of TIRG for funding to be approved.

Annex 2 - Relevant licence provisions

The following paragraphs summarise the licence provisions in relation to asset value adjusting events.

Asset value adjusting events

Special Condition J3 of SHETL's Transmission Licence sets out the provisions in relation to asset value adjusting events. A 'TIRG asset value adjusting event' means relevant additional preconstruction works or a relevant amendment to the scope of construction works that the Authority is satisfied is expected to cause costs and/or expenses to be incurred (or saved) in relation to a specific transmission investment project. Under the provisions of Special Condition J3, paragraph 6(c), the licensee shall give notice to the Authority, as soon as is reasonably practicable after the event has occurred, confirming that it considers an event has taken place which has materially increased (or decreased), or is expected to materially increase (or decrease), the costs of the licensee. However, the Authority has the power to allow the licensee to submit its notice at a later date.

When submitting a notice of an asset value adjusting event, the licensee must detail the particulars required by the licence including how it considers the costs have been efficiently incurred, and must confirm that they cannot be recovered under the existing TIRG revenue allowance. Following consideration of the notice and supporting documentation, the Authority shall determine whether such an event has occurred and determine what the asset value adjustment ($AFFTIRG_t^i$) should be. The Authority can determine the adjustment to be either the amount requested by the licensee, or a different amount, at its discretion. The depreciation calculation for the relevant project will be affected by any adjustment to the asset value, such that the associated depreciation term ($AFFTIRGDepn_t^i$) would also need to be adjusted via a determination by the Authority.