



*taking care of the essentials*

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Our Ref.

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## **Offshore Electricity Transmission – a joint Ofgem / BERR Policy Statement**

Dear Colin,

Centrica welcomes the opportunity to comment on the joint Ofgem / BERR Policy Statement concerning the regulation of offshore electricity transmission. We appreciate the Government and Ofgem's recognition that generators need to be more heavily involved in the design of an offshore regime when compared with the development of onshore arrangements.

As a major offshore developer and generator, Centrica has some reservations that the proposed regime is becoming increasingly complex and will not address the original objectives envisaged by the implementation of a regulated approach. It has become apparent that implementation of the proposed regime will be a lengthy and complex process, with intricacies that will have to be endured with each tender round. Further, we are concerned that the proposals will not deliver the intended outcome, i.e. that the costs of offshore transmission will be more expensive through the price control process than through a merchant approach. As such, Centrica believes that there is merit in reconsidering the merchant approach, allowing developers more responsibility and flexibility. We want the best regime that will deliver the infrastructure to support our projects in a timely and cost efficient manner, whilst simultaneously driving down costs for consumers and ensuring that Governmental policy objectives are being met.

As noted above, Centrica's preference is for a merchant approach, however, should Ofgem and BERR decide that there is no scope for reconsidering this approach, it is critical to stick to the non-exclusive, regulated regime which, if delivered effectively, will present more opportunity for competition, cost-savings, and more project security for generators, than the exclusive approach.

A main concern with the current proposals, however, is that the detail of the proposed regime does not yet align with the process for developing and consenting a project, or with the design of the assets offshore. The key information needed by developers to successfully deliver offshore projects includes certainty over security standards, clear

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definition over what will be considered 'economic and efficient' investment (i.e. adoption criteria) and clarity on the price control and charging regime. A clear understanding of the costs associated with connection and transmission assets is essential to establishing the financial viability of a project.

Please find below our responses to the specific questions raised in the policy statement.

### Chapter Three

*Question 1: Do you agree with our proposals for the design of the regulatory regime as outlined in this chapter? In particular, we would welcome your views on*

*- the role of the OFTO and the obligations it would undertake;*

Broadly, Centrica supports the obligations that have been outlined for the OFTO. However, we contend that there is a need for an obligation within the new regime that requires a formal agreement / bilateral contract to exist between the OFTO and the generator. Under the proposals outlined in the policy statement, a contractual agreement only exists whereby the two parties need to diversify their design from the standard regime. This should be extended to ensure that proper communication takes place with the generator during the design and construction of the new connection.

*- the regulatory and contractual framework, including the duration of (and what happens at the end of) the revenue stream, predefined adjustment mechanisms, transfer arrangements, and business separation requirements;*

We are concerned about the proposal to use a twenty year revenue stream for offshore assets. This is inconsistent with the onshore arrangements, where a forty year term is used, and with the duration of the offshore leases which are for up to fifty years. Furthermore, it is inconsistent with the expected life of assets. Whilst there may be some uncertainty as to the lifetime of an offshore substation, there are examples of sub sea cables that have been operating for thirty years, and are still in service.

Centrica would like clarification on what will happen at the end of the twenty year period of the price control. If the wind farm is re-powered, and the existing transmission infrastructure is used, it will not be right to recover further revenue from assets that have had their value fully recovered. As such, we contend that licences should specify that any further revenue streams after the twenty year period, should only account for operation and maintenance costs and any necessary replacement costs. If further revenue recovery is allowed then this benefit should be shared with users.

With regard to the existing OFTO, provided the performance of the OFTO is compliant with the relevant licence conditions and standards, we believe that conducting a re-tendering exercise is potentially unnecessary and will incur avoidable costs and time delays. We believe that, based on performance, the existing OFTO should be allowed to continue, if willing, at the end of the lifetime to avoid unnecessary tender processes and the associated costs.

Centrica believes that there is substantial risk in not allowing re-openers in the absence of a periodic price control review, not least as this is a new regime and not all risks and issues are fully understood at this stage. Further, the lack of re-openers opens up a possibility of corner-cutting and inflated bids to cover risk that will be front-ended, i.e.

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construction and stranding risk. There is no mechanism to reduce the price once these risks have been removed, i.e. post-construction, nor will there be scope to ascertain if the levels of investment are efficient during the development of the project. Of greater concern to potential OFTOs will be the fact that there is also no mechanism for recovery of costs resulting from a *force majeure* occurrence. OFTOs will require some assurance that they will not be subjected to risks that are beyond their control in order to guarantee their participation in the offshore regime.

We require more information on the proposed price control and how rates of return will be set and monitored for OFTOs. It is important to maintain a balance between the level of risk and reward that the OFTO is taking and this should be monitored over the twenty year licence period. If the OFTO is making windfall profit to the extent that generators and consumers are disadvantaged, a mechanism similar to the SO incentive scheme should be introduced with a cap and collar model, thus enabling the OFTO to retain a proportion of their financial gains but also ensuring that the regime has been successful in driving down costs for generators and consumers.

Whilst we acknowledge that more should be done to encourage potential OFTOs to come forward to invest offshore, this should not be at the expense of generators or consumers and any incentive scheme should encourage both cost savings and innovation.

- *the form and quantum of performance incentives;*

We eagerly await further information on this aspect of the regime, however, we are supportive of the motion to reimburse generators for loss of availability. The compensatory amount should be equivalent to the value paid in TNUoS, or in excess of this figure, in order to remunerate against loss of ROCs. Our preference would involve the amendment of industry agreements to enable the GBSO to provide the rebate to the generator, as opposed to a separate refund arrangement, via a separate bilateral agreement, between the OFTO and the generator.

It will be key for the generator to be able to determine the commissioning date and for incentives to be formed around meeting this target date.

When determining the thresholds for performance incentives, it should be remembered that there will be differences with onshore, for example, in terms of annual availability.

- *dealing with changes to generator requirements; and*

Centrica recognises that there is scope within the regime for deviation from a standard design. Centrica is concerned that amendments to the standard design will not be dealt with under the standard arrangements and feel strongly that any innovation or design amendments should be incorporated within the existing revenue stream between the generator and the GBSO, and the GBSO and the OFTO. It will become increasingly complex and costly for the generator and the OFTO to devise bilateral agreements for 'bolt-ons' that sit outside the regime. As noted, there should be a means of incorporating such variations to the standard template into the existing, regulated charges.

Placing a cap of twenty per cent on any incremental investment does not promote innovation, nor does it encourage the development of wind farms with additional capacity for future expansion.

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- *the allocation of risk.*

Centrica feels that the allocation of risk requires more work. The risk of loss of availability and outages should not be borne solely by the generator, but instead by the OFTO.

In the instance of insolvency of the generator, there is no justification that the treatment should differ to the onshore arrangements. Security provisions are already in place within the existing industry codes in the event of generator insolvency. Any additional costs are recovered through adjustments to TNUoS and so are recovered from the whole industry. As stated above, there is no justification why offshore generation should be treated differently and the offshore arrangements should mirror the onshore arrangements wherever possible. If this principle is adhered to, then the OFTO should not be exposed to any more risks in the event of insolvency than the onshore TOs.

It is important to note, however, that the ability to mirror the onshore arrangements in the above example is dependent upon the outcome of National Grid's consultation on the offshore charging methodology. The above solution would not be available if option 3 is adopted whereby the use of system boundary is set at the onshore connection point and all offshore charges are therefore connection-related. This strengthens the need to maintain a link with the charging proposals when developing the new offshore transmission regime in its entirety.

*Question 2: Do you feel that there is any aspect of the design of the regulatory regime that we have not considered sufficiently?*

Overall, we believe the framework of the proposed regulatory regime has been adequately described. However, as ever, the detail is fundamental to the successful implementation of these new arrangements.

## **Chapter Four**

*Question 1: Do you agree with our proposals for the enduring competitive process as outlined in this chapter? In particular, we would welcome your views on:*

- *the use of an annual tender application window;*

Centrica is not supportive of tender windows. They will be difficult to co-ordinate with the connection application process and cause unnecessary delays in an already long process and will consolidate the workload of the tender panel. A similar process is not used onshore so we see no merit in introducing it offshore.

- *the design of the tender process, and the stages we have outlined;*

We disagree with the anticipated timescale of one year for completion of the tender process. As consents must be granted during the tender process, eighteen months to two years would be a more feasible timeframe for delivery. It is also likely that the offshore generator will not apply for consents until a firm connection offer has been awarded, which would provide a good case for reducing the tender process to a three month delivery schedule.

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As an offshore generator, it is important that we are provided with comfort that changes to the design of the assets, e.g. the route-to-shore or the onshore connection point, will not change drastically so as to cause financial loss to the generator, either by means of loss of secured sums (to be provided from the offset at the point of an indicative connection offer, and especially non-refundable under the generic user commitment model), or through loss of connection application fees or consents costs. The tender process outlined in the policy statement does not protect the generator from changes that can be made by either the OFTO or the GBSO.

We strongly believe that it is out of scope for the GBSO to conduct the sea-bed surveys. This does not fit with the scope of the existing licence and it is difficult to see what justification could be used to allow the system operator to start work offshore to contract and execute contracts for work such as geotechnical surveys. It would be more appropriate for either the offshore generator to carry out such works, or for a Governmental agency to conduct the surveys whilst tendering for new leasing areas. We suggest this may come under the remit of the future MMO as described by the Marine Bill White Paper.

*- recovery of the tender costs; and*

Centrica would like further clarification on how Ofgem's tender costs will be recovered. An overview of the likely costs would also be beneficial.

We agree that it is appropriate for bidders to absorb the costs associated with their own bid.

*- running the tender process.*

We are happy that the tender process will be managed by Ofgem. We note that BERR would be equally qualified for this role.

As an aside, we feel that it is important for the offshore generator to play a greater role in appointing an OFTO for a number of reasons. Most importantly, the generator will need to agree the revenue stream to make sure that its involvement in the project will also be economically viable. There is an element of co-ordination also required in terms of agreeing the design and specification of the assets, and also the lifetime, as mentioned above. There needs to be a mechanism that prevents the OFTO acting against the generators wishes and building additional capacity, for example, which the generator does not wish to finance. In the current proposals, there appears to be no guarantee for the generator that the OFTO will follow the generator's project specification.

It is important to note that should a generator become involved in assessing the bids, confidentiality agreements must exist in the event of the generator bidding to become its own OFTO.

*Question 2: Do you feel that there is any aspect of the enduring tender process that we have not considered sufficiently?*

Centrica has grave concerns that there will be no OFTO of last resort for the enduring regime. As a generator, we require confidence that our projects will be provided with connections to the onshore transmission system, however, the regime provides no

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certainty that an OFTO will be selected, and makes no allowance for a process for delivery of a connection if not.

## Chapter Five

*Question 1: Do you agree with our proposals for the transitional arrangements as outlined in this chapter? In particular, we would welcome your views on:*

- *the pre-conditions for qualifying transitional projects;*

It should be noted that Centrica's projects operate on a balance sheet basis and will not experience "financial close" as detailed in the policy statement. We welcome Ofgem's acknowledgement of this but note that it is very unlikely that *unconditional parent company support* will be granted for any project. There may also be many different interpretations of "financial close" within different organisations and consistent criteria used across projects will be appropriate.

- *the tender process for transitional projects, and whether they capture the potential projects that will require adoption;*

Centrica has some reservations regarding the treatment of projects which will have commenced design works, and therefore incurred costs, but will not meet the pre-conditions for transition and will therefore fall under the enduring regime. In these instances, such projects could suffer delays, will not have the security that the generator can become the OFTO of last resort, and will not be guaranteed recovery of the RAV.

Centrica requests a clear and timely indication of the type and detail of information requirements that Ofgem have in relation to assessing transitional projects.

- *the transfer of assets; and*

Centrica agrees that the transfer of assets should take place post-construction, allowing the generator to maintain ownership for design and construction. As a consequence of this, as mentioned earlier in the response, the generator should be privy to the bid information presented to the tender panel to ensure consistency with their proposed design, and to prevent delays resulting from any potential disagreements between the elected OFTO and the generator.

- *interaction with the enduring regime.*

We welcome the opportunity for the generator to become the OFTO of last resort but stress that we would like to see the same arrangement apply for the enduring regime.

We also question whether it will be necessary for the generator to be subject to the same price control approach if it were to become the resultant OFTO through the "OFTO of last resort" mechanism. Further clarity on this matter would be appreciated.

*Question 2: Do you feel that there is any aspect of the transitional arrangements that we have not considered sufficiently?*

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Centrica would like more clarity over Ofgem's determination of efficient costs in relation to the RAV assessment. Additionally, Centrica believes that the guarantee of seventy-five per cent of *ex ante* costs is not sufficient and would prefer to see a guarantee of at least one hundred per cent of the *ex ante* investment.

Centrica is further concerned that seventy-five per cent of the *ex ante* costs are not guaranteed unless the tender process has been initiated by the 'go-active' date.

## Chapter Six

*Question 1: Do you agree with our proposals for the connection application process as outlined in this chapter? In particular, we would welcome your views on:*

- *the pre-application process;*

We believe that there is merit in the publication of potential connection information by the GBSO and believe it will benefit all developers of all types of generation. However, we note that as a rule, onshore connection sites with available capacity are not necessarily where developers need to connect wind farms. Enhanced dialogue and communication between the generator and the GBSO prior to submission of the initial connection application will assist in the determination of both parties' requirements and should aid time efficiency.

Our only reservation in the provision of additional data by the GBSO, potentially in the SYS, is that the process may be resource-intensive and we would therefore like to understand the costs involved in providing this service and how these costs will be apportioned.

The pre-application process should aid the connection application and tender process and should not introduce unnecessary time constraints.

- *the indicative offer process (stage 1);*

As aforementioned, we are concerned that a requirement to provide security at this stage of the process will potentially result in the generator incurring costs resulting from OFTO-led changes impacting the final connection offer. The tender process for the OFTO can only start after an onshore connection application has been made by the developer. This is a significant risk for the developer as there is no requirement for the OFTO to provide a connection at the point selected by the developer. As such, the developer is exposed not only to multiple connection application fees but also to termination (final sums) amounts as a result of an OFTO selecting an alternative connection point. We strongly believe this risk needs to be mitigated within the proposed arrangements.

We believe that the three month timescales are sufficient and should be maintained with a view to ensuring as much consistency with the onshore arrangements as possible.

- *the final offer process (stage 2); and*

As discussed above, we are concerned that the final connection offer may be fundamentally different to the indicative offer which has time and cost implications for the generator.

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- *the roles of the generator, the GBSO, and the OFTO in this process.*

We require further clarification on the party / parties whose responsibility it will be to undertake the sea-bed survey. As alluded to earlier in this response, we feel that it is not appropriate for the GBSO to undertake this survey, and that the offshore generator may be more suited to undertake this obligation.

We agree that the connection agreement should remain as a bilateral agreement between the generator and the GBSO.

We concur with the view that the GBSO should collate tender information in a data room following adequate dialogue with the generator.

*Question 2: Do you feel that there is any aspect of the connection application process that we have not considered sufficiently?*

Centrica is concerned that the timescales and obligations for the connection process and tender process are not currently fully aligned. For example, the connection process outlined will be constrained by the tender process timescales and will thus last up to a year. This has implications for the onshore works that the generator is expected to secure. Additionally, it is expected that the developer will have achieved consent for some aspects of the project. In order for this to be achieved, details of the cable route and onshore connection will be required as well as a substantial amount of environmental information to inform an Environmental Impact Assessment. This is not realistic, given the time and costs involved, unless there is an obligation on the OFTO to accept the works carried out by the developer. Clarity is required on the timing and allocation of responsibility of these aspects before they are finally set in the process.

*Question 3: We outline two options for annual tender application windows. Which of the following options do you think are appropriate?*

- *Option 1: A mandatory annual tender application window, to be incorporated into the offshore connection application and tender process; or*
- *Option 2: To rule out an annual tender application window and allow generators to realise cooperation benefits independently and optionally.*

As stated earlier, we do not see the advantage in co-ordination windows as they may impose limits on the level of offshore activity and force delays onto projects eager to connect. The windows will also consolidate the work of the tender panel into certain months of the year. Further, the pre-application process has been designed to allow developers to take advantage of shared connection routes and this should work more effectively than a tender window.

The tender process and the connection application process are intrinsically linked and therefore, the implementation of tender windows, if desired, should not present onshore applicants with an unfair advantage over offshore users.

## Chapter Seven

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*Question 1: Do you agree with our proposals for connection via distribution networks as outlined in this chapter? In particular, we would welcome your views on:*

- *comparable types of connection;*

We support the classification of an embedded transmission connection.

- *charging arrangements; and*

Centrica concurs with the suggestion that both connection charges / DUoS will be payable via the GBSO, however, the proposed charges do not appear to be consistent with onshore arrangements whereby existing schemes only pay connection charges but are not subject to DUoS.

- *connection application process.*

Centrica is supportive of the lines of communication suggested in the policy statement in that it will be the GBSO's role to liaise with the DNOs onshore.

*Question 2: Do you feel that there is any aspect of connection via distribution networks that we have not considered sufficiently?*

It is important that the industry is fully involved in the development and sign-off of legal text and changes to existing industry codes. We believe these changes should be made through the existing industry processes in the interests of transparency.

## **Chapter Eight**

*Question 1: Do you agree with our proposals for charging, access and compensation as outlined in this chapter? In particular, we would welcome your views on:*

- *the development of charging arrangements;*

Centrica has provided a response to National Grid's pre-consultation on the proposals for the offshore charging methodology and eagerly await National Grid's response. It is important to note, however, that some decisions resulting from the pre-consultation may impact the design of the regulatory regime offshore, i.e. re-openers may be necessary from a cost reporting perspective and project specific expansion factors may need to be calculated following the tender process, again forcing a revision of the bid revenue stream, hence the regulatory regime must not be considered in isolation.

- *access products; and*

We concur with Ofgem and BERR's view that the offshore access product should be consistent with onshore arrangements.

- *compensation proposals, particularly whether there should be a penalty only regime in place for the OFTO.*

As an offshore generator, Centrica believes that there needs to be flexibility within the regime to allow developers to design for a higher security standard offshore. We believe

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that this arrangement should form part of the standard regime design and should not sit outside as a bilateral agreement between the OFTO and the generator.

This further strengthens our argument for the generator to have more involvement in the bid assessment process. If a generator is willing to pay more for a different type of cable / circuit, this needs to be reflected in the revenue stream bid by the elected OFTO.

We feel strongly that an OFTO should be incentivised to maximise availability via a penalty payment to the generators to the scale of TNUoS, or a higher figure to remunerate for loss of contribution towards RO targets. This should not be a one-off payment but should continue throughout the outage period in order to encourage timely reparation of faults.

*Question 2: Do you feel that there are any aspects of charging, access and compensation that we have not considered sufficiently?*

No further comments.

## Chapter Nine

*Question 1: Do you agree with our proposals for technical rules as outlined in this chapter? In particular, we would welcome your views on:*

- *security standards; and*

Centrica is supportive of the proposals for the extensions to the GBSQSS, Grid Code and STC.

- *the recommendations for developing technical rules.*

We are satisfied that the technical rules are being sufficiently addressed and look forward to further output from the sub-group.

*Question 2: Do you feel that there is any aspect of technical rules that we have not considered sufficiently?*

No further comments.

## Chapter Ten

*Question 1: Do you agree with our proposals for implementation as outlined in this chapter? In particular, we would welcome your views on:*

- *changes to licences; and*

We support the way forward and await the drafting of the legal text for industry approval.

- *changes to codes.*

As above, we support the proposed changes in principle and would like to be involved in the sign-off process. As far as possible existing industry processes should be used.

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*Question 2: Do you feel that there is any aspect of implementation that we have not considered sufficiently?*

Changes should be kept to a minimum and simplified where possible to avoid extensive, complex and time consuming changes which could cause delays to the implementation of the regime.

## **Chapter Eleven**

*Question 1: Do you agree with our proposed work programme as outlined in this chapter? In particular, we would welcome your views on our proposed approach to industry engagement.*

Centrica would like to see the new regime implemented in accordance with the timescales outlined in this chapter, incurring no further delays.

We are keen for generators and developers to maintain an involvement in the development of the new regime.

*Question 2: Do you feel that there is any aspect of our proposed work programme that we have not considered sufficiently?*

In order to progress the regime according to the desired timescales, we welcome the publication of deadlines for information relating to transitional projects.

Notwithstanding our prior comments on the extent to which the proposed regime will meet its objectives, Centrica welcomes the provision of the additional detail in the latest policy statement but feels that the proposals outlined need to be developed further and should take into consideration the design / profile of existing wind farm developments offshore.

In developing the detail of the regime, Ofgem and BERR should consider the original objectives of introducing a regulatory regime, namely to achieve the most cost effective solution for offshore renewable generation by removing the upfront costs from developers and regulating the monopoly provision of transmission assets, either by reconsideration of the merchant approach or review and simplification of the non-exclusive approach.

If you have any questions or comments relating to this response, please contact me on the number above or at [laura.jeffs@centrica.com](mailto:laura.jeffs@centrica.com)

Yours sincerely

Laura Jeffs  
Commercial Manager

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