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30 April 2007
Our Reference NG/LAD

Dear Giles,

Offshore Electricity Transmission Second Scoping Document

National Grid is keen to explore the option of becoming an investor in offshore transmission networks and the opportunity to bring value from our expertise in managing the establishment of offshore networks. This response provides our views on the issues raised in the 2nd scoping document from the perspective of a potential investor in offshore networks. (National Grid's views as onshore licensee and as designate GBSO for offshore networks are the subject of a separate response.)

The second scoping document contains a useful structure for considering the development of the offshore regulatory regime and helpfully sets out Ofgem's views on the identified issues. We found the communication sessions a valuable summary and opportunity to discuss issues and the way forward.

Regime development process

In terms of the regime development process, we note and support the intention to have separate and parallel working groups on the various technical, GB access and regulatory issues. In the regulatory area in particular, we agree that there is sufficient separation of issues to justify parallel working on transition/adoption, tender/bidding and licenses/controls. However, it is also likely that there will be a need for significant interaction between these areas as work progresses. This interaction is likely to be assisted by a requirement by most companies to have the same individual providing representation to these groups. A scheduling of meetings with this in mind (preferably by arranging them to be consecutive on the same day) would be very helpful.

In terms of interactions between the commercial/technical/regulatory areas, a detailed and explicit examination of the manner in which co-ordinated network development can be encouraged and achieved will be important and valuable. We agree that application windows will be important in determining the volumes of connection in each area in each round for which network economies of scale might be appropriate. However, other features will also be important in ensuring a co-ordinated approach over time. For example, the balance between detailed technical standards that will ensure

modular and extensible development must be considered against the benefits of open functional requirements which will better facilitate solutions using new technologies.

Connection application process

From the perspective of a network investor, key requirements of the connection application process are:

- 1) To encourage provision of the best information on the nature of customer need (for the purposes of deciding the best connection solutions), and
- 2) To provide evidence that offered solutions are economic and efficient (by virtue of users' willingness to commit to pay cost-reflective charges).

On the basis that the regulatory regime, even one based on long-term contracts, can only offer limited protection to investors from the consequences of unwanted or grossly under utilised assets, all network investors will want to ensure that the GBSO to user agreement process represents an appropriate economic test. A two part agreement would seem very relevant in this context so that an initial user agreement to proceed on the basis of very indicative costs can be refined to a more specific 'willing to pay' test.

Tender process

The stages suggested for the tender process in the scoping document appear sensible and comprehensive. We agree that it will be important to minimise bid costs, particularly in the early stages. However, the key issue must be to achieve a process which identifies the most cost-effective solution and provide certainty that, for all controllable factors, it will be delivered as agreed. This poses a number of significant design challenges:

- 1) Low cost bids, at least initially, imply low investment in acquiring specific information for tailored bids. On what basis are such bids short-listed in the tender negotiation framework?
- 2) What aspects of a bid will be the subject of pre-defined qualification criteria and which can be left open for bidders to distinguish themselves competitively? Will this include the user-commitment elements? How might significantly different quality undertakings be compared?
- 3) How can applications be standardised so that experience from one project benefits the next?

Licences and regulatory contract

We agree with the topics highlighted. The specification of the contracted service is an area which is closely tied to the form of the tender process (especially issue 2 above). Clarity on how risks and uncertainties that cannot be resolved at the tender negotiation stage will be treated in the future will be important and valuable. A consideration of all the conditions in an onshore transmission licence and their suitability for the offshore context will be useful work area.

Interim arrangements

While a number of the issues associated with adopting assets developed in transitional arrangements are specific to the particular development projects concerned, there are a number of issues which are closely related to the tender process and form of regulatory contract. It will therefore be important to ensure these interactions and dependencies are addressed in the process.

In terms of the pre-conditions for assets to be treated as transitional, we suggest that it might be beneficial to separately address certain items of intellectual property (e.g. sea-bed surveys, consents, and routing studies) which may be valuable in facilitating the tender process.

A specific issue for network investors considering the adoption of assets partially or fully constructed under transitional arrangements will be the scope for regulatory valuation of the assets to be renegotiated/reopened once the tender process and transfer discussions ensue. To what extent can the original developer be directed under the regime to transfer assets at a particular price? How do such transfer arrangements interact with developers' rights to appeal?

Conclusions

We are encouraged that there is a well designed structure for developing policy and draft documentation for the offshore regime. The timescales, however, are very ambitious and there are a number of implementation areas where significant detail will be dependent on important policy considerations that are yet to be made. We look forward to a period of intensive and constructive engagement to meet the desired objectives.

Please contact me directly if you wish to discuss any points raised in this response, or the manner in which National Grid can assist with the regime development process.

Yours sincerely,

Lewis Dale

Cc: Paul Whittaker