



Response to Ofgem Scoping Paper on Offshore Transmission

30th April 2007

EXECUTIVE SUMMARY

We have the ambition and capability to be a leader in the provision, ownership and operation of the transmission infrastructure required to harness the UK's rich offshore renewable resources. We will continue to play a full part in the development of a framework that can balance the interests of all stakeholders.

Taking a Balanced and Coordinated Approach

As we have stated in previous responses, the primary objective for the offshore regulatory framework, of which the licensing regime is a fundamental part, must be to facilitate economic and effective connection of offshore renewables. This will require a coordinated approach to be taken to the design, delivery, ongoing operation and extension of offshore transmission networks.

We welcome recognition from Ofgem of the need for a coordinated approach. However, we remain concerned that the proposed non-exclusive framework could result in an entirely point-to-point approach. It is very important that the detailed framework is designed so as to facilitate this coordination. The key requirements are as follows:

- Asset based tenders from prospective Transmission Owners (TOs) for individual developments and clusters of developments as appropriate.
- Clusters to be identified at the application stage and tendered as clusters.
- TOs responsible for coordinating design, delivery and operation of assets.

Competitive Model

We support the concept of a multiple TO model within the BETTA framework and believe that this will deliver benefits to users of the network and to customers in general. However, we note that both the Authority and Ofgem have indicated strong support for full ownership unbundling of transmission activities from any retail/wholesale activities across Europe. This would prevent developers from acting as TOs and would, in our opinion, severely limit the scope for competition for offshore transmission licences.

Connection Application Process

We remain of the view that it will not be possible for any party to develop a connection offer that has any degree of firmness, on either cost or delivery timetable, in a 3-month period. Depending on the scale of the project the preparation of a firm offer could take up to 12 months. We therefore see no merit in the proposed indicative offer process. Far from providing greater certainty, we are concerned that this will mislead developers and create uncertainty, as there is a high probability that the actual cost/timetable could be significantly different. Any offer issued within a 3-month period should not deal with the costs/timetable associated with the offshore works.

Minimising Tender Costs

We support the objective of minimising tender costs. However, this must be balanced with the need to encourage serious bidders to submit robust and deliverable tenders. We remain firmly of the view that serious bidders should have their efficient costs funded, regardless of whether the bids are successful.

Our high level comments on the main issues are set out overleaf.

GENERAL

We are committed to providing our full support, in terms of resources and expertise, to develop a regulatory regime that can facilitate economic and effective connection of offshore renewables.

We support the concept of a multiple TO model within the BETTA framework and believe that this will deliver benefits to users of the network and to customers in general. Another advantage of this model is that it provides developers, subject to meeting requirements on legal separation, to become TOs for the assets connecting their developments.

However, we note that both the Authority and Ofgem have indicated strong support for full ownership unbundling of transmission activities from any retail/wholesale activities across Europe. This would prevent developers from acting as TOs and would, in our opinion, severely limit the scope for competition for offshore transmission licences as no party would be able to compete with National Grid under this scenario.

CONNECTION APPLICATION PROCESS

Indicative Offer

We understand that, from a connection queue perspective, it is imperative that offshore developments are not disadvantaged relative to onshore developments. It is therefore important that offshore developers receive some form of offer within a 3-month period. However, we do not believe that it is desirable, or in the interests of any party, for an indicative offer to be issued covering costs or delivery timescales for the offshore works.

We remain of the view that that it will not be possible for any party to develop a connection offer that has any degree of firmness, on either cost or delivery timetable, in a 3-month period. Depending on the scale of the project the preparation of a firm offer could take up to 12 months. This would involve a detailed engineering and environmental design and a formal tender process to prospective manufacturers and contractors. It will only be possible to carry out a desktop design/costing in a 3-month period. Our analysis indicates that actual costs could vary by as much as 50% from a cost estimate developed by a desktop study.

We therefore see no merit in the indicative offer process set out by Ofgem. Far from providing greater certainty, we are very concerned that this will mislead developers and create uncertainty, as there is a high probability that the actual cost/timetable could be significantly different. Any offer issued within a 3-month period should not deal with the costs/timetable of the offshore works.

Consideration must be given to the fact that the vast majority of developments will already have an onshore connection offer and, in many cases, will have accepted this offer. We are not convinced that there is a need for another offer to be issued in these cases.

If it is decided that an indicative offer incorporating costs/timetable for the offshore works is required then great care will be required to ensure that this does not provide National Grid with an advantage over potential competitors. Given that all of the offshore developments currently proposed are in England & Wales, the host TO will be National Grid. In order to minimise this advantage it will be important to ensure that all information made available to National Grid is immediately released to other potential TOs.

Application/Commitment Window

A coordinated approach in locations where there are a number of developments will require some form of application/commitment window to work with a clustering approach. Such a window would provide an opportunity for adjacent developments to secure the appropriate consents and financial approvals and make the necessary user commitment to allow construction of the transmission assets to commence. This could result in a delay for some of the early movers in a particular area but should ultimately result in more MWs connecting.

Rather than having a fixed window, as is suggested in the Ofgem paper, we believe that some flexibility should be retained based on the intended timescales of the various developers in a particular location. This could result in a window of less than or greater than one-year being applied.

CONNECTION VIA DISTRIBUTION NETWORKS

We note the statement in paragraph 4.1 of the Ofgem document that the majority of Round 2 projects consist of offshore 132kV circuits connecting to an onshore distribution system. Our analysis indicates that this is not the case and that it is in fact a minority of such circuits that will connect to a distribution system.

We generally support the preliminary model outlined in the paper for dealing with this issue. On the issue of how the GBSO recovers the costs of connecting to the DNO network, then we would not object to the principle of these costs being funded by the OFTO and recovered through the ongoing payments from the GBSO. However, recovery of these costs in full must be guaranteed within the OFTO licence.

DESIGN OF THE TENDER PROCESS

We generally support the outline of the iterative tender process set out in the Ofgem paper. Our concerns are:

- the degree to which it will be possible to differentiate between bidders on price in advance of detailed pre-construction work; and
- the need to encourage serious bidders by funding efficient tender and pre-construction costs.

Differentiating on Price

We do not think that it will be possible for price to be the main differentiating factor at the initial stage of bid evaluation. As previously stated, we do not think that it is possible for a firm price to be developed in advance of detailed pre-construction works. Prices bid at this early stage must therefore be considered as indicative only.

There is a range of criteria that we believe should be considered in addition to price:

- ability to meet licence obligations;
- safety case and the priority given to safety;
- environmental impact (this would include the number of cable routes and landing sites);
- delivery timetable (although this will, again, be indicative at the initial stage);
- the need to have a number of TOs to encourage competition and comparison; and
- level of network losses implicit in design.

Minimising Tender Costs

We support the objective of minimising tender costs. However, this must be balanced with the need to encourage serious bidders to submit robust and deliverable tenders. We remain firmly of the view that serious bidders should have their efficient costs funded, regardless of whether the bids are successful.

It is sensible to seek to share seabed surveys and other environmental works. However, as stated in previous consultation responses, care will be required to ensure that a desire to minimise tender costs does not remove the scope for design and delivery innovation on the part of tendering TOs. TOs should also have no liability in the event that such shared studies prove to be flawed.

Role of National Grid as System Operator

We welcome recognition of issues around the potential for the TO business of National Grid to gain an unfair advantage from the involvement of its SO business in the tender process and are pleased that tender evaluation is to be led by an independent panel. However, if other prospective TOs are to have sufficient confidence in the process, it is important that the role of the SO at each stage is clearly set out as soon as possible. This will inform the development of measures to ensure that there is no scope for National Grid to gain an unfair advantage and to ensure impartiality and strict confidentiality between its SO and TO functions.

Authority Approval of Award

We note the intention that the Authority approve any award following the tender process. While we understand the legal requirement for such an approval, we believe that it is essential to clarify this aspect of the process. In particular, clarification is required as to what would happen in the event that the Authority rejects or proposes changes to the terms of a proposed award. If the Authority proposes a change to the terms of an award then, as a point of principle, the prospective TO should have the choice of rejecting the proposed changes.

PRICE CONTROL / REGULATORY REGIME

In principle the price control / regulatory framework should involve a light touch from Ofgem, be as simple and straightforward as possible and incentivise outputs that are within the control of the licensee. The main issues are covered below.

Obligations

The obligations applicable to an offshore TO should be consistent with those applicable to onshore TOs.

Output Specification and Performance Incentives

As recognised in the Ofgem paper, it is extremely important that a clear specification of transmission requirements is available against which a prospective TO can prepare a bid. The technical performance criteria set out in such a specification must be realistic and deliverable.

We note the examples set out in the Ofgem paper include minimum availability, maximum number of unplanned power interruptions and maximum number of major cable failures. Performance incentives are important but care is required in designing such incentives to ensure that the specified outputs can be influenced by the TO and the targets can be met.

Proper consideration must be given to the fact that TOs will not have a diverse set of assets of different ages and condition and in different locations but will have a small number of similar assets in the same location. While the assets can, in theory, be designed to meet a minimum set of requirements, the TO will not be in control of them over the 25-year life. Consideration must also be given to the lack of experience of operation of offshore transmission assets over an extended period. It is also possible, for example in the event that serious problems were to materialise with sub-sea cables, that further capital investment could be required to maintain performance within required levels.

We note the statement that targets for network losses might be expected to be included in a performance regime. While the level of losses is an important issue, and the assets can be designed for specific levels, the TO is not in a position to influence losses over the operational life of the assets. Rather, it will be the actions of the SO and the generator that will influence the level of losses over the life of the assets. Losses should not therefore be included in a performance regime for the TO.

The impact on the costs of providing, owning and operating the offshore assets must be considered when designing the incentive regime. Care is required to ensure that the performance incentives are not so onerous that they force TOs to incorporate additional redundancy or significantly increase the level of risk borne by the TO.

Certainty of Delivery

We note the statement in the Ofgem paper that prospective TOs should be able to demonstrate that contractually binding commitments are in place to finance, construct and maintain the required infrastructure during the latter stages of the bidding process. We would comment that it might not be possible to have binding commitments in place until a licence has been awarded. Contractors might not be willing to sign binding commitments until there is a certainty that a particular party will be the TO for a particular set of assets.

Adjustment Mechanisms

Our previous consultation responses have highlighted the potential for costs to move due to factors outside the control of the TO. Such movements in excess of pre-defined thresholds should be dealt with by adjustment mechanisms.