



*taking care of the essentials*

By email  
Sam Cope  
Ofgem  
9 Millbank  
London  
SW1P 3GE

Millstream East  
Maidenhead Road  
Windsor  
SL4 5GD

Tel. 07789 577609  
Fax (01753) 431150  
[www.centrica.com](http://www.centrica.com)  
Thursday 18 December 2008

## **Offshore Electricity Transmission – A further Joint Ofgem/DECC Regulatory Policy Update**

Dear Sam,

Centrica welcomes the opportunity to respond to the Offshore Electricity Transmission further Joint Ofgem/DECC Regulatory Policy Update. This non confidential response is on behalf of the Centrica group of companies excluding Centrica Storage Ltd.

The consultation document has provided significantly more detail and has addressed certain areas where Centrica has previously identified issues. We would like to thank Ofgem and DECC for the extensive work to date and significant progress made since the last consultation.

We note your request for any material comments by 18 December 2008, with a full response by 9 January 2009. As Centrica is both an Offshore Wind Developer and an international energy business with upstream, midstream and downstream interests this consultation is extremely important to our future business plans. To fully understand the impacts on our business we need to review, in detail, all aspects of the extensive consultation and gather information from a number of critical internal parties. Thus these deadlines are challenging.

However, Centrica remains committed to the Offshore Regime, and in order to assist Ofgem and DECC in its development, we have provided our initial view of some material issues below. We do not wish this to preclude the raising of any further material issues in our final response by 9 January 2009.

Our initial material comments are as follows:

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## **Developer involvement in the appointment of an OFTO**

Ofgem and DECC have asserted that the Third Package of EU legislation will exclude generators from owning offshore transmission assets. Whilst the exact detail of ownership is uncertain and will be subject to legal interpretation, this should reduce concern about developers being involved in the OFTO selection process. We would support Ofgem giving developers sight of the bidders invited to tender and their resulting bids such that the developer can provide valuable advisory input in the selection of the preferred bidder.

Where the developer does not support the selection of the preferred bidder there would be benefit in having some means by which to appeal to Ofgem in certain circumstances. This could avoid situations arising where an OFTO has been appointed and in which the developer does not wish to accept the amended connection agreement, resulting in potentially costly legal routes. An appeal could for example, be allowed in such circumstances where the developer can provide evidence that the selected bidder is not of appropriate standard. The generator and OFTO will be forced into a long term relationship and it is essential that good working relations can be developed.

A developer should also be able to appeal where they can provide evidence that the revenue streams do not appear to be efficient. As developers (particularly in the transitional regime) could be able to estimate an appropriate revenue stream, having such an appeals mechanism could prove beneficial to ensure that the generator, and ultimately the consumer, gets the best value out of the regime. Such evidence could result in Ofgem entering into further negotiations with the preferred bidder.

## **OFTO of Last Resort**

The purpose of having an OFTO of Last Resort mechanism is to ensure that a generator is never left stranded. Paragraph 2.32 indicates that under the OFTO of Last Resort mechanism (for transitional projects) TO's would be 'invited to submit proposals to Ofgem for taking over the transmission assets in question'. It is not clear what would occur if no TOs accepted that invitation and what powers of compulsion Ofgem could enforce. Unless there is an obligation to submit proposals, there remains a risk of the developer being left with a stranded asset. Additionally, it is not clear what would be contained in these proposals by the TOs and what requirements will be set by Ofgem. If they are substantially less onerous than the tender process then there is an incentive for TOs to bypass the tender process (taking the risk that others will do the same) and then submit proposals for the OFTO of Last Resort process.

Notwithstanding the concern raised regarding the exact make up of the OFTO of Last Resort process, we believe these can be overcome. We welcome the proposal for an OFTO of Last Resort process in the event of abandonment. We continue to believe that an OFTO of Last Resort process in the enduring regime for new builds would be beneficial to provide investors with confidence that projects will not be unduly delayed and will be provided with connections to the onshore transmission system. This would assist in achieving the 2020 government renewable targets.

## **BM Unit configuration**

It has come to our attention that the regime could result in an undesirable and inefficient BM Unit configuration. We believe that, due to the definition of the OFTO boundary as the

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low voltage side of the offshore substation, this has impacts under the BSC. Consequential changes to Section K of the BSC should be considered.

The Transmission System Boundary Point will be close to the wind farm – potentially on the offshore platform. It is therefore feasible that the BSC, as currently drafted, may require the generator to register multiple BM Units where it would actually more efficient for both the party and National Grid to register a smaller number.

As a potential solution, changes could be made to the definition of Power Park Module to allow for the possibility of multiple Boundary Points being registered as a single BM Unit. Whilst it is theoretically possible to apply within the BSC for a non-standard BM Unit configuration, the use of these provisions for new projects does not give the developer sufficient certainty at the appropriate time to be able to design and build assets in the most efficient manner. A potential compromise solution is that the burden of proof should be shifted to National Grid to determine why an offshore wind farm could not have a single BM Unit rather than the registrant having to show that it should.

### **Performance Incentive**

We support how the banking mechanism suggested for the performance incentive seeks to provide the OFTO encouragement to exceed the 98 percent performance target. The benefits of exceeding this target can be substantial so we welcome this symmetrical element. The detail of the incentive is therefore very important.

We believe that it is perverse that performing well in one year should allow for poor performance in future years. Wholesale prices can vary significantly from year to year, so it is of no benefit, for example, if the OFTO performs well in three years of benign prices, banks credits, and then performs poorly in a year of high prices. We would like to see an incentive regime that maintains a high availability percentage.

The banking mechanism is purely a way of spreading the 10 percent OFTO revenue stream that is at risk over the entire 20 year period. Given the 10 percent cap of revenue that is subject to this incentive, this effectively gives a £x million figure over the 20 years at risk. Therefore a performance incentive that uses this £x million as both the upside and downside could be considered.

We also believe that the period of a year for each incentive period is too long and would prefer this incentive to be on a more regular (for example, monthly) basis to ensure the incentive is ongoing.

We acknowledge that maintenance requirements in any individual year may vary (for example, more significant planned outages typically occur on a four or five year cycle). Therefore, we suggest that bidders outline their planned maintenance during the tender process, and subject to generator agreement, this is excluded from the performance incentive. This would enable a higher availability performance level in excess of 99 percent.

We have had some initial thoughts on a variation to the banking mechanism that would include the above elements and could be considered by Ofgem. We intend to provide further detail and an example in our 9 January 2009 response.

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## **Construction Securities**

We are concerned that Ofgem have reduced the security required from OFTO's for the risk of abandonment during construction from 100 percent to between 15 and 30 percent. It is not clear who Ofgem intend to have bear this risk. The reason that has been given for the reduction is to ensure that investors are not deterred. This would not be consistent with the 100 percent security that the generator has to post when signing a connection agreement. Centrica would support the use of a sliding scale for OFTO security.

## **Other areas for comment by 9 January 2009:**

We have provided an indication of the initial material concerns that are apparent to us at the time of writing. We are still evaluating other areas in which we are likely to provide comments by the final deadline of 9 January 2009. These are likely to include (but are not restricted to) the following areas:

- The Revocation Mechanism;
- Late delivery of Onshore – liquidated damages;
- Extending/retendering after 20 years;
- EU unbundling implications;
- Delivery Incentives;
- The impact of the proposed change to transmission charges;
- Alignment and co-ordination of the various construction elements;
- Increases in capacity over 20% - whether to index this, and the need for generator agreement
- How will the regime create incentives create appropriate strategic planning for zones with multiple sites?
- OFTO insolvency and how it is replaced;
- Unknown unknowns – IAE provisions should be symmetrical;
- Known unknowns – preference for partial indexation;
- Do OFTO's require compulsory purchase rights?
- How to manage integrated transmission and generation assets in the transitional arrangements;
- Disclosure and warranty obligations for the data room;
- Details on how the RAV will be calculated;
- Exit arrangements;
- The drafted changes to the Codes and Licences; and
- The cost recovery of tenders.

Finally, we would like to reiterate our thanks to Ofgem and all other parties contributing to the policy update. We will provide our full material response by 9 January.

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

Yours sincerely

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*By e-mail*

Chris Stewart  
Commercial Manager  
Business Development  
Centrica Energy

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