Highlands and Islands Enterprise
Iomairt na Gàidhealtachd 's nan Eilean

alena.fielding@ofgem.gov.uk

22 February 2018

Dear Alena

CONSULTATION ON PRINCIPLES TO BE CONSIDERED WHEN RECOVERING THE COSTS OF PROVIDING 'FLEXIBLE CONNECTIONS'

Thank you for the opportunity to respond to the above. Given the potential impact of the proposed changes we welcome the decision from Ofgem to consult.

HIE along with its local partners - the democratically elected local authorities covering the north of Scotland and the islands; Shetland Islands Council, Orkney Islands Council, Comhairle nan Eilean Siar, The Highland Council and Argyll & Bute Council, make representations to key participants on behalf of industry to influence the way in which regulation of the energy industry is managed in order to ensure the needs and interests of the Highlands and Islands are understood and taken into consideration. HIE also works closely with Scottish Government in relation to regulatory matters.

The Scottish Highlands and the Islands off the north and west coast represent a large geographical region. The region has a low population density with many pockets of population spread across areas that are often remote. The region is home to a large volume of renewable energy power stations – from small scale, local developments to very large commercial installations. There are many more sites across the region that could be exploited to provide yet more cost effective, low carbon, renewable energy. The distribution network in the region is owned by Scottish Hydro Electric Power Distribution.

Our region has been exposed to network constraints in one form or another for many years. This has led to early network innovation occurring in the region – including the Orkney ANM scheme and the NINES project – both examples progressed by SSEN. These projects have helped to facilitate greater penetration of renewable energy than would have otherwise been possible by simply using normal network investment approaches. As trailblazing projects, such as the Orkney ANM scheme, lots of industry leaning has been gleaned from the experiences of both the DNOs and generators. However, network access across the region is still extremely difficult as much of the distribution system is heavily utilised and subscribed with contracted generation. Similarly, transmission system constraints have affected generation across the region for many, many years. For a long time, these constraints have stopped or stalled all but the very smallest domestic installations from progressing. Generation in the region is also exposed to very high network use of system costs, as a function of the current locational charging arrangements, which has a significant impact on the business case and route to market for many renewable projects in the region.

We welcome the pro-active approach that has been taken by SSEN to ensure that there is an ongoing route for funding ANM schemes and other types of flexible connection. We believe that the continued timely delivery of these types of scheme is extremely important for delivering greater penetration of low carbon, renewable generation technologies in the highlands and islands region. However, we have a number of concerns relating to the proposals that have been submitted by SSEN.

Evidence to support proposed change in methodology

We would welcome further evidence to support the SSEN proposals. In particular, we would like to understand what the scale of impact of the different options for charging for these schemes would be. The evidence presented as part of the consultation does not provide a clear, objective analysis of the issue – considering the cost impact of all the options in relation to spend expected over the remainder of the RIIO-ED1 period. Therefore, we would encourage SSEN to undertake such a piece before moving forward with this change in charging methodology. Further, we similarly consider that the impact of these proposals on connecting customers needs further substantiation and analysis.

Timing of proposals

We are concerned that these proposals will presuppose the outcomes of the Open Networks and in particular the Charging Futures work. Therefore, we think that delaying such significant changes to the charging statement should be considered.

Alternative funding models for ANM

Nonetheless, we think that this funding issue should not delay the implementation of flexible connection schemes which are critical to ensuring that more renewables can be connected so that the energy system continues to deliver low cost, low carbon energy to UK consumers. Therefore, we consider that some form of letter of comfort from Ofgem to the DNOs, or interim funding arrangements should be put in place to cover the costs of these schemes which are developed ahead of there being clarity on future charging arrangements, currently being developed through the access and charging task forces under the Charging Futures Forum.

Classification of costs relating to 'flexible connections'

The evidence provided by SSEN does not clearly set out why the running costs for ANM schemes should be treated separately to normal network operational costs.

We believe that better network measurement and control is going to become a critical aspect of distribution network operation in the future. Particularly in the context of DSO – where better data management will likely be used to deliver more efficient use of existing and future network assets. ANM schemes are effectively a set of network measurement, analysis and control protocols to allow more energy to use the network infrastructure for more of the time. Therefore, we do not understand the rationale or justification for passing ANM operational costs onto specific customers given that this is likely to be a fundamental part of DNO functional business models moving forward. Particularly in the context of the 'DSO' models being discussed as part of the Open Networks project.

Interpretation of the 'Minimum Scheme'
We disagree with the interpretation that all ANM schemes and 'flexible connections' cannot be deemed the 'minimum scheme'. The term 'minimum scheme' suggests the lowest cost connection solution overall. Through the Open Networks project, the DNOs are proposing to develop a functional business model which depends on greater network data collection and more active network management to reduce need for traditional network reinforcement. Therefore, there must be an expectation that actively managing the network will reduce connection costs for customers. However, if all ANM schemes are deemed above and beyond the minimum scheme design (hence not lowest cost), then these types of schemes cannot possibly reduce costs for customers in the long term. This position seems quite contradictory.

Apportionment of costs of 'flexible connections'
We are concerned that passing the operation and maintenance costs directly onto connecting customers rather than as part of the DNO's overall regulatory settlement will not provide appropriate incentives to ensure optimal levels of service for ANM schemes and flexible connections.

The model presented does not expose the DNO to penalties or incentives against the performance of the ANM scheme – i.e. no level of service guarantees. All the risk is placed on the connecting customers. For example, the reliability of telecoms arrangements, control equipment, etc.

Further, the model does not reflect the fact that flexible connection schemes facilitate more connections, more networks users, and therefore a larger customer base for the DNOs.

Other change proposals
We note that there are several other change proposals that do not relate to flexible connections. In particular, the proposed changes to paragraphs 6.30 and 6.32 – aligning O&M charges (for assets beyond the minimum scheme) for generation and demand and removing the detail of the O&M charge percentage.

We support the simplification of charging arrangements – this is important to help a wider stakeholder group engage in the industry. However, we are concerned that this will result in higher charges overall. Therefore, we would like to encourage SSEN to publish further information about how the proposed changes will affect the overall revenue collection from each customer group compared to the current methodology.

We are also concerned about the forecast O&M estimates. It is not clear how the estimated O&M estimates have been derived as there is no analysis or justification for the proposed figures. Therefore, we recommend that Ofgem should request substantiation from SSEN of these estimates. Further, it is not clear how the 25 year period, over which the capitalised O&M charge is charged, has been determined.

We hope these comments are useful.

Yours sincerely

Elaine Hanton
Head of Energy: Emerging Technologies and Regulation

In partnership with:-
Shetland Islands Council
Orkney Islands Council
Comhairle nan Eilean Siar
The Highland Council
Argyll & Bute Council