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Dear Duarte and Robert

Offshore Electricity Transmission

Thank you for the opportunity to comment on your Regulatory Policy Update document as issued on 20 November 2008. This response is made by DONG Energy A/S and contains our further comments.

DONG Energy would like to reiterate its concern that the central proposal for the enduring regime, where OFTO tenders are conducted prior to construction, will likely lead to delays and increased costs for the development of offshore wind. The proposed termination rights in the offshore construction agreement add to our concern in this area, as the drafting proposed is less flexible, and with additional termination rights for NGET, when compared with the equivalent onshore agreements. We comment on this in more detail in Annex 2, but note at this stage we would have thought that approach should have been to offer the generator *more* flexibility in terms of programme revisions given that the OFTO tender process increases the overall development period and will be to a large extent outside its control.

Besides the responses attached we would like to comment that the Revised Regulatory Impact Assessment appears overly optimistic on the benefits of the regime. Our view remains that even over the longer term, the requirement for OFTOs to construct the transmission assets will increase risk and timescale of developments, hence increasing cost overall. We also note that the calculations do not take into account the cost of the Renewables Obligation.

We note the assessment of Ofgem and DECC that the regime will impose costs of £10 to £15 million *per project* on existing developments. DONG Energy has yet to determine its view on the appropriate figure and would request that Ofgem and DECC provide further details on how their estimate was arrived at, to ensure that we are comparing like-with-like. We would also like to understand from Ofgem and DECC how an existing or under construction project is going to be able to recoup such a sum, as the benefits of the OFTO regime, as stated in the RIA, appear to be mostly arise for future projects and/or the wider economy. This is particularly of concern to licence exempt projects that also stand to lose material sums from the loss of some or all of the embedded benefits they would currently enjoy.

Yours sincerely

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Annex 1: List of Questions and Answers

Questions - Chapter 2

We seek respondents' views as to our revised approach to the OFTO of last resort mechanism

DONG Energy regards this approach as rather undesirable in that it forces an existing TO to take on a role that it either did not wish to do (ie because it did not bid in the first place) or because it was not the best bidder (when it did bid but its bid was not accepted). We also believe that if such a provision is used for the first transitional tender, the only viable person to take on such a role is NGET, as the other existing TOs (SHETL and SPTL) would presumably be debarred under the anticipated Third Package reforms.

Instead DONG Energy thinks that in the short term it would be more appropriate to ask the secretary of state to issue to the generator an Transmission Licence exemption under section 5 of the Electricity Act to allow the generator to continue to function, with a view to rebidding the assets in the next available tender round.

Furthermore, if on a rebidding situation, or if this mechanism has to be used for more than one project, we would suggest this shows a rather fundamental problem with the proposed design of the Offshore Regime and would propose that this trigger reassessment of the whole approach.

We seek respondents view on the drafting of the licence condition that reflects our updated policy (see separate annex 1)

We have no comments on the drafting as we do agree with the proposed approach.

Questions - Chapter 3

We would welcome views on our approach to the following issues:

Extending or re-tendering licences at the end of the 20 year revenue stream – what are your views on the proposed options?

*DONG Energy remains of the view that a 20 year revenue stream is too short and discriminates against offshore generators as onshore, the **transmission asset life** is what determines the period of depreciation, and not the connecting party's asset life.*

Of the issues presented we note the omission of consideration of the value of deferral of decommissioning costs. Over the 20 year life the generator will have paid for not only the construction, financing and operation of the assets, but also funded the decommissioning costs. In the event that there is extension of the License or retendering for future use of the assets, credit should be given from the original OFTO to the generator or the new OFTO, in a sum representing the avoided or deferred decommissioning costs.

Indexation and adjustment of the revenue stream – do you have comments on our proposals in respect of: - Inflation? - Refinancing? - Business rates and licence fees?

DONG Energy favours OFTOs being exposed to less, rather than more, risks that are outside of their control, as otherwise the cost of such risks are likely to fall back on the generator as “risk premia”. Allowing the tenders to take place during construction, with the asset being transferred afterwards, would avoid the need to factor in the benefit of post-construction financing (which could be substantial, but is extremely hard to value and predict).

What are your views about dealing with the late delivery of onshore reinforcement works by onshore TO/DNOs through a liquidated damages provision?

We understand that liquidated damages, to the extent that they exist at all in the current regime, are typically set at levels too small to have any impact.

How can our detailed proposal on the availability incentive be further refined and improved?

Per our previous comments on this issue, the penalty needs to be much larger, and the initial availability target should be higher.

How should Ofgem appropriately respond to persistent poor performance by an OFTO, and how should any revocation mechanism be designed?

Revocation of the licence should be accompanied by temporary licence exemption to allow the generator to operate the assets until a new OFTO could be appointed.

What are your views on our proposal to manage the risk of OFTO abandonment through the OFTO of Last Resort scheme and construction securities?

DONG Energy does not see how these proposals “manage the risk”, rather the developer should be given the opportunity in the enduring regime to construct the assets and then transfer them to an OFTO post completion.

Questions - Chapter 4

Does the drafting in the annexed codes accurately reflect the policy positions set out in this document?

The CUSC drafting (at Exhibit B, the BCA application form) implies that entry into the enduring tender process requires a project to have submitted a section 36 application, we were not aware that such a decision had been made.

The Grid Code drafting (at BC1.42(a)(ii)) states that PNs are required from Small Power Stations where connected to offshore transmission systems. We were not aware of a policy decision to require this, nor of the possible system needs given the de-minimis nature of such stations (ie under 10MW) which, to be connected to the transmission system at all must be part of a much larger offshore generation development. This appears to impose unnecessary costs on such power stations.

DONG Energy does not agree with the statement at section 1.17 of the GBSQSS “the offshore generator’s circuits cannot be at a voltage level of 132kV” and does not believe that it is consistent with earlier policy decision to allow “customer choice” in terms of the boundary point between an offshore generator and an OFTO. DONG Energy does not agree with the following statement that “such circuits would then constitute part of an offshore transmission system”. According to the current Grid Code drafting an Offshore Transmission System is “a system consisting (wholly or mainly) of high voltage electric lines owned or operated by an Offshore Transmission Licensee and used for the transmission of electricity from one Power Station to a sub-station or to another Power Station or between sub-stations ...”

Were the ownership boundary set (for example) on the high voltage side of a 33/132kV transformer that transformer and any small length of 132kV line and/or busbar would be part of the power station and not a transmission system. This seems exactly the same as exists with onshore power stations where the 275kV or 400kV transformers (and 275kV or 400kV generation circuits) may be owned by the generator. We are not necessarily arguing that the whole of the export cable should be treated as part of the power station (although we are aware that this is a position that could be taken). Rather, we wish to ensure that the option remains of placing the generator/OFTO boundary at the 132kV side of the offshore platform. We do not agree that any offshore assets at 132kV are automatically “transmission” as this does not accord with the Electricity Act definition, which refers to a system consisting wholly (of mainly) of high voltage lines and electrical plant; such a generators would own a system comprising substantial distances of 33kV lines, and very little 132kV lines, so it would still be mainly 33kV lines and electrical plant.

Furthermore, we had always understood that the ownership boundary could be at the 132kV level (or higher), see the following extract taken from the Revised Final Report of the Grid Code Subgroup “Recommendations for the application of Grid Code technical requirements to Offshore Electricity Transmission Networks”: “In line with the GB SQSS subgroup the group initially assumed that the Offshore Grid Entry Point would be at the disconnecter on the busbar side of the circuit breaker on the LV (likely to be 33kV) busbar on the outgoing windfarm circuits on the offshore platform. However following discussion within the group it was agreed that Offshore Generators should have the option to connect to an Offshore TO at a voltage level of their choosing (e.g. 33kV, 132kV 220kV). Therefore it is important that any recommendations made by the group are applicable to generator connections at various voltage levels” .

DONG Energy has not made any final decision on how the ownership boundary should be set on its transitional projects, but one option being considered is to have the OFTO ownership to start at the sealing end of the export cable as it leaves the Offshore Platform. We understand this arrangement is being adopted for offshore projects in Germany and we trust it will also be available in the UK.

For information we consider a boundary point at the 33kV feeders operationally undesirable and also understand from discussion with NGET that each feeder would need to have separate boundary point metering which would be rather costly under some configurations, and under all configurations will increase costs to some extent.

Are there any other modifications which you consider appropriate for implementing the new regime?

In the Grid Code (at GC4.3) the Panel consist of a specified number of members including just one person representing those Generators each having Large Power Stations with a total Registered Capacity of 3 GW or less, whereas there are three persons representing those Generators each having Large Power Stations with a total Registered Capacity in excess of 3 GW. As the offshore definition of Large Power Station is now just 10MW, it is likely that there will be many more persons in this category and the representation should be increased to at least two. Alternatively a new category should be created ie a person representing those Generators each having Large Offshore Power Stations, and such persons excluded from the "Novel Units" representation.

More generally, we wonder if any provision are needed in the CUSC, BSC or elsewhere to deal explicitly with transitional projects; as written the drafting all appears to be about the enduring regime, it is not clear how those projects under construction as at Go Live will be dealt with in the period up until the OFTO takes ownership of the transmission assets. In particular, how will commissioning power be dealt with in terms of a) exports through the offshore cable being an illegal "transmission" activity; b) registration under the CUSC and BSC of the offshore meter(s) and the onshore meter; and c) bids and offers into the Balancing Mechanism. In addition, existing construction contracts will no longer be consistent with the standard form of agreement in the CUSC, does it not need to be explicitly stated that these will continue in their existing form until the works are complete?

Annex 2: Detailed Comments on the Code Modifications

1. Consolidated Transmission Licence

In the definition of “incremental investment threshold” the term “original investment cost” seems rather vague. Also it is unclear if or how this term should apply to licensees who have acquired assets from a developer under the transitional regime.

2. BSC

As mentioned in our letter dated 18 December 2008, in order to clarify the treatment of existing offshore generators that will become connected to Offshore Transmission Systems and which are exemptible, add, at the end of section K4.7.2b) “For the purposes of this paragraph, an Exempt Export BM Unit that is connected to an Offshore Transmission System, which is in turn connected to a Distribution System, is considered to be in the GSP Group that includes that Distribution System”.

3. CUSC

Main Text

We note that under Paragraph 2.13.10, NGET will have the right to terminate the BCA “in the event that the Authority notifies The Company that the Offshore Tender Process is not being progressed”. Can you advise under what circumstance such notice would be given, it appears rather a vague term, it is important for the confidence of investors that key contracts will not be terminated unilaterally. There may be good reasons why the tender is not being progressed at any particular time, including that the requested date of entry into the tender process (as per CUSC Exhibit B) has not yet occurred. See further comments on this issue below.

For clarity, it is suggested that in the definition of “Onshore Construction Works” the words “connecting Offshore” be added after “User”.

Exhibit B (Application Form)

It is noted that in section 8 of the “notes” there is a carve-out from the general provisions of Paragraph 6.10.3. Should there not be a corresponding amendment to 6.10.3 to this effect?

In section 11 of the “notes” it is suggested that the following be added: “The Company’s Offer will however set out those assumptions”.

In section 11 of the “notes” it is stated that a precondition of Entry into the offshore Tender Process is that the Applicant will have initiated the consenting process under section 36 of the Act. We were not aware of this requirement from previous consultations.

In section 12 of Exhibit B it is stated that the applicant should advise the year of entry into the offshore Tender Process. As Ofgem/DECC are now indicating that a more flexible approach is to be taken in this regards it may be more applicable to say something like “the earliest date the application would wish to enter the offshore Tender Process”. However, we note that later in the application form (section D) this information is requested again in the form of “Expected date of entry into the Offshore Tender Process”.

Exhibit C (Offer)

We recall that in the workshop on “Getting Connected”, NGET advised that they would be providing in the data room for OFTO bidders, both the Offer and “options that were considered but ruled out”. We consider that this information should first be made available to the applicant as part of the Offer. It should therefore be included in CUSC Exhibit C.

In section 8 the words in brackets at the end appear superfluous.

Schedule 2 Exhibit 1 (BCA)

Clause 10 needs to be reworded to clarify that the Maximum Export Capacity (as measured on shore) may be less than the TEC (as measured offshore) and the restriction on availability should only bite when the exports (as reduced by losses through the offshore transmission system) exceed the MEC. Further, as the MEC is set in relation to the OFTO/DNO interface, where there are more than one offshore generator exporting through the same ET Interface Point, the restriction should only bite to the extent that the sum of the exports from both or all stations exceed the MEC. In terms of drafting, DONG Energy would not object to the MEC being expressed on a pro-rata basis in each User’s BCA provided that it was clear that any one generator could use any part of the MEC allocated to another User if that User was not using it.

The amendment to clause 12.4 (allowing NGET To unilaterally vary Appendices F1 to F5) does not appear to be an appropriate as it is not in itself required for the introduction of the offshore TO regime (or if it is why should it be applied to all BCAs and not just offshore ones?)

Schedule 2 Exhibit 3A (Construction Agreement)

Why is the second part of recital B deleted?

Clause 1.2.3 we think there should be a reasonableness test here and therefore propose to replace “shall include such terms and conditions as The Company in its absolute discretion requires as a consequence of such amendments” with “shall include such terms and conditions as The Company reasonably requires as a consequence of such amendments”.

Clause 1.3, DONG Energy is strongly opposed to the termination provisions contained here. Under on-shore construction agreements generators will have given their best estimates of their programme and have the opportunity to Mod App completion dates subject only to the

backstop date which can anyway be varied subject to NGET's discretion. In order to prevent unreasonable capacity holding NGET has the new powers under CAP 150 to reduce TEC if a User does not make the necessary Mod Apps of its own volition. In the offshore environment we do not see why additional termination rights should be added, even if subject to "confirmation from the Authority". Unless developers are to wait until all other aspects of the project are certain before submitting for Grid Connection, certain assumption will have been made about the timing of critical matters including consents. These assumptions will be set out in the proposed programme, including the intended Tender Process start date. In the event of delays, the User will want to postpone its completion date and programme, it will not want NGET to cancel the agreement with consequent liabilities for Cancellation Charges or Final Sums. Furthermore, as written, termination could arise under 1.3.1, 1.3.3 and 1.3.4 for no fault of the User and termination would not be an appropriate penalty. We consider that the provisions in 1.3 should instead be addressed by giving NGET a right to defer the Completion Date in the event that no OFTO is appointed (or can reasonably be expected to be appointed) by the date set out in the Construction Programme. It should be noted that if these termination rights are not changed, it may lead to developers being overly cautious in their assumptions and thus potentially delay their projects in the event that everything proceeds to plan.

Clause 1.4, we are unsure what this clause is intended to do, at the start of the tender process, either the Users Data will remain valid or it will have changed. We would prefer to see a rather more "positive" clause along the following lines: "In the event that the User becomes aware prior to the start of the Offshore Tender Process that the User Data is no longer correct, the User shall resubmit the same to the Company. In such event, The Company shall be entitled to make such changes to the Completion Date and the Construction Programme as is reasonable in the light of the change, including for the avoidance of doubt a change to the Assumed Offshore Tender Process Start Date."

Clause 2.2 we note that NGET will no longer be seeking consents for the onshore works until after appointment of the OFTO. We consider that NGET should nevertheless commence its onshore consent works ahead of this if required by the programme. This is best done by retaining the existing clause 2.2 but making it in respect of the Onshore works only, then adding a new clause to deal with the Offshore Works (although we recognise that in practice developers are likely to seek to obtain the necessary offshore consents with a view to minimising the delays caused by the OFTO Process).

4. DCUSA

No comments

5. Distribution Code

Our only comment is that the "Guide to the Distribution Code" should be updated to reflect the introduction of the OTSO and embedded transmission.

6. Grid Code

Definition of “Control Point”. We note that the last paragraph states “For a Generator this will normally be at a Power Station but may be at an alternative location agreed with NGET”. Offshore generators will not generally be controlled from the power station and we don’t consider that in every case we should have to agree with NGET that location (it is after all, a matter of fact as to where the generator is controlled from). We therefore propose to add “Onshore” before “Generator” and then add the following new text: “For an Offshore Power Station this will be at the location advised to NGET by the Generator”.

In the definition of “Offshore Transmission System” change “one” to “one or more”.

In the Connection Conditions we note a number of obligations (such as CC6.3.2, 6.3.4, 6.3.8 and 6.3.15) have been changed such that the existing obligation becomes applicable only to On-shore generators, as new sections were added for Off-shore generators/power park modules. However these are only applicable for transmission connected plant since the terms explicitly reference the “Interface Point” or the “Offshore Grid Entry Point”, neither of which exist for 33kV connected offshore wind farms. Large or Medium Power Stations located offshore and connected to shore by assets operating below 132kV should have to comply with the original obligations (subject of course to any derogations).

7. STC

In clause 4.1.4 the expression “the notice from the Authority” is used but this is not defined.

8. GBSSQSS

As set out earlier, DONG Energy does not agree with the statement at section 1.17 “However, the offshore generator’s circuits cannot be at a voltage level of 132kV or above since such circuits would then constitute part of an offshore transmission system”. This should be deleted.

Table 8 on page 46 should be labelled “8.1” and “10.1” is missing from the Table on page 50

Appendix A section A.11. DONG Energy remains of the view that the double busbar design is not appropriate offshore on the grounds of cost (taking into account offshore platform design considerations); we are also concerned about the operational reliability of such arrangements. However, our current intention would be to designate an ownership boundary such that the busbars were owned by the offshore generator and thus fall outside the ambit of the GBSQSS.

9. Special Licence Conditions

No comments