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Dear Colin

Offshore Electricity Transmission - a joint Ofgem/BERR Policy Statement consultation

energywatch welcomes the opportunity to respond to the issues raised by this consultation. This response is non-confidential and we are happy for it to be published on the Ofgem/BERR websites.

Consumers expect the delivery of safe, secure and reliable supplies of electricity in an efficient and economic manner. Transmission owners and the GB system operator are under licence obligations to meet these expectations with regard to the transmission network wherever it is situated. Ofgem is under a primary statutory duty to protect the interests of consumers, current and future, through the promotion of competition in generation and supply. We believe that consumers need assurances that Ofgem/BERR will establish a regulatory framework for offshore transmission which meets Ofgem's primary, and some of its secondary, duties and creates a 'joined-up' approach for the onshore and offshore transmission regimes.

We support wider Government objectives to increase the diversity of fuel sources for electricity supply and believe that offshore development of renewable generation is part of that approach. The delivery of offshore generation requires appropriate mechanisms for offshore transmission connections to the mainland. We note the various initiatives underway to reduce barriers to entry to the transmission grid, whether through planning law reform or a more flexible regime for transmission access to optimise the use of existing capacity and ensure that only efficient and economic new capacity is built.

The regulatory regime

We agree that a competitive tender approach for offshore transmission connections could deliver a more efficient regime for consumers. By identifying Offshore Transmission Operators (OFTOs) through tendering, there would be a commitment to develop and build only the capacity that would be required to connect generation projects, limiting potential stranded asset risk. The risk of developing the connection must lie with OFTOs as consumers have no control in this respect.

We agree that OFTOs must be licensed entities. They should have appropriate obligations to ensure they operate according to the relevant rules, and should sign industry codes and agreements to create consistency as far as possible with the onshore regime and allow the future development of market rules. This approach also allows Ofgem to effectively monitor the OFTO's licensed activity and enforce the licence if necessary. This is particularly important should a generator, an OFTO or other licensed entity become insolvent, as the associated risk will lie with end consumers and must be minimised through any energy administration process.

The extension of National Grid's GB system operator (GBSO) role offshore provides both continuity and consistency between the current onshore and proposed offshore transmission regimes. We have no strong views on how a transfer of assets should occur if an OFTO has its licence revoked, other than to note that consumers will require assurances on continuity and a degree of certainty that revocation does not create new financial and security of supply risks.

A regulated revenue stream would create stability and certainty for the OFTO, helping prospective bidders to secure finance; for the generators who will connect in respect of likely network charges; and, most importantly, for consumers about the limit of pass through costs associated with the connection. The tendering process must be robust enough to ensure that only viable projects go ahead. We agree that regular price reviews for OFTOs may not be appropriate but adequate cost reporting may be more effective in keeping OFTO activity under scrutiny and ensuring that additional efficiencies can be passed back to users and consumers.

We believe that, at the very least, there must be ring fencing of funds and activity should an OFTO tender be approved where the OFTO is a generator-affiliate. Our preference is for bidding OFTOs to be completely independent of offshore generators seeking a connection, as unbundling of activities provides the best guarantee of transparent market operation and effective competition.

We support the use of performance criteria when developing any tendering package as it is critical that consumers have confidence in the ability of prospective OFTOs to deliver asset reliability and availability so as to maintain security of supply. The tendering criteria must reflect objectively determined best practice in this respect. After approval of a bid, the OFTO should continue to be monitored. Where performance falls below required standards, penalties should be imposed. Incentives, if used at all, should aim to maximise the efficient and economic use of assets and not reward OFTOs for activity that they ought to ordinarily undertake.

We require further clarity on how 'variant' bids will work, as well as how any bilateral arrangements between the OFTO and connecting generators which differ from existing standards and processes will operate. What would be the implications for consumers - is the purpose of a variation to enhance effective operation and system security? Will it sacrifice efficiency for flexibility? A benchmark level of transmission operation which meets consumers' expectations must be delivered regardless of the potential for variation.

The enduring competitive framework

We note the process which is planned to allow tendering by, and licensing of, a prospective OFTO as outlined in the document. We agree that the process should not be stretched out over a long period, should be flexible as necessary, and that the proposed four stages for tendering are a good starting point. The use of expressions of interest and pre-qualification should assist in filtering out unsuitable candidates early on. In a similar way, it is appropriate to coordinate the application by, and issue of connection offers to, offshore generators by the GBSO with the tendering process to optimise decision-making and development of the infrastructure.

We accept the role envisaged for Ofgem in terms of running the tendering process. We are concerned about the resource implications however. Ofgem should apply sufficient resources towards a robust process which does not detract from its other activities which are intended to meet its primary statutory duty to protect the interests of consumers. Some assurance will be required through ongoing discussion and debate about how Ofgem intends to tackle this area of work.

Transitional arrangements

We note and support the approach to be applied to offshore generation projects which are already, or will be, in the pipeline prior to the introduction of enduring arrangements. By setting out the framework and the timetable for 'go active' and 'go live' now, the developers involved will be given comfort and certainty about how the adoption of assets by an OFTO will occur and on what basis.

We also believe that offshore developers must bear an appropriate share of the costs of development and should limit the risk of leaving stranded assets for adoption. Consumers are not in a position to manage this risk at all although they will ultimately pay for the connected assets to whatever extent they are used. Developers should only be able to recoup costs associated with an efficient investment in such assets. Similarly, any incremental costs which enhance the level of security provided by the connection should be borne by the developer. Consumers are in no position to determine whether additional costs are necessary or not.

As with the enduring process, we agree that the tendering process for appointing OFTOs for transitional phase projects is appropriate. Maintaining a high level of consistency of approach and robustness is necessary for both processes, whilst ensuring that any appropriate differences are recognised and reflected. Where no OFTO is appointed, we agree that the developer may become the 'OFTO of last resort' but consumers require assurance that the developer has undertaken the connection project efficiently and not increased risks to consumers of stranding.

Other comments

We note the proposals to extend distribution licensing and agreements to define contractual relationships, and the treatment of offshore connections as similar to the connection of large power stations to the distribution networks. We agree that a suitable governance regime is required to ensure that there is a measure of control

over how connection and charging processes are established and changed going forward in response to future developments. However, wherever the governance arrangements sit, all affected licensees must work together to ensure that there is efficient and effective coordination to deliver offshore electricity in line with consumers' expectations.

We agree that National Grid, as the GBSO, has a key role in establishing charging arrangements for offshore connections. We would look to the GBSO to deliver consistent and coordinated charging methodologies which ensure that only efficiently incurred system operation costs are recovered from users and consumers, whilst minimising the impact of any actual differences between onshore and offshore connections. The development of access products for offshore transmission must ensure efficient use of the connection when it is available. Availability must not be constrained off if it would contribute to safe, efficient and economic system operation by the GBSO.

We agree that Ofgem is best placed to coordinate all the relevant licence and code changes required to facilitate the successful creation of the offshore transmission regime, ensuring that there should be consistency for offshore and onshore transmission as far as practically possible. This document has set out a number of issues that require further consideration and so the timetable is quite challenging. Ofgem must ensure that delays, if any, to implementation of the regime are kept to a minimum to allow the optimal development of offshore networks to meet consumers' expectations.

Going forward, we will continue to keep these issues under review as and when they are raised, always considering the possible impact on consumers.

We would appreciate being kept informed of the progress of the consultation and hope to engage further with Ofgem and BERR through any planned external communication sessions in the future.

If you do wish to discuss our response further please do not hesitate to contact me on 0191 2212072.

Yours sincerely

Carole Pitkeathley
Head of Regulatory Affairs