

Greenlink Interconnector Limited,  
electricity interconnector  
licensees, and other interested  
parties

Direct Dial: 020 3263 9825

Email: [cap.floor@ofgem.gov.uk](mailto:cap.floor@ofgem.gov.uk)

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Dear stakeholders,

### **Preliminary cap and floor levels for the Greenlink interconnector to Ireland**

In May 2020, we published a decision to enable project finance solutions for two cap and floor projects, Greenlink and NeuConnect. The project developers requested changes to our cap and floor regime to broaden the sources of financing available for them to progress their projects through construction.<sup>1</sup>

One of the changes we approved was to set the floor level based on either of the two alternative approaches below:

- **Approach 1:** Notional approach using *UK Non-financial iBoxx BBB 10+ years* as the relevant debt index with everything else remaining the same as in the default regime (such as paying the notional cost of debt on 100% of the Regulated Asset Value (RAV)); or
- **Approach 2:** Market-based approach using an actual cost of debt and gearing that result from a competitive debt raising process, and introducing a mechanism for developers to repay consumers any extra cost over *Approach 1* if the overall cost under *Approach 2* is higher. This floor level is set to allow repayment of debt only, and shareholders are not allowed to recover invested equity or a return on it at the floor level set based on *Approach 2* (Actual Floor Level).

Our 2020 decision give developers the option to choose between approaches 1 and 2 above. Special Condition 3, paragraph 3 of the Greenlink Interconnector Limited (GIL) licence allows GIL to notify us of its elected approach within 10 days after financial close.

### **Final Project Assessment (FPA) decision for Greenlink**

In March 2021, we consulted on the efficient costs for the Greenlink interconnector.<sup>2</sup> In October 2021, we set the GB share of Greenlink's development and capital costs at

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<sup>1</sup> [Decision on proposed changes to our electricity interconnector cap and floor regime to enable project finance solutions](#)

<sup>2</sup> [Consultation on the Final Project Assessment of the Greenlink interconnector to Ireland](#)

£217.6m.<sup>3</sup> We noted that these costs would be converted into preliminary cap and floor levels based on financial parameters agreed between the developer GIL and lenders at financial close with Ofgem overseeing the process.

### **Debt financing process and financing parameters**

We summarise our oversight of the process undertaken by GIL to secure debt finance, leading to financial close on 15 March 2022. Our oversight process was designed to protect consumer interests while not unduly delaying the delivery of the interconnector. Our oversight covered four key areas:

- **Market sounding process** – this covered the approach taken by GIL to test market appetite for the project, including both commercial and non-commercial lenders. GIL provided key risks and characteristics of the transaction to potential lenders. The number of commercial lenders approached (more than 50 banks and institutional investors) provided a good sample of the market. We consider that the type and identity of the commercial lenders approached by GIL is consistent with those seen on recent Offshore Transmission Owner (OFTO) transactions.

Based on an analysis of the market sounding feedback, GIL decided to pursue a bank financed option, rather than using institutional investors. This decision was based on institutional investors providing a higher indicative all-in cost on both the GBP and EUR tranches of debt. The slightly longer tenor debt proposed by the institutional investors when compared to the banks, was potentially not sufficient to compensate for the higher cost given the regime length for GIL. This assessment by GIL and its financial advisor appears reasonable.

- **Market launch process** – this stage involved the sharing of more information on the project with a selected group of potential lenders. This covered the Information Memorandum (IM), a financial model (FM), a long form termsheet or draft Facility Agreement (FA), and due diligence reports prepared by lenders' advisors – including technical, insurance, revenue etc. The IM and audited FM prepared by GIL and its financial advisor are comprehensive and typical for a transaction of this type. As part of the package, GIL provided guidance on pricing at a level below that proposed by a number of banks invited to the market launch. It further indicated that a pricing competition would be run if more banks than required achieved credit approval. This approach by GIL and its financial advisor appears reasonable.
- **Credit response process** - Greenlink received responses and provided a summary of the responses to Ofgem. A majority of commercial banks included in the market launch responded positively – with a number of banks reducing their pricing from that at market sounding and many coming in below the guide pricing. Total commitments were approximately twice the funding requirement. While GIL had previously indicated it would run a pricing competition if there were more banks than required at this stage, instead it proposed to set consensus pricing lower than the guide pricing and asked 8 banks from the original list to align with this pricing. While a pricing competition (reducing margins step-by-step until only those banks that are left are needed to meet the funding requirement) may have driven

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<sup>3</sup> [Decision on the Final Project Assessment of the Greenlink interconnector to Ireland](#)

somewhat lower pricing, the concern to include within the group banks those that could provide the necessary hedging and fill the required roles is understandable.

- **Financial close process** - carried the risk that the consumer benefit established by the debt competition could be eroded. GIL shared the financial close protocol and financial agreements for Ofgem's review. GIL also led a number of trial runs to ensure that the live financial close process would go as smoothly as possible. Ofgem also participated in the final financial close process.

### **Our view on the GIL debt raise process**

We consider the process followed by GIL in selecting commercial banks to have been appropriate for a transaction of this kind, especially when considering the first-of-a-kind nature. A wide range of potential funders were approached with appropriate levels of information, in a structured manner, which may be expected to drive competitive pricing behaviour. GIL selected the final banking group based on pricing and extra considerations such as ability to get credit approval within required timeline. These considerations were deemed relevant to a successful financing process.

We consider that the absence of non-commercial lenders such as the European Investment Bank (EIB), who may have been able to reduce the all-in cost of debt to the project, led to slightly higher overall costs. GIL also considered Export Credit Agencies (ECAs).

We understand that the timeline set out by GIL to secure the project's cable manufacturing slot, in order to reduce the potential for further project delays, required formally involving the ECAs and EIB earlier in the process than GIL did. As such, project timing was a factor in determining the involvement of such institutions. There was scope for GIL to better consider the internal approval processes followed by such institutions and how this would align with the overall project delivery timeline.

Overall, we consider that the trade-off between potential delays to the project delivery timeline to wait for the non-commercial lenders and the potential reduction in the all-in financing costs was reasonable considering the transaction size. Whilst we note above that the cost of debt might have been marginally lower, we consider that the final financing costs are reasonable and that a competitive process has led to a good market outcome.

### **Preliminary Cap and Floor (Notional and Actual) levels**

The financial parameters for the Greenlink project have been confirmed following the conclusion of the debt raise process. This includes the actual gearing, debt and coverage ratio which underpin our calculation of the actual floor level for the Greenlink project.

We have updated the Greenlink Cap and Floor Financial Model (GCFFM1) published alongside our June 2021 decision<sup>4</sup> to generate the preliminary cap, notional floor and actual floor levels for the Greenlink project. The values are based on project costs we approved at FPA and financial parameters determined at financial close.<sup>5</sup>

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<sup>4</sup> [Decision on changes to the electricity interconnector licence held by Greenlink Interconnector Limited \(GIL\) and the electricity interconnector licence held by NeuConnect Britain Limited \(NBL\) | Ofgem](#)

<sup>5</sup> Inputs underpinning the actual floor level in the GCFFM1 are different from the corresponding inputs in the GIL project finance model. The GCFFM1 inputs have been selected to ensure that the actual floor level it generates matches the actual cost of debt floor level generated in the GIL project finance model as have been agreed with lenders to the Greenlink project.

**Our Preliminary Cap Level for the Greenlink interconnector is £31.24 million and Preliminary Notional Floor Level is £15.58 million; and Preliminary Actual Floor Level is £18.60 million<sup>6</sup> (in 2020/21 prices).**

The updated GCFFM1 and model handbook (CFFMH1-ACOD) are published alongside this decision.

Following conclusion of its debt raise process and financial close on 15 March 2022, GIL notified Ofgem on 21 March 2022 of its election to use Approach 2 (as set out on page 1 of this decision document) to set the floor level for the Greenlink project. In line with Approach 2, consumers will top up revenues to the Actual Floor Level when necessary. GIL will need to repay the difference between any floor payments based on Approach 2 and potential floor payments based on Approach 1 before shareholders can take any equity returns or dividends from the project. To be clear, we note that borrowing by shareholders or equivalent that may seem like a workaround for the restrictions on equity distributions or dividends payment will not be allowed.

If you have any questions in relation to this letter please contact Aliabbas Bhamani by email ([Aliabbas.Bhamani@ofgem.gov.uk](mailto:Aliabbas.Bhamani@ofgem.gov.uk)).

Yours sincerely,



**Stuart Borland**

**Deputy Director, Offshore Network Regulation**

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<sup>6</sup> We note that the Preliminary Actual Floor Level for GIL is divided into two components: 1) a component based on the operating costs, replacement capex, decommissioning costs and tax elements - this component will be indexed annually by outturn UK RPI inflation rates; and a component based on the debt service and the debt service cover ratio - this component will be indexed at a pre-specified RPI fixed rates schedule to ensure that it remains fixed for the entirety of the regime.