

George Cobb
Head of OFTO Regime
Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

20 September 2022

Dear George,

Offshore Transmission Owner (OFTO) End of Tender Revenue Stream – 2nd Policy Development Consultation

I am writing to you on behalf of Transmission Capital Partners (“TCP”) in response to the Consultation dated 22 June 2022 on the regulatory financial arrangements for the End of Tender Revenue (“EoTRS”) policy development. TCP welcomes the opportunity to help shape this area of Ofgem policy development which will frame key areas of the future offshore regime including the use of competition to determine future OFTO licencees and regulated revenues, offshore transmission asset value, and the design of performance incentives.

TCP is an established and proven consortium comprising International Public Partnerships and Transmission Capital Partners LP, which provides the necessary skills, capabilities and experience to succeed in the takeover and operation of offshore transmission assets. TCP has been involved in the OFTO regime from the original Ofgem consultation on the establishment of OFTOs back in 2009 and has subsequently participated in every OFTO tender process.

TCP currently acts as the OFTO for nine transmission assets, including Robin Rigg, Gunfleet Sands, Barrow, Ormonde, Lincs, Westernmost Rough, Dudgeon, Beatrice and Rampion. TCP is also preferred bidder on two further transmission assets; East Anglia One and Moray East. Through its proactive approach to managing these assets over the cumulative 64 OFTO-year operating history, TCP has achieved transmission system availability in excess of 99.9%.

We believe that TCP’s proactive approach to asset management sets it apart from other industry operators and we hope this approach and continued investment is recognised and valued by Ofgem. This approach is supportive of the UK Net Zero targets and should allow for the maximum possible life to be achieved from the transmission assets under TCP’s management.

This response addresses all of the questions set out in Ofgem’s consultation document. Annex A includes non-confidential responses.

Annex B contains responses which include confidential information relating to current / ongoing bidding rounds and so must be treated as ‘commercially confidential’ and not shared with other industry participants or be placed in the public domain.

In addition to the detailed responses set out in Annex A and B, TCP would like to draw your attention to the following core elements of our response:

- (i) TCP firmly believes that the greatest benefit to customers will be achieved through Ofgem focussing on maintaining the attractiveness of the sector to current and future participants
- (ii) Sector attractiveness and reliability of transmission services will be maximised by Ofgem establishing clear and proportionate regulatory provisions for the revenue extension process that confirm incumbent OFTO legitimate expectations of residual value. By doing so, Ofgem will avoid creating potential perverse incentives that may arise toward the end of the initial revenue period

- (iii) Competition has a central role to play in this sector and TCP believes that the greatest benefits from competition are derived at the initial tender / OFTO transfer. The benefits from competition at revenue extension for any EoTRS period are likely to be far more marginal and, in many cases, will be outweighed by the costs of running a tender competition and any associated transfer costs.
- (iv) TCP therefore urges Ofgem to adopt a pragmatic use of competition in the revenue extension process and to set a threshold (based on size of OFTO and the potential extension term) below which no competitive tender would take place and the incumbent operation would continue on terms agreed in discussions with Ofgem and the wind farm

We would welcome the opportunity to discuss this further with Ofgem.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'Chris Veal', written in a cursive, flowing style.

Chris Veal

Director

APPENDIX A – NON-CONFIDENTIAL RESPONSES

	Question	Response
1.	Have we captured the regulatory and commercial context for EoTRS policy appropriately? Are there other key contextual issues we need to bear in mind?	<p>TCP agrees that Ofgem has broadly captured the regulatory and commercial context for the EoTRS policy. However, TCP wishes to stress the following matters:</p> <ul style="list-style-type: none"> (i) TCP firmly believes that the existing OFTO regulatory regime provides a suitable framework for any revenue extension with the incumbent. (ii) TCP is unclear of Ofgem's view of the legal mechanics that Ofgem would have recourse to force a transfer of its OFTO assets. In particular in situations such as OFTO and Ofgem being unable to reach agreement on the asset transfer value or where the OFTO wishes to pursue alternative use / decommissioning of its assets. We note, that in contrast to other regulated asset classes (e.g. passenger rail franchises which explicitly contemplate future franchise transfers), at the time of ITT licence grant, there was ambiguity as to outcomes on the licence conclusion and the disposal by the OFTO to a future licensee. TCP would like to engage as early as possible directly with the windfarm owner to better assess / promote the decisions regarding any life extension (e.g. duration of extension, contingent / exceptional event protections, TNUoS charge, incentives regime etc.).
2.	What are your views on the EoTRS policy objectives we propose? Are they appropriate in the context of the decisions we propose to take?	<p>TCP urges Ofgem to place significant weight on the need for proportionality of regulation to maintain the attractiveness of the sector when establishing the final arrangements for the extension regime. Ofgem must not lose sight that the greatest benefit for customers - cost efficiency and innovation - will be derived from having a stable regulatory framework. Any interventions to introduce competitive tension into the extension regime will only generate value where there is scope for the benefits to outweigh the material costs of running a tender exercise (see response to Question 13). Such interventions must also avoid creating a perception of increasing risk for upcoming and future asset tenders.</p> <p>Introducing regulatory risks / uncertainties in respect of the EoTRS framework will have an immediate [negative] impact on existing asset tenders. To drive long term value for the UK consumer it will be important to define objective thresholds that could trigger the introduction of competition.</p> <p>A considered and pragmatic use of competitive processes is expected to support these objectives, but only where Ofgem can be confident in the net benefits to consumers and where the resulting revenue model and performance incentives create a sustainable long-term business for successful bidders. Given the large demand for investment in new offshore transmission assets, the objectives and efforts should be balanced in favour of proportionality, delivery and asset stewardship so these assets can continue to deliver the current high-performance levels and maintain interest</p>

Question	Response								
	<p data-bbox="339 1375 363 1534">in the sector.</p> <p data-bbox="384 896 408 1534">We set out below TCPs view on each policy objective.</p> <table border="1" data-bbox="443 127 1377 1543"> <thead> <tr> <th data-bbox="451 1167 512 1543">Policy Objective</th><th data-bbox="451 127 512 1167">TCP Comment</th></tr> </thead> <tbody> <tr> <td data-bbox="512 1167 869 1543">1. Deliver transmission infrastructure to connect offshore generation on a timely basis</td><td data-bbox="512 127 869 1167"> <p data-bbox="531 136 683 1158">Agreed – Considerations should be given in the context of the Offshore Transmission Network Review (“OTNR”) in which TCP is an active participant. OFTOs assets primary transmission equipment has a design life that extend beyond 40 years. Certain equipment may be suitable for life extension that prolong well beyond existing generation assets life extension.</p> <p data-bbox="703 136 855 1158">If at the EoTRS, transfer by an incumbent OFTO to a new OFTO is required, care must be taken to design a transfer system that allows an extension of the incumbent OFTO revenue stream in circumstances where there is a delay to asset transfer. Delays in negotiated transfer (or in reliance on a compulsory transfer) could ultimately impact on the availability of transmission infrastructure.</p> </td></tr> <tr> <td data-bbox="869 1167 1027 1543">2. Ensure OFTOs are robust and can deliver transmission services successfully over the licence period</td><td data-bbox="869 127 1027 1167">Agreed.</td></tr> <tr> <td data-bbox="1027 1167 1377 1543">3. Provide certainty and best value to consumers through the competitive process.</td><td data-bbox="1027 127 1377 1167"> <p data-bbox="1046 136 1137 1158">The introduction of a competitive tender process for the EoTRS period is not expected to provide certainty and best value for consumers. In TCP's view, this is particularly true for smaller projects.</p> <p data-bbox="1158 136 1369 1158">A competitive tender process will introduce direct costs as well as a degree of risk and uncertainty caused by the complexities of completing an asset transfer (as evidenced by existing OFTO asset transfer processes). Bidders will require compensation for such uncertainties. The OFTO asset transfer process is complex, lengthy, and requires significant allocation of resource / time to successfully achieve asset transfer. As evidenced by TCP's answer to Question 13, OFTO asset transfer costs are material and not linear with the price paid to acquire the transmission assets.</p> </td></tr> </tbody> </table>	Policy Objective	TCP Comment	1. Deliver transmission infrastructure to connect offshore generation on a timely basis	<p data-bbox="531 136 683 1158">Agreed – Considerations should be given in the context of the Offshore Transmission Network Review (“OTNR”) in which TCP is an active participant. OFTOs assets primary transmission equipment has a design life that extend beyond 40 years. Certain equipment may be suitable for life extension that prolong well beyond existing generation assets life extension.</p> <p data-bbox="703 136 855 1158">If at the EoTRS, transfer by an incumbent OFTO to a new OFTO is required, care must be taken to design a transfer system that allows an extension of the incumbent OFTO revenue stream in circumstances where there is a delay to asset transfer. Delays in negotiated transfer (or in reliance on a compulsory transfer) could ultimately impact on the availability of transmission infrastructure.</p>	2. Ensure OFTOs are robust and can deliver transmission services successfully over the licence period	Agreed.	3. Provide certainty and best value to consumers through the competitive process.	<p data-bbox="1046 136 1137 1158">The introduction of a competitive tender process for the EoTRS period is not expected to provide certainty and best value for consumers. In TCP's view, this is particularly true for smaller projects.</p> <p data-bbox="1158 136 1369 1158">A competitive tender process will introduce direct costs as well as a degree of risk and uncertainty caused by the complexities of completing an asset transfer (as evidenced by existing OFTO asset transfer processes). Bidders will require compensation for such uncertainties. The OFTO asset transfer process is complex, lengthy, and requires significant allocation of resource / time to successfully achieve asset transfer. As evidenced by TCP's answer to Question 13, OFTO asset transfer costs are material and not linear with the price paid to acquire the transmission assets.</p>
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Question	Response
	<p>Transfer costs for OFTO assets with a lower transfer value are considered disproportionate and it will be difficult to prove the benefit of introducing competition for these projects.</p> <p>TCP believes that the introduction of competition for the TRS extension of transmission assets with a residual value / Asset Transfer Value lower than £250m (in nominal term at the end of the initial revenue period) or where the extension period is less than 7 years would not pass a robust cost benefit assessment to the UK consumers.</p>
	<p>4. Attracts new entrants to the transmission sector</p> <p>TCP firmly believes that the greatest benefit for consumers, cost efficiency and innovation will be derived from having a consistent and competitive tender regime at the establishment of an OFTO.</p> <p>In that respect, Ofgem should focus where benefits to consumers are greatest, namely attracting new entrants to new/future tender rounds rather than tender extensions where they have less ability to drive greater value.</p>
	<p>5. Undertake streamlined and efficient tender processes</p> <p>In practice a streamlined tender process is unlikely to be achieved given the age and nature of the assets being transferred. As evidenced by ongoing OFTO processes, the grant of a licence via a tender is a lengthy and costly process expected to outweigh potential benefits brought by the introduction of competition.</p> <p>We feel this is particularly likely to be the case in respect of older assets, where manufacturer warranties will not be available, and exiting OFTOs will be unable to provide indemnity or similar protection due to the absence of a future revenue stream.</p>
	<p>6. Maximise the operating life of transmission assets where it is economic to do so</p> <p>Agreed</p>
	<p>7. Value-for-money TNUoS charges for wind farm and consumers</p> <p>Agreed</p>

Question	Response
	<p>8. Good asset stewardship and conduct by transmission assets owners</p> <p>A change of OFTO is inevitably going to lead to disruptions before, during and after completion of the asset transfer.</p> <p>Before = potential perverse incentive on maintenance regime</p> <p>During = diversion of resource to complete a transfer of assets rather than focus on maintaining high reliability</p> <p>After = transition period / change of operational teams etc.</p>
	<p>9. Proportionate EoTRS regulation</p> <p>Agreed</p>
<p>3. What are your views on our proposed approach to use competition to improve the value-for-money of ERS offers?</p>	<p>TCP supports initiatives that will create value for money to the UK consumers and we understand that Ofgem needs to have mechanisms to do so. Whilst the introduction of competition has delivered significant benefits to consumers, including bringing greater diversity of investors and innovation to the sector for the initial transfer, TCP believes that introduction of competition is highly unlikely to drive value for the UK consumer in the context of a life extension.</p> <p>Running a competitive process to effect a transfer of OFTO assets is expected to involve significant costs for both bidders and Ofgem. These costs will need to be recovered by various stakeholders including potential losing bidders and ultimately they will be passed through to the UK consumers. Our analysis suggests, on average, these costs could amount to £7.5m per project and exclude the cost of arranging new financing for the purchase of the assets. The analysis shows that there is limited correlation between the Final Transfer Value (“FTV”) and the transfer costs such that for small projects the transfer costs represent a significant proportion of the FTV. On smaller assets, transfer cost can exceed 15% of the transfer value. Indeed, TCP believes that for OFTO extension projects with Asset Transfer Values¹ less than £250m and short revenue extension period (< 7years) the costs of running a competitive tender will significantly outweigh the benefits. By default they would fail a cost benefit assessment.</p> <p>TCP believes the same outcomes can be achieved via a robust bilateral process with the incumbent including suitable benchmarks, taking into account the specificities of each OFTO project and its asset health review.</p>

¹ At the time the extension period would commence

	Question	Response
		In our response to question 13, we have listed the costs efficiently incurred that have allowed transfer of OFTO assets to occur.
4.	Are there any specific issues we should consider when considering the ERS drivers outlined in this section?	<p>ERS drivers are considered appropriate. In addition,</p> <ul style="list-style-type: none"> - TCP believes that the asset health review will be key to inform future decisions regarding the most valuable use of a particular OFTO asset. Each OFTO asset should be assessed individually taking into account its alternative use potential in the context of the OTNR or any other potential generation / storage activities as well as the life extension of the existing wind farm to which the assets are connected. The asset location, historic performance and overall conditions should inform the allocation of risk that will drive the most beneficial outcome for the UK consumer in the context of the UK Net Zero emissions target. For example, contingent event protections for operational failure, the level of working capital requirement and bankability / longevity of project will be key factors ultimately driving the most beneficial use of the OFTO assets - The finally determined risk allocation will define the cost of capital for the financing of the asset transfer value. - Transfer costs (i.e., arrangement fees, contingent liability financial guarantees and bid costs) may represent a significant portion of the ERS. - The indexation method ERS is expected to drive the ERS and should be considered. - Transfer method and value of intellectual property / software.
5.	Do you agree that we should define the extension period revenue model before requesting the incumbent OFTO's extension period offer? What will be the most important aspects to confirm? What could be left to later?	<p>Yes - It is critical that the revenue model is finally determined before requiring the incumbent to place its bid.</p> <p>Defining the revenue model (including the number (and length) of extension periods, availability regime and overall risk allocation) is one of the key inputs required to determine the level of ERS. The length of the extension period will not just drive the financing structure but also impact any potential upgrade capex and overall risk profile of the project.</p> <p>Changing the revenue model between the incumbent bid and a competitive tender process would prevent any reasonable comparison between bids and so undermine the entire process. If the model were to be changed, the incumbent must be allowed to restate their bid based upon the changed revenue model allowing all of the factors to be considered in the round.</p> <p>More broadly, the incentive structure, the extent of the protections afforded under the exceptional event and income adjusting event terms of the licence will need to be finally determined ahead of the incumbent OFTO offer submission.</p>

	Question	Response
		<p>In line with the existing OFTO regime, the incumbent will need a clear allocation of operational, financial and regulatory risks ahead of any bid submission.</p> <p>The items that could be left to later should be transparently observable via reliable / industry recognised sources.</p>
6.	<p>How long is it reasonable to expect the incumbent OFTO to hold its extension period offer valid? How might we adapt our approach to extend that period or ensure the incumbent OFTO is not exposed to unmanageable risk?</p>	<p>We would encourage any such period to be time-limited to a maximum of six months to avoid having to introduce enduring complexity (e.g. through use of ex-post regulation) to create a temporary pseudo-competitive pressure on the incumbent. Such an approach risks increasing costs in the long-term through greater regulatory burden and perverse incentives for the incumbents operational and investment decisions.</p> <p>The incumbent bid should be submitted late in the public interest test process, once Ofgem has finally determined the revenue model, transfer value and incentive regime and collated relevant benchmarks for comparison. The fixed offer period should be released where Ofgem concludes that there is sufficient potential benefit for consumers to run a tender process.</p> <p>In order that the incumbent OFTO is not exposed to an unmanageable timing risk compared to the potential later tender bidders, it would appear fair for Ofgem to allow the incumbent to submit an updated bid in the event Ofgem elects to run a tender.</p> <p>It will be very challenging (if not impossible) to define a process that will encapsulate all potential risks associated with the timing, changes of circumstances (financial market conditions, operational) to create a fair bidding process. Defining a set of adjustments parameters applicable to the incumbent bid assumptions is unlikely to be workable. TCP believes the current proposal is exposing Ofgem to potential administrative appeal given it will carry out an assessment of bids at two separate point in time.</p>
7.	<p>Should we consider the use of cost-plus methods or pre-defined uncertainty mechanisms to help extension period offers remain valid? What should we consider when designing any such arrangements?</p>	<p>TCP expects the level of transfer cost to represent an uneconomical proposition for projects with an Asset Transfer Value of less than £[250]m at the time of the extension.</p> <p>We do not think it is proportionate to modify the current, successful, TRS regulatory regime and incentive arrangements, to create a short-lived pressure on the incumbent to make a competitive bid for the extension. Simply allowing the incumbent to bid, as all other bidders into the tender would remove any need for the additional complexity of constructing and operating a new regulatory regime for the extension period.</p> <p>The options being considered, e.g. Cost-plus methods, have shown a significant increase in the regulatory burden including frequently repeated, in-detail efficiency assessments across the entirety of the business operation. SmartDCC and NG ESO are two examples currently regulated by Ofgem. For example, for the last regulatory year SmartDCC produced 334 published pages of information to support its claim for costs and gain share and Ofgem produced a</p>

	Question	Response
		<p>consultation document of 140 pages.</p> <p>If Ofgem were to persist with not allowing the incumbent to re-state its bid as part of the competitive process, a pre-defined re-opener with well-defined trigger conditions may provide a proportionate method for dealing with specific risks, identified by the incumbent, and enable a focussed discussion on what has changed, why and what is the efficient answer. These triggers could be applied for known uncertain costs, and provide a window and threshold approach where the incumbent would be able to call for change to its bid e.g. due to cumulative small issues that go beyond a threshold of a material effect on its bid. Furthermore, TCP believes that not allowing the incumbent to re-state its bid would potentially expose Ofgem to administrative appeal or other legal challenge.</p>
8.	<p>What are your views on asking incumbent OFTOs to hold their extension offers throughout a competitive re-tender process? If we did not do that, how could we ensure incumbent OFTOs present the most attractive extension offer possible?</p>	<p>TCP believes it is neither realistic nor in the interests of customers to be asking the incumbent to hold their extension offer for an extended period of time (i.e. more than 6 months).</p> <p>As evidenced by existing OFTO asset transfer processes, there are numerous exogenous factors that impact the validity of a bid. These include issues that may arise as part of the asset monitoring / ongoing maintenance regime after the asset health review / incumbent bid submission. Other factors may include financing conditions both (debt and equity).</p> <p>It is the transfer cost and human resource mobilised for an OFTO asset transfer that incentivise the incumbent OFTO to provide a bid that is highly competitive. Opening up the extension opportunity to a wider competition may not be the most appropriate tool available to Ofgem to ensure the incumbent presents the most attractive extension offer. TCP believes the use of a wide range of benchmarks to determine the costs efficiently incurred to extend the life of OFTO (and generation) assets, is expected to drive a better outcome overall without unnecessarily diverting significant cost and resource in running a tender process.</p> <p>The consultation notes in paragraph 3.20 that the purpose of this pre-tender bid is to improve Ofgem's position in bilateral negotiations should a competitive re-tender process be not launched. "<i>Holding the incumbent to its initial offer as far as possible maintains the benefits of competitive tension once it is no longer credible to re-tender</i>"</p> <p>However, once a competition is triggered, Ofgem can rely on the natural competitive tension and the incumbent OFTO should be treated as every other bidder, with the opportunity to provide a revised tender response.</p>
9.	<p>What arrangements would we need to put in place to ensure we can compare on a fair basis the incumbent OFTO's extension offer and those received from</p>	<p>See response to question 6 and question 8</p> <p>All bids must be made based on the same level of information, at the same point in time, and against the same revenue model and performance incentives. It is not realistic to compare bids that would be submitted at different points in time.</p>

	Question	Response
	other parties in a competitive re-tender process?	
10.	In what circumstances would it be appropriate to invite the incumbent OFTO to update its extension offer? When might a best-and-final-offer ('BAFO') invitation be appropriate?	The incumbent OFTO should be participating in the same process as all other bidders and therefore a potential BAFO should be used as per that process.
11.	What measures should we take to ensure incumbent OFTO extension offers are aligned with the findings of their asset reviews?	<p>TCP believes the findings of the asset health review will be key to determine the most appropriate revenue extension regime or indeed, the most suitable alternative use in the context e.g. of the OTNR initiative.</p> <p>As such defining an appropriate scope for the asset health review will be necessary to allow the asset health review audience to make the right decision in respect of a particular OFTO asset (i.e. extension, decommissioning, alternative use). TCP expects the outcome of asset health reviews will be very diverse between various OFTO assets, each OFTO asset is expected to have individual features that will potentially require adjustments to the specific regulation applicable to a particular OFTO asset. Indeed, it is reasonable to expect that greater value for money for the UK consumers will be achieved if Ofgem is able to establish an optimal risk allocation for each OFTO asset.</p> <p>To the extent the scope of the asset health review is comprehensive enough, the OFTO extension offer will reflect the findings of the asset health review.</p> <p>TCP's view is that the scope of the asset health review should be openly debated amongst stakeholders (e.g., through consultations) to ensure that OFTO extension offers are aligned with the findings of the asset health review. The contents of this process should be discussed as part of the ONTR forum and take account of how the asset health review can be designed to contribute to meeting the UK net zero emissions targets.</p>
12.	What information might it be suitable (or unsuitable) to share between the wind farm, incumbent OFTO or participants in a competitive re-tender process?	<p>Suitable: Asset health reports.</p> <p>Unsuitable: Incumbent extension bid or any assumptions within it</p>
	Competition public interest test	

	Question	Response
13.	Do you agree with the concept of the competition public interest test?	TCP broadly agrees with the concept of public interest test, where Ofgem is able to decide not to run a competition where there is no clear evidence that the balance of the cost of running such process, is substantially lower than the estimates of potential benefits that would accrue to consumers.
14.	Do you agree with the two proposed assessments in the competition public interest test? Are there any additional areas we should cover?	<p>The two proposed assessments appear logical in principle, as they assess the depth of market and potential value upside for consumers versus the benchmark bid. The challenge for Ofgem will be in making the assessment sufficiently robust and objective to be effective in screening those EoTRS OFTOs where there is realistic chance of an effective competition and understanding the value the incumbent OFTO brings.</p> <p>These two points are discussed further in answers to Q15 and Q17</p>
15.	What steps should we take to ensure any re-tender process attracts competitive bids that can be held through to asset transfer?	The competitive process will fail if there are insufficient competitors who are willing to bid or bids are of insufficient quality or credibility. Therefore, any re-tender process needs to have a robust test to establish the likely numbers of prospective credible bidders. The proposed market engagement must have objective criteria which will allow Ofgem to judge the likelihood of sufficient existing, or new entrants, participating in the tender process. This would need to be clear on the requirements for bidders e.g. to hold their bids for multiple years in order to avoid potential bidders withdrawing and the process failing. Any opportunity afforded to the bidders to revise, update or amend their bids during the process should equally be applied to the incumbent OFTO.
16.	What wider impacts on the OFTO programme should we consider as part of the competition public interest test? What would be most important to consider?	<p>Ofgem, OFTOs, Developers and potential bidders have limited transaction resources. Ofgem must consider where to best focus these resources in the interests of UK consumers. There are significant numbers of new, large OFTOs coming forward, whose value would suggest that making small gains in efficiency would vastly outweigh the benefits of dedicating resources to retendering early transitional OFTOs.</p> <p>Ofgem should consider how the application of the competition public interest test can be made sufficiently objective, to avoid having a knock-on impact on new OFTO tender processes. The transparency to bidders for new OFTOs of the circumstances where a competition would be applied at the EoTRS point will be important when developing their current bids. Ambiguity or uncertainty in the criteria for a competition will flow through as a downside risk embedded into TRS for forthcoming new OFTOs.</p>
17.	How should we best compare ongoing cost components of incumbent OFTO extension offers against cost reporting information and recent tenders?	The incumbent OFTO would be expected to have the best information on the needs of the asset to achieve a reliable transmission operation during the extension period. This should be aligned and commented upon in the findings of the asset health review. While unit costs for remedial works may be comparable, costs of retrofitting are unlikely to be comparable to new build.

	Question	Response
		<p>There is a risk that standard benchmarking may not be suitable for early asset designs. This could be addressed through making allowances for older designs and different levels of reliability compared to the next generation of transmission assets.</p>
18.	How should we consider if any profit/return element of an incumbent OFTO extension offer is appropriate and in line with opportunities with a comparable risk profile?	<p>The outcome of the competitive interest test / collating appropriate benchmark for projects with an Asset Transfer Value of less than £250m, is expected to be sufficiently informative to allow Ofgem to assess the appropriateness and value for money of the incumbent OFTO extension offer.</p> <p>For assets with a transfer value greater than £250m (where it is more likely that the outcome of the competitive interest test may suggest a net benefit from competition), Ofgem and TCP recognise that these ERS assets may, in themselves, be a new asset class, therefore any comparison could only be indicative of a likely range of acceptable returns. The competitive tension in the initial OFTO processes was considered sufficient not to require explicit examination of the returns, and we would advocate adopting the same principle here. If an additional assessment were included for the incumbent OFTO bid, it may undermine confidence in the competitive process that has previously been trusted to reveal the level of required returns.</p> <p>Further, the margins/returns are expected to drive a significantly smaller proportion in the determination of the ERS than the original TRS for the OFTO assets, therefore any assessment should be proportionate to the value it drives in any ERS.</p>
19.	How should we consider incoming licences would need to pay an asset transfer value? Will we need to set an indicative transfer value before the incumbent OFTO submits its extension offer?	<p>Incoming licensees must be required to pay the full Asset Transfer Value at the time of the transaction.</p> <p>Assets must be sold on an as is where is basis, with any risks or issues identified in due diligence priced into the bid ERS. This is necessarily distinct to the original OFTO transaction process, where the incoming OFTO takes the benefit of the manufacturer's warranties for new assets and if indemnity protection is required it is able to be offered by the wind farm developer, which has a clear revenue stream and assets of substance.</p> <p>Exiting OFTOs will be unable to provide this level of certainty and need to be able to exit. As Special Purpose Vehicles without a clear revenue stream post initial licence period, incumbent OFTOs would not be in a position to provide multi-year protections to purchasers. We would suggest that warranties be limited and alternative protections e.g. warranty and indemnity insurance be used to enable clean exit by the OFTO.</p> <p>As indicated, Asset Transfer Value is an essential component that must be determined before the incumbent provides its extension offer. The transfer value will be determined after considering all potential scenarios that should be considered in the asset health review. These scenarios may include an extension, a re-purpose of certain assets, alternative use in the context of the ONTR or dismantlement. The transfer value is expected to be the higher of these</p>

	Question	Response
		value as it will be legitimate for the incumbent OFTO to want to have a reasonable degree of confidence that an extension scenario provides it with a fair market value on the assets it owns, considering all potential alternative use of its assets.
20.	Could it be possible to potentially estimate the regulatory revenue stream savings from competitive tendering even before receiving an offer from the incumbent OFTO? If so, how could we best approach that assessment?	<p>We do not believe this would be possible.</p> <p>To the extent it could be undertaken, TCP strongly advocates that it would be largely an academic exercise that would necessarily require generalising assumptions that would not reflect the actual situation of the OFTO and that could not be relied upon to make an informed decision.</p>
	OFTO Asset value	
21.	Do you agree with the principles/objectives for the EoTRS asset valuation that we have proposed? What alternative or additional principles and issues do you consider we should take into consideration?	We agree with the principles outlined by Ofgem. In particular, we welcome the recognition in those principles of the need to properly reflect the circumstances around the original acquisition.
22.	Do you agree that at minimum, the EoTRS asset transfer value should seek to cover the NAV of decommissioned tangible assets?	<p>It is reasonable to expect from OFTO assets owners that they will look to maximise the value of their assets at the end of the initial revenue period.</p> <p>In the event the generation activities of the wind farm cease, the OFTO will consider the following alternative options:</p> <ul style="list-style-type: none"> (i) Repurpose of its offshore and onshore transmission assets in the context of the ONTR and Holistic Network Design currently being considered for the UK transmission networks. In this context TCP believes its primary transmission assets could have useful economic life extending well beyond that of the existing windfarm life extension. (ii) Separation between the onshore and offshore assets such that TCP is able to recover the value of the offshore assets decommissioned assuming a decommissioning of the offshore substation platform coupled with second hand sale of key components (eg. transformers) and metal scrap recovery (copper and offshore metal scrap).

	Question	Response
		<p>(iii) The value of non-decommissioned onshore assets will be greater than the value of decommissioned onshore assets. As such the OFTO will be incentivise to repurpose the onshore substation assets (i.e. grid connection points, cable landing points) for alternate generation activities. In addition, some OFTOs hold interest in land (freehold / leasehold) which could be re-purposed in the context of alternate generation activities (eg battery storage).</p> <p>Whilst TCP's preference is to continue owning and operating OFTO assets, it will be important for Ofgem to create a framework where the incumbent OFTO is confident that it will receive a fair market value for the assets and therefore will be willing to participate in an asset transfer transaction with any incoming new OFTO licensee.</p> <p>The alternative scenario, where Ofgem determines a fair value under a property transfer scheme, would have far reaching consequences for the OFTO regime. Any asset transfer value must recognise the full future value of the OFTO tangible and intangible assets that were necessary for the operation of the transmission connection for the offshore wind farm.</p> <p>The alternative uses of the onshore assets should wind farm not to continue are numerous and represent an active market where grid network connections are in short supply.</p>
23.	What is your view on setting the EoTRS asset transfer value higher than the NAV? If so, do you think this increase should cover "additional assets", a positive adjustment, or both?	<p>We would support an approach that recognises that not all OFTO incumbents are the same. For those that have procured or generated assets that would be of significant operational value to an incoming incumbent then these should be recognised in the transfer value.</p> <p>In addition, Ofgem should recognise where good asset management has led to consumer benefit (e.g. longer life, lower future costs) which should be shared with the incumbent OFTO.</p>
24.	If "additional assets" were to be included in the EoTRS asset transfer value, what types of assets do you believe should be included, if any?	<p>We have taken "additional assets" to be those in excess of what is necessary for the strict operational purposes of the transmission system for connecting the Offshore wind farm. The additional assets can be either tangible or intangible in nature.</p> <p>Tangible assets would typically include assets that enable enhanced asset health monitoring, e.g. Distributed Temperature System or additional spares. Intangible assets could include bespoke asset policies, intellectual property and procedures, historic survey data analysis, O&M data and reports etc. While learning from these would be consolidated into the asset health report, individual asset reports are valuable where there is a need for proactive asset management.</p>

	Question	Response
		TCP expects Ofgem will value good asset stewardship. This should be opined on by an independent adviser in the context of the asset health review.
25.	<p>If an adjustment was to be added to the NAV, do you have any feedback regarding approaches to set the positive or negative adjustment size?</p>	<p>The adjustment appears to be intended to incentivise the incumbent to maintain the health of the OFTO assets as reported in the asset health review up to the point of the asset transfer. Expenditure that gives value by maintaining the performance of the asset against the reliability incentive up the transfer date would not be in the incumbent's interest without this incentive adjustment.</p> <p>To make this adjustment effective, it would have to be sufficiently material such that the incumbent would effectively recover the residual value of such maintenance investments in the Asset Transfer Value. The residual value would occur where the new OFTO is able to delay an intervention in the future avoiding risk or costly repairs, and is therefore incentivised to continue to manage to the lowest lifecycle cost.</p> <p>Recognising that any significant asset failure or similar would be a reason to reopen the deal, these adjustments would be a question of lifecycle cost optimisation. Therefore, the value that should be payable could be assessed by reference to the incumbent lifecycle cost estimate underpinning its bid, and the effect of such interventions completed before the asset transfer. The value to the outgoing OFTO would reflect the overall impact of optimised spend, translated into a premium in the transfer value. Incumbent would be allowed to recover the intervention cost and receive the benefit of the lifecycle optimisation value, from the deferral or total avoided spend in the future.</p>
26.	<p>What standard assumptions might be appropriate to apply when determining NAV for assets in early tender rounds? What project-specific adjustments might need to be made?</p>	Residual values assumptions used in winning bids in early tender rounds should be included in the NAV, as these represented an expectation and plan for extended life. The assumption of a residual value offsets the amount of remedial work that might otherwise have been needed if the assets were managed to a 20 or 25 year asset life.
27.	Do you have any suggestions for alternative approaches to determine the EoTRS asset transfer value?	Residual economic life, i.e. assessed based on the outcome of the asset health review.
28.	Do you have any suggestions regarding payment structures for the EoTRS asset transfer value?	In the event the OFTO assets are transferred to a third party, TCP strongly advocates a single payment is made on the asset transfer date.

	Question	Response
	Performance incentives	
29.	Do you consider it appropriate to have more than one option for creating a performance incentive?	OFTOs have performed well under the current incentive regime. Whilst there may be marginal improvements worth considering (e.g. in respect of coordination between generator and OFTO maintenance regime), there is a risk of overcomplicating a proven regulatory framework.
30.	Are there any additional performance incentive approaches you believe we should consider for the extension period?	Under paragraph 5.8 (i) Ofgem explores an increase of the level of penalty relative to the level of revenue. TCP considers this option is expected to increase the risk profile of the OFTO and reduce the OFTO's ability to finance the asset transfer at competitive rates provided by senior lenders. Substantial savings for UK consumers have been achieved thanks to the stability of the OFTO regime. In particular, the 10% cap imposed on availability deductions provides a high degree of predictability in the revenue structure which itself leads to low financing costs.
31.	Do you think that the alternative return / penalty mechanisms discussed here should be applied in the extension period? Are there any further return / penalty mechanisms you think we should consider, and why?	In TCP's view it is too early to opine on practicalities of the incentive regime. This will need to be driven by the findings of asset health reviews. TCP does not believe that a balanced scorecard is expected to drive substantial improvement to the OFTO extension regime. In TCP's opinion, criteria such as Health and Safety improvements should form part of the OFTO's fundamental duty of care and should not be subject to financial incentives.
32.	Are there any specific incentives that you would like to see introduced into the OFTO regime? Please explain.	In line with the existing OFTO regime, the incentive package should be centred around the availability of the primary transmission asset. TCP believes the outcome of the asset health review should also inform potential adjustments to the licence to incorporate asset specific conditions.