

Warwick Energy Limited

Comments on Ofgem Consultation Document 21/09 Offshore Electricity Transmission: Updated Proposals for the Competitive Tender Process 5th March 2009

Scope

This document summarises Warwick Energy Limited's (Warwick's) comments in response to the Ofgem Consultation Document 21/09 and associated Appendices and Annexes.

Warwick notes in particular that a number of comments made in response to the earlier tender process proposals (Ref: 142/08) have not been addressed in the present proposals, but remain equally valid. As such Warwick requests Ofgem revisit this earlier response.

The present response should be considered along with the associated covering letter and comments already submitted by Warwick in response to earlier Ofgem consultations on Offshore Transmission.

Detailed Comments

Comments are detailed below against the following sections as per the structure of the consultation document.

Summary

The diagram of the proposed process is a useful addition to the documentation. The splitting of the initial stages of the process into a pre-qualification and qualification to tender appears a welcome improvement. This should help ensure that more appropriate bidders are likely to reach the ITT stage. The requirement to nominate which projects are of interest at the pre-qualification stage appears unnecessary. The overall level of detail required in the 2 stages appears over complex and some of this material would be better covered at the ITT stage.

The period taken by the pre-qualification and qualification stages still appears over long in comparison to the overall timescale of 12 months to license award. The subsequent 6 month period for bidders to develop a viable technical solution and obtain prices from the supply chain, plus Ofgem to assess the tenders and select a preferred bidder appears unrealistically short – particularly in the enduring regime. It appears extremely unlikely that an optimum design or proposal can be developed in this time. This is therefore likely to add unnecessary costs to the OFTO network to the detriment of generators and wider system users.

Section 2 Introduction

Item 2.3

It is not clear why the OFTO of last resort should be restricted to a TO company. EU Unbundling appears to allow for ownership of transmission networks by generators until at least 2012. It would be beneficial if developers of transitional projects had the option to become OFTO of last resort for their own projects. This would minimise the potential detrimental effect of changing ownership during the critical construction phase of many of the transitional projects. The possibility of developers becoming OFTO of last resort should be re-examined and included within the new regime.

It also remains unclear as to why there is no OFTO of last resort in the enduring regime. This omission means that offshore projects are discriminated against in comparison to onshore projects – since there is no guarantee of a connection being provided by the competitive tender process. In contrast onshore projects are guaranteed a connection since the onshore TO (and DNOs) have a license obligation to connect projects. This aspect of the enduring regime should be re-examined in the light of non-discrimination requirements placed on Ofgem and TOs.

Item 2.6 (End of the Revenue Stream)

The treatment of the OFTO at the end of the 20 year license period is unclear. As noted in response to previous consultations it is likely that the OFTO assets will be required on an on-going basis beyond the 20 year period since Offshore sites are relatively scarce and new sites will be expensive to develop. The 20 year right down of costs will also act as a barrier to offshore developments in comparison to the 40 year period used for Onshore projects. This approach is discriminatory and will tend to prevent projects coming forward.

At the end of the 20 year license period Ofgem indicates that *“The Authority would make its decision on the ongoing regulation of the transmission assets before 20 years had lapsed, based on the ongoing demand for the asset.”*

This introduces uncertainty regarding timing of this decision and lack of transparency which OFTOs will need to account for in their proposals. This is only likely to increase costs for all concerned. The issue of decommissioning is also relevant to this since OFTOs are required to include decommissioning costs within bids. Given that the OFTO has no control over when decommissioning will occur it is difficult to see how these costs can be fairly accounted for without the OFTO enduring undue risk.

Furthermore the approach does not provide an incentive to the OFTO to maintain assets adequately towards the end of the 20 year period. Indeed to minimise costs, and improve the chance of winning the tender, this will be a perverse incentive for potential OFTOs to cut maintenance in the final years of a project. This appears to be a flaw in the proposals which should be addressed.

Item 2.7 Adjustments to the Revenue Stream

Warwick believes that some event specific re-openers should be available to adjust the revenue stream. These should aim to reduce risk to the OFTO thereby reducing costs for generators and wider system users. Examples where it does not seem sensible or desirable to cover risk by insurance or other risk mitigating measures include for instance changes to Health and Safety Legislation, code changes and type faults on equipment such as switch gear. For OFTOs there is no means within the proposed Offshore regime of mitigating against such risks - and there will therefore be a potential cost premium into the revenue stream as a result. Warwick believes that there should be a mechanism introduced to allow recovery of a range of specific and pre-defined unknown costs.

In all the above cases onshore TOs can make representation for funding to Ofgem as part of the Regulatory process. A similar mechanism should be in place for OFTOs. The present proposals are clearly discriminatory against Offshore projects and will tend to increase OFTO risk – and thence cost.

Item 2.8 Adjustments to the Revenue Stream

Warwick supports the inclusion of some form of indexation to reduce risk to OFTOs. However it is not clear that simple RPI indexation for a 20 year period is the best way of doing this. Warwick notes that onshore the basic indexation is subject to adjustment as part of the 5 yearly Regulatory Review process. It would seem reasonable to include such a mechanism for OFTOs since RPI may not be the most efficient or realistic means of

indexation – variations both above and below this level may be more appropriate throughout the 20 year license period.

The previous consultation included the proposal to allow the Authority the right to review the level of the revenue stream at predefined intervals over the license period, which was a welcome new proposal; i.e. this is an approach more in keeping with Onshore Regulatory practice. However it is unclear whether this mechanism is still included in the latest Regulatory update. The proposal requires further explanation/ development to clarify this before the new regime is put in place.

Indexation should help reduce OFTO risks and therefore reduce costs to generator and wider demand customers. However the proposal that indexation should be the only means of managing the cost of unknowns is unlikely to minimise overall costs – and is inconsistent with Onshore regimes.

Warwick agrees that utilisation of existing assets to allow connection of additional generation may be preferable to significant additional investment. However if network reinforcement is required it appears unlikely that the 20% cap on additional cost will allow the existing OFTO to carry out the necessary system extension. This will lead to the need to carry out a costly re-tendering exercise. It also does little to foster co-ordinated system development. Warwick continues to be opposed to the 20% cap on investment – the real test should be whether the network extension proposed by the existing OFTO is economic and efficient.

The proposals for possible claw back of re-financing gains (or indeed losses) are not clear and require further detail before it is possible to comment in a meaningful way. It is clear that for a 20 year license period re-financing could lead to major cost changes which could not be predicted at the time of the tender. As such a suitable means of cost sharing of such cost changes should be included in the overall proposals in a consistent and pre-defined manner. The uncertainty and possible inconsistencies created by the current proposals should be removed – otherwise there is a risk that some projects will be treated differently from others and hence be subject to discrimination.

As noted elsewhere the costs that OFTOs should allow for decommissioning may well be unrealistic since the decommissioning time is subject to decision by Ofgem and the future plans of the generator (or possible future generators). It appears more logical to ring fence decommissioning costs so that these can be removed from the revenue stream if necessary at a later date; for instance in the event that the OFTO license is terminated and awarded to a new OFTO after the initial 20 year period.

Code Changes – Warwick welcomes the introduction of a symmetrical adjustment mechanism for changes to revenue as a result of STC changes. This principle should however cover changes to all relevant codes such as Grid Code GBSQSS etc.

Item 2.12

The proposal to introduce a performance bond will have limited effect in preventing an OFTO from potentially neglecting assets towards the end of the license period. This is because it is likely that any neglect of assets in the final years of a license period will not become apparent until after the 20 year period has passed. Hence as this will be in a new license period it will be the incoming OFTO as well as the generator that suffer the adverse consequences and not the original OFTO. If the original OFTO re-bids for a license extension then any necessary premium to account for O&M neglect in the final years can easily be built in – leaving the OFTO with a clear financial benefit at the expense of the generator.

Item 2.33 Risk

The suggestion by Ofgem that a long term Regulatory Regime with predefined revenue adjustment mechanisms reduces risks to the OFTO does not appear credible. Offshore transmission is a new and emerging industry. The requirement on OFTOs to bid for a long term license in a rapidly developing industry is inherently high risk. This is likely to be reflected in inflated bids from potential OFTOs. The simultaneous development of a new form of Regulatory Regime at the same time adds further to this risk. It remains unclear why the obvious alternative of long term licenses with periodic Regulatory Review – as per the onshore approach – has been ignored. Warwick continues to believe that the proposed OFTO appointment system and Regulatory Regime will add risk and complexity to projects, delay schemes that do proceed and add risk and therefore cost to OFTO bids. All the consequences are contrary to Government stated aims. As such Warwick believes a fundamental review of the entire Regulatory proposals should be carried out.

Section 3 Update on Transitional Projects

Item 3.2

The process that applies for transitional projects that are mid construction at the Go Live date remains unclear. Item 3.2 indicates that the transfer to the OFTO will occur post-construction. However it is likely that projects may be at the commissioning stage at Go Live and therefore will be unable to complete construction without an OFTO License - since transmission at 132kV and above will then be a prohibited activity. It appears sensible to allow the developer to initially run the transmission network during this vital stage of project development. Warwick requests clarification on whether this will be possible post Go Live date – and if not how this process is to be managed.

Item 3.5

This states that Ofgem has developed a cost assessment process since October 2008 for transitional projects which could be used to determine the economic and efficient cost of transitional projects. Warwick is not aware that this process has been subject to consultation and can find no detailed description of the methodology to be adopted in the present consultation. This seems a basic omission as the cost evaluation process should be open, transparent and the methodology subject to wider industry comment.

Item 3.9

The Developer Information Request (DIR) is clearly an important part of assessing the RAV for transitional projects. Warwick believes that the form and detail of the DIR documentation should be available for wider industry comment and input. As such it is disappointing that this information is not included in the present consultation.

Section 4 Pre-Tender Requirements for Projects

Item 4.1

Warwick notes that Ofgem is now proposing developing a “*model sale and purchase agreement for each developer to populate*”. Completion of this agreement is a pre-requisite for entry into a tender round. Given that the first tender round is due shortly after Go Active in June 2009 this does not leave much time for this documentation to be developed. Warwick is concerned over the proposed timescales for this late revision to the Regulatory proposals to be developed, populated and agreed on a project specific basis.

Item 4.19

Warwick agrees that separating pre-conditions for defining transitional project from those for a project to enter a transitional tender round (1st or 2nd transitional only) is an improvement over the previous proposals.

Item 4.20/4.21 Independent Engineering Audit Report

The requirement for projects that have been in operation prior to Go Active or Go Live to submit an engineering audit report seems of dubious benefit. Any potential OFTO bidder will be required to undertake a suitable due-diligence process based on information held within the data room. The form and level of detail involved in this due diligence is entirely at the discretion of the potential OFTO. As such Warwick believes that any independent engineering report will be of limited (if any) real value. It therefore appears to be an unnecessary expense. A further difficulty with this proposal is that many of the transitional projects listed will be partly constructed at the time the audit report is required. The meaning and validity of an audit on a partially completed project is not obvious.

Item 4.22-4.25 Financing Issues

Warwick remains unconvinced that offshore transmission involves a long-term low risk profile investment. Further there is currently insufficient evidence to make such an assertion. The current economic climate exacerbates the situation and raising finance is likely to be an issue. One major issue that Ofgem appears to have neglected is the fact that there is no certainty for generators that an OFTO license will be awarded. This increases the risk in overall project development and will make raising finance for the main generation schemes significantly more difficult. Since the sums required for the generation schemes themselves are many times the transmission system cost the uncertainty over availability of a connection becomes a key stumbling block in the entire finance raising process. Under these circumstances it appears likely that there may be more attractive investment opportunities elsewhere where there is no new Regulatory Regime to contend with.

Warwick remains unclear how transmission assets constructed after Go Live can be commissioned without the assets being transferred to the OFTO. This is because operating (and hence commissioning) the assets will not be permissible without an OFTO license.

The obvious solution to commissioning dates for transitional projects being post Go Live is that the developer be granted an OFTO License for the initial period of operation. This then gives certainty to the eventual OFTO of items such as transfer date and revenue stream.

Item 4.26 Pre-Conditions in the Enduring Regime

A particular concern is the proposed requirement that developers sign up to a Connection Agreement with NGET before there is any certainty over the design or cost of the OFTO network. Warwick has commented repeatedly on this problem in response to previous consultations. The latest consultation does nothing to address this basic issue – and a fundamental review of the arrangements is needed.

It is also disappointing that concerns raised over the pre-condition to enter into a CUSC bilateral Connection Agreement with NGET are not even mentioned in the latest documentation. The issues to address include the need to sign up to FSL and the fact that NGET has indicated it will not start any Onshore reinforcement works until an OFTO is appointed. Both these factors will tend to prevent new projects coming forward and then delay those that do.

Warwick also notes that the present requirement is discriminatory against offshore projects – since for an onshore project signing a Connection Agreement with NGET affords a guarantee of a connection. However for an offshore project no such guarantee is offered since it is possible that no OFTO will bid for the offshore works let alone be awarded a license by Ofgem. Warwick believes this is a fundamental flaw in the proposals which is clearly discriminatory. The arrangements should be revised accordingly.

Item 4.27 Pre-Conditions in the Enduring Regime

Warwick agrees that it will be necessary for developers to continue to obtain consents and leases.

The concerns expressed in responses to Consultation 84-04 remain unaddressed by the proposals. In particular the leases, consents and surveys will mean that the technical solution adopted for each project will need to be effectively defined by the developer prior to the tender process. This will tend to prevent a co-ordinated approach to design and limit opportunities for innovative solutions.

Warwick notes that Ofgem states *"it would be sufficient for a developer to have demonstrated it has obtained an agreement for a lease from The Crown Estate"*. Warwick assumes that this means that entering into the lease itself is no longer a pre-requisite. If this interpretation is correct this is a welcome improvement. If not Warwick maintains its opposition to the proposed pre-condition of entering into lease arrangements with The Crown Estate. These concerns are documented in Warwick's response to Consultation 84-04.

Item 4.28 Updated Proposals

Warwick agrees that a data room will be necessary to allow potential OFTOs to access relevant information on the project during the tender stage. However Warwick believes that a large part of project design will need to have been carried out in advance of the tender process. The scope of information in the data room is therefore likely to be wider than that envisaged by Ofgem.

Item 4.29 Updated Proposals

Warwick agrees that splitting the stages into a PQ stage and then a QTT to decide which tender round a project enters appears an improvement. However additional stage is likely to delay some projects by adding a further level of qualification. This additional delay is unwelcome and will tend to prevent projects being developed in a timely manner. The issue could be addressed by moving some of the scope of the PQ and QTT stages into the ITT stage. The time for the ITT could then be extended to allow greater chance of bidders developing proposals properly.

Item 4.31 Qualifying Project Pre-Conditions

See comments elsewhere regarding requirement to enter a CUSC bilateral agreement with NGET. This requirement is discriminatory against offshore projects.

Item 4.32 Tender Entry Pre-Conditions

The requirement stated by Ofgem is that the developer shall *"provide information to our satisfaction to enable us to establish a data room for bidders to be able to bid effectively"*. As noted elsewhere Warwick believes that a large part of the basic system design of the OFTO network will need to be complete to allow bidders to tender effectively. Ofgem should clarify how it envisages this to work and at what stage the design will need to be complete. Warwick does not believe it credible that the system design can be undertaken within the timescales proposed for the ITT stage of the project.

Item 4.36-4.37 Updated Proposals Tender Entry Pre-Conditions

Warwick notes the proposal to develop a model sale and purchase agreement (SPA) and that Ofgem intends holding workshops to facilitate this. The SPA would need to be available on a project specific basis at the time of commencement of the first tender round for transitional projects. Given the Go Active date is June 2009 it appears extremely unlikely that this will be achievable. In support of this Warwick notes the concerns raised by Ofgem in Section 4.37 i.e. that this *"approach raises a number of detailed issues and that a process of firstly developing a model SPA and then secondly agreeing it with many developers is challenging"*.

The proposals for a model SPA cover an extensive range of project specific issues. It does not appear credible that such agreements can be developed within the time available before Go Active for 1st round transitional projects.

Warwick is concerned that the SPA will therefore be of no value unless the Go Active date is postponed. Warwick believes that in the overall best interests of the wider industry postponing the introduction of the new regime would be beneficial by allowing such critical issues to be addressed properly.

Section 5 Tender Process for the Transitional Regime

Summary

While it may be true that the OFTO will not face a construction risk for transitional projects there will be issues of potential non-compliance with the proposed technical rules and Codes. In this respect Warwick has highlighted in previous consultation responses a number of areas where transitional projects may not comply with the evolving rules and Codes. It is disappointing that Ofgem's proposals do not appear to include any means by which these risks can be removed prior to the Tender Process. Such risk management combined with suitable amendment of the proposed OFTO rules would reduce OFTO risk and thereby ensure competitive bids for transitional assets.

Warwick therefore requests Ofgem to put a suitable mechanism in place to address these concerns.

The possibility that any potential OFTO may bid (and win) more than one project is an inherent part of the proposed regime. However there would be potentially significant extra work (and costs) for an OFTO to prepare independent compliant bids (and cost models) for separate projects as well as a further offers assuming more than one bid is successful. In view of this it seems unlikely that any potential economies of scale arising from successfully bidding more than one project will be realised.

The use of tender windows also increases the likelihood that bidder resource and supply chain constraints will lead to cherry picking of projects. This is likely to reduce competition with potential cost increases in the resultant successful bids. Warwick remains opposed to the use of tender windows.

In these respects Warwick believes that the process needs modification.

Item 5.1

Warwick still believes that the proposed regime will not provide certainty or best value to customers through the competitive tender process. In particular lack of design co-ordination is one major issue with the proposals. The capacity in the supply chain is already limited and this will be made worse by:

- Concentrating the bidding artificially into tender windows; and
- Increasing competition for resources from projects in more favourable Regulatory environments elsewhere in the world.

Warwick sees nothing in the latest proposals which address supply chain resource issues and the likelihood that cherry picking of certain projects will probably result in a lack of bids for other projects. This will impact negatively on overall offshore generation targets both by delaying project and in some cases preventing projects proceeding at all.

Item 5.9 Updated Proposals

The timescales set out in Appendix 7 suggest it will take a full 12 months to award a license even in the transitional regime. Even this assumes that the issues raised by the introduction of an SPA can be addressed prior to the ITT stage. It also does not include any time for the possible Best and Final Offer (BAFO) stage. This means that for transitional projects there is no margin for slippage given that the time between Go Active and Go Live is also 12 months. There is therefore a risk that transitional projects will be unable to operate after Go Live if there is any slippage in the entire OFTO tender process. Warwick believes that Ofgem should ensure that this situation cannot arise – and if necessary defer the Go Live date if it becomes apparent that this problem will arise.

For the enduring regime the timescale will also introduce unnecessary delays to new projects. Given that it will take 12 months for transitional projects the requirement to design and construct new networks is only likely to add further delay.

Item 5.12-5.13 Updated Proposals

The evaluation approach uses a number of financial measures as a means of assessing whether an OFTO will qualify for the combined total of all the projects in which an interest is expressed. This is likely to discourage/ prevent smaller OFTOs being successful in the process. In particular the financial measures will force OFTOs to make an early decision about which projects to bid for – and this decision will be made before full information on the different projects is available. This appears contrary to the stated aims of encouraging new entrants and competition.

If a financial metric is to be used then OFTOs would be better served by a process requirement to indicate their expected level of investment capability (minimum and maximum values). This would still allow a fair assessment of financial strength against investment required by Ofgem, but not tie a small OFTO to 1 or 2 specific projects. In particular if a small OFTO picks “popular” projects it could be eliminated completely from the process at an early stage. Increasing the flexibility would also potentially help stimulate greater levels of competition later in the process – i.e. in cases where there are few or no bidders for particular projects.

Item 5.14-5.16 PQ Stage

The proposed process appears confused – at the PQ stage bidders are required to select which projects are of interest but information available about each project is extremely high level only. The aim of this stage is to produce a long list of potential OFTOs – and tying these to particular projects seems unnecessary. Generic assessment criteria should be used against overall financial capability/ level of potential investment available. The updated proposals still risk discarding potentially economic and efficient OFTOs at this very early stage in the process.

Information on projects in the transitional regime should also include high level information on project programme, completion status, and suppliers of key equipment (e.g. cables, substation equipment etc).

The proposal to make PQ stage assessment on a more general rather than project specific basis is welcome. However as noted elsewhere it is not clear how this would work for financial criteria which need to be assessed against specific project value.

Item 5.18 QTT Stage

This states that “*Applicants would be required to re-confirm the projects they are interested in bidding*”. As noted elsewhere potential OFTOs may initially express an interest in bidding for multiple projects on the basis that they are unlikely to succeed in all cases. There appears no means of dealing with such an approach in the proposals.

OFTOs may also wish to make combined bids based on being successful in obtaining licenses for more than one project. The previous consultation discussed variant bids at some length although this raised a number of points of concern. The present proposals are unclear in this respect and need clarification. Clearly sharing of costs between OFTO bids may allow economies of scale – particularly for services which may be shared between different projects such as network control, O&M facilities, spares etc.

Item 5.19-5.21 QTT Stage

The Information Memorandum is a basic requirement for bidders to assess whether to bid or not. Without this information it will not be possible for bidders to make an informed choice about which projects it may wish to bid.

As noted elsewhere the process appears confused. It would seem reasonable to provide a significant portion of this information at the PQ stage rather than the QTT stage – if indicating which projects are of interest to the OFTO remains a requirement at the PQ stage. Note that Warwick believes that the requirement for OFTO's to select projects of interest at the PQ stage will hinder the overall aim of producing a long list of potential OFTOs.

One valid concern raised by Ofgem is that there may be insufficient interest shown in particular projects during the PQ/QTT stages. It is also worth noting that selected bidders may withdraw at the ITT stage – this could impact on the viability of the ITT stage even after the QT stage is complete and the ITT issued.

In Warwick's opinion this is a fundamental problem with the entire Regulatory Regime. For the transitional regime there is the OFTO of last resort mechanism which provides a natural fall back position. This is also analogous to onshore networks where a connection is effectively guaranteed once a connection offer is made. For the enduring regime there is no such OFTO of last resort mechanism – and this makes the difficulty highlighted by Ofgem in these sections more problematic. The proposal to bundle an “unpopular” project with another project or projects does not seem a satisfactory solution – and may even make the overall combined portfolio unattractive. In such cases more than 1 project may suffer as a result of this basic flaw in the Regulatory Regime.

Item 5.23-5.25 Consortium Changes

It is not clear to Warwick whether consortia are required to be finalised at the start of the QTT process or prior to submission of a tender at the ITT stage. The latter appears more reasonable.

The supply chain is clearly restricted – particularly in the provision of certain plant and equipment. A restriction on inclusion of supply chain in consortia on an exclusive basis however may not prevent supply chain issues from distorting competition. For instance suppliers may quite legitimately choose to offer more advantageous terms to certain OFTOs based on track record, perceived project risk – and all the other factors which influence a supplier in choosing whether or not to tender for work. Equally suppliers may choose not to offer their services to other OFTOs. Limitations in the supply chain are a significant issue which need to be actively tackled – taking power in the tender regulations in itself appears unlikely to resolve the issue.

Item 5.26-5.33 Selection Criteria and Process

The proposed requirement to measure existing net assets against those of preferred projects appears unnecessary. In particular applicants for the long list are likely to want to pre-qualify for as many projects as possible to increase the chance of being able to select preferred projects later in the process.

There appears to be no requirement for capability in terms of overall design. This should be relevant to transitional projects since lack of design capability may preclude possible future extension of the OFTO network. Clearly for enduring regime some design capability – or demonstration of access to this capability should be a pre-requisite.

Item 5.34-5.36 Identifying Qualifying Bidders

The scoring and ranking process for bidders appears reasonable – so long as a consistent scoring system is adopted. Such scoring systems are often at best semi-quantitative and it is therefore important that an adequate number of assessors is used for comparative scoring of each bid.

The proposed increased flexibility in the number of bids is welcome however there is no real justification to impose limits if potentially suitable bids could still be received.

Warwick believes that this proposal is artificial and could effectively eliminate the potentially most cost effective bid before the ITT stage is even reached. This in turn would lead to inefficient proposals being successful and adding costs to generators and demand customers alike.

In the event that less than 3 parties are suitably qualified it may still be possible to select an economic and efficient OFTO so long as:

- The bidders are not aware of the actual number of competitors in a specific tender; and
- Some form of benchmarking is adopted against other projects.

In terms of benchmarking Warwick believes that this could be a useful tool for the industry and this area should be further by Ofgem.

As noted elsewhere it seems likely that potential OFTOs will try to pre-qualify for multiple projects. This would be in the expectation that selection of preferred projects can then be made in a more informed manner – once greater project specific detail is made available in subsequent stages. The proposals do not appear to make adequate allowance for this.

In addition bidders may be capable of pre-qualifying for any single individual project but might not have the resources (financial or otherwise) to successfully bid for or indeed own/operate multiple networks. The fact that it is Ofgem which will effectively select which potential bidders are chosen to take forward to the ITT stage for each project seems inappropriate. The process should leave this choice to the bidders themselves – this would best foster competition and cost effective bids.

The above issues will also make Ofgem's task in selecting bidders to take forward on an individual project basis more difficult. Bidders may also drop out after the ITT is issued and this could lead to uncompetitive OFTOs being appointed.

There are also obvious problems of process where a bidder wishes to tender for multiple OFTO networks as a single package. There seems little prospect that the process will encourage should multiple bids – leading to loss of potential economies of scale.

The costs of the ITT process itself are likely to be relatively small in comparison to the costs incurred of not selecting the most cost effective provider. For this reason Warwick believes that the choice of whether qualifying bidders take part in the ITT should be left as a commercial decision for potential OFTOs. Wasted bid costs could be avoided by Ofgem notifying all qualifying entrants of the number of qualifying projects – for instance if this number is greater than 5. This would then allow entrants to assess the level of commercial risk associated with entering the ITT stage. The most important factor is that the winning

bid delivers a cost effective solution. The Ofgem proposal of limiting entrants to the ITT stage to 3-5 therefore appears perverse.

Item 5.39-5.41 Invitation to Tender Stage – Evaluation Criteria and Process

The proposed time to prepare bids and produce a “firm and binding” offer and for Ofgem to assess the tenders and select a preferred bidder is 6 months. Warwick does not believe that delivering a firm and final offer which is cost effective within this timescale will be possible. This is particularly true for the enduring regime where the construction cost and risk will form a major part of the process. Even using the full 6 month window for tender preparation alone is unlikely to allow bidders time to obtain “firm” or cost competitive prices from potential sub-suppliers – and in any case the duration of the tender process itself, and uncertainty over the construction/ connection dates is going to make fixing prices difficult.

Warwick would also refer Ofgem to the issues raised by NGET in its “*Open Letter to Industry – Offer Pricing Options*” dated 5th November 2008. This letter explains the difficulties and additional costs which arise from the need to agree a “firm” price before construction contracts can be tendered. For the OFTO regime the level of risk associated with fixed prices are likely to result in highly inflated bids being received.

The wording suggests that Ofgem’s key assessment criteria will be cost. Warwick is concerned that over-emphasis on cost may lead to bids with excessive risk or inadequate technical or operational processes being awarded licences. This may then lead to subsequent failure of the OFTO with its resulting adverse impact on the associated generation project(s).

Warwick is also concerned that Ofgem will need to develop the skills and procedures to assess tenders from scratch – since this is not an activity presently undertaken by the Authority. Hence there is a risk that early projects will suffer as Ofgem acquires these new skill sets and appropriate management controls are put in place.

Some form of industry overview/ governance procedures should be introduced into the process to ensure that Ofgem manages the entire process in a proper and effective manner.

Item 5.43-5.44 Information Available

Warwick reiterates the point made in previous consultation that confidentiality agreements with Ofgem may not be sufficient to allow release of all relevant project material to potential bidders. For example turbine manufacturers often have particularly onerous confidentiality requirements with direct agreement with the manufacturer being required in some cases. The confidentiality requirements need to take account of such issues – the proposal for a single overarching agreement to cover subcontractors may not be adequate. These issues need further consideration.

Regarding detailed information required on each project there are a number of relevant issues:

- Contracts, leases, warranties – it is unlikely that contracts can easily be split between transmission and generator assets. It may be prejudicial to the generator to reveal contractual information about its own plant and equipment. Warwick has previously raised the issue that splitting of leases/consents is not possible and new consents will be required. There appears to be no means of addressing this issue in the process;
- The relevant Connection Agreements are not yet available since the OFTO will need to know the terms at both the onshore and offshore transmission system boundaries;
- Investment and operation plans for the transmission project – it seems plausible that since the Regulatory Regime will supersede such plans that developers will not have

- investment or operation plans in place. This is particularly relevant to projects still under construction or projects taking part in the 2nd transitional tender round;
- Evidence of compliance with industry regulations etc. There are at least 3 issues with this:
 - Projects may require derogations/ grand fathering arrangements to cover issues where the sites are non-compliant with relevant codes. This requires firstly identification of possible non-compliance issues and then granting of appropriate derogations (lifetime) by Ofgem. Warwick is unclear whether a suitable process is in place to address these issues prior to the tender round commencing. Clarification is requested on this key issue;
 - For projects which are under construction or commissioning the compliance procedures necessary to demonstrate adequate performance against relevant codes will not be complete. Hence it will not be possible to demonstrate compliance at the tender stage – this will leave a residual risk on the OFTO which will need to be factored into the revenue stream as a risk premium;
 - Compliance at the offshore boundary is not a present requirement. Hence relevant evidence will need to be provided by the developer on a project by project basis.
 - Concerns raised regarding the SPA are relevant to transfer terms and are unlikely to be available within the required timescales;
 - Warwick believes that dialogue between the OFTO and developer as the 2 signatories to the SPA is essential. However any dialogue will have timescale implications and likely delay the award of a license.

Item 5.47-5.51 Bidder Dialogue

Warwick supports the idea that the developer should be involved in structured discussion with different bidders with regard to the SPA. These discussions may need to continue into the Preferred Bidder Stage.

Equally the proposals of different bidders may have different levels of attractiveness to the developer. This could include for instance O&M strategy, management structure etc. Given that the Ofgem assessment process will be quantitative it would seem possible that the developer could provide input to this - for instance independent scoring/ranking by the generator of certain aspects of the OFTO proposal. Such input would form a check on the assessment carried out by Ofgem – in cases where there is a significant material difference in scores then these issues could be re-examined. Clearly such input from the generator would need to be informative only but would help ensure a suitable OFTO is chosen. The ultimate selection of the OFTO could still be made by Ofgem.

Items 5.52-5.55 Bidder Clarification

Warwick supports the idea that the developer should be involved in structured clarification process with different bidders. Some issues on which bidders require clarification may however relate to particular features of their proposals which give a competitive edge. The proposal to allow access to all questions and answers from all bidders, even on an anonymous basis, may negate such advantages. This could stifle innovative solutions – in both transitional and enduring regimes. It therefore would seem appropriate to allow any questions and answers reasonably identified by a bidder as confidential to remain confidential between bidder, developer and Ofgem. The process should make due allowance for this, as to do otherwise is likely to reduce the effect of competition.

Warwick also notes that clarifications of bids may be required by Ofgem, or indeed the developer. The process should allow for this too.

One general concern is the potential timescales for clarifications – which may impact on the ability of OFTOs to complete their bids in a timely manner. Suitable principles for dealing with such issues need to be set out in advance of the ITT stage.

Item 5.56-5.57 Tender Documentation

See comments later regarding Annexes 1-3.

Item 5.58-5.59 Best and Final Offer

Warwick supports the principle that a BAFO stage may provide some advantage in terms of overall economics/ technical performance of the successful bid. The obvious concerns are:

- There is no definite proposal and the approach adopted on any given project could therefore be construed as unfair or inconsistent;
- Developers benefiting from a BAFO stage could be argued as having favourable treatment in comparison to others. This could be construed as anti-competitive behaviour on the part of Ofgem;
- There are potential timescale implications in delaying appointment of an OFTO of holding a BAFO. For transitional projects this could lead to a situation where an OFTO license is not available at Go Live; i.e. the tender process/ license award is already anticipated to take the full 12months presently available. In practice there are a number of possible consequences of this:
 - Ofgem does not consider a BAFO for transitional projects due to time constraints. This leads to selection of sub-optimal OFTO bids;
 - Lack of a BAFO stage leads to increased on-going generator costs and potentially also could add cost to wider system users. This is contrary to overall Regulatory aims;
 - A generator may be prevented from operating due to the license award being delayed beyond the Go Live date;
 - Ofgem has to delay the Go Live date since OFTO licenses have not been awarded;
- Warwick believes that Ofgem should include a clear definition of BAFO and whether in practice this stage will be applied for transitional projects.

As currently framed the inclusion of BAFO appears to be window dressing as in practice for at least the 1st tender round it will not be applied.

Item 5.60 Preferred Bidder and License Grant

Ofgem proposes identifying a preferred bidder and potentially a reserve bidder. Warwick does not believe that using a reserve bidder will be practical within the available timescales. Particular issues include the SPA, and how the costs for the reserve bidder continuing in the process are to be met. It seems unlikely that reserve bidders will be willing to (or should be expected to) fund this on an on-going basis.

Item 5.62 Timing for Tenders in the Transitional Regime

As noted elsewhere in this response Warwick has real concerns over the proposed timescales which appear unrealistically optimistic. The process is time consuming and is likely to delay award of license beyond Go Live date for at least some projects.

Item 5.63-5.66 Further Development of the Tender Process

Ofgem apparently already recognises in Section 5.63 that the proposed process as currently framed will not meet the objectives; i.e. Ofgem states: *“we have a number of key objectives for the competitive tender process. It will be important for the ongoing success of the approach to consider the extent to which these are met over time.”*

It appears perverse to introduce a new regime with the expectation that after a single tender round the regime will need to be re-designed. This is potentially discriminatory against both the 1st tender round and depending on changes made going forward the subsequent rounds as well. For this reason Warwick believes that the introduction of the new regime at the proposed date is not achievable and should be delayed – this would

delay the need for a license and allow developers to retain any assets within their own control. Alternatively transitional projects should be given the option to opt out of the tender process altogether. If the present proposed Go Live date is retained then the existing developer could be awarded a license by Ofgem pending confirmation of the final Regulatory Regime.

New entrants would likely be of benefit to the industry - given the proposed offshore Regulatory Regime. However it is by no means certain that a competitive approach will deliver more economic or efficient solutions than the present regional monopoly approach adopted onshore.

With regard to possible auctions introduced into the tender process this would represent a fundamental change to the approach as currently framed. The fact that Ofgem is considering such significant changes so late in the day appears to support a view that the basic proposals are unsuitable. As stated in response to previous consultations Warwick does not believe that the proposals will meet overall objectives and should be subject to fundamental review.

Section 6 Tender Process for the Enduring Regime

Chapter Summary

Warwick has raised numerous issues with the proposals for the transitional regime. Given the similarities with the proposals for the enduring regime the majority of the difficulties raised are equally applicable to the enduring regime.

The scope of the enduring regime introduces significant additional problems in terms of the additional timescales required for the design process. The overall processes appear overly complex and unwieldy and are therefore likely to hinder the development of offshore wind in a timely and efficient manner. Warwick notes that Ofgem itself is already indicating that significant changes to the proposals may be required to:

- Achieve overall Regulatory goals;
- Encourage new entrants; and
- Improve competition by introducing auctions.

Set against this background it is increasingly clear that Ofgem itself is concerned that the present proposals will need significant revision. This could equally be interpreted that the basic proposals are not fit for purpose and a fundamental review is required before the proposals are imposed on the industry.

As the overall proposals are developed in increasing detail in successive consultation the inherent problems of the basic Regulatory framework are becoming increasingly apparent. For these reasons Warwick would call for a fundamental review of the offshore Regulatory Regime.

Item 6.1

Warwick still believes that the proposed regime will not provide certainty or best value to customers.

Item 6.2 (Introduction)

Warwick notes the proposed zonal arrangements under the Crown Estates Round 3 proposals. These imply some belated recognition that the current regime proposals for Offshore transmission offer no means of providing an overall co-ordinated approach to network development. This seems ironic given that in March 2007, the government decided that the offshore electricity transmission regime should be a competitive, or non-exclusive, rather than an exclusive monopoly activity. The Crown Estates proposals now

imply that a regional monopolistic approach to Offshore transmission would be more favourable. This is contrary to the entire Regulatory Regime being put in place.

Having said that Round 1 and Round 2 projects will still most likely proceed on the basis of pure radial connections with little prospect of cost sharing. Warwick therefore believes that the entire enduring arrangements should be subject to major review for this reason. A delay in introducing the new proposals would also allow the lessons learnt from transitional projects to be incorporated into the regime more readily.

Annex 1 - Draft Template Prequalification Document (Ref: 21/09c)

Important Notice

Information provided by the developer will remain vested in the developer and will not be subject to any copyright from Ofgem. Similar comments apply to the notice within the ITT document – except in this case the extent of information vested in the developer will most likely significantly exceed any information provided by Ofgem. It is important that intellectual property is treated in an appropriate manner and the wording of the proposals appears inadequate in this respect.

Ofgem indicates that all information is provided “in good faith”, similar criteria should apply to information within the project “data room”. This is contrary to Ofgem’s requirements elsewhere that the developer must provide a warranty on such information. This inconsistency should be corrected.

Item 1.3 Overview of Project

Since the level of detail will be high potential bidders are likely to want to pre-qualify for all available projects. Selection of their preferred project(s) is more likely to be possible at the ITT stage. The level of detail requested for pre-qualification (and qualification) appears overly complex within this context.

It is in any case likely that there will be insufficient information to allow potential bidders to select those projects of greatest interest to them. The following then become potential adverse consequences to this early selection of projects by bidders:

- Potential OFTOs will seek to pre-qualify for all available projects – in the expectation that some of these will not be bid at the ITT stage. However in reality the potential OFTOs would only wish to bid for a subset of the available projects;
- Successful pre-qualifying/ qualifying entrants may choose not to enter the ITT stage for particular (or indeed all) projects. Reasons for not bidding might include insufficient funding, preference for other projects, or high perceived risks that only become apparent with access to the detailed information available at the ITT stage;
- There are a limited number of potential OFTOs and these seek to select the most advantageous projects to take forward. The early decision required at the PQQ stage increases the risk that there may be limited (or indeed no) competition for some projects.

Overall it would seem more logical to allow potential bidders to decide which projects to bid for at the ITT stage when greater project detail will be available.

Item 1.4.5 Preferred Bidder

The reference to the Preferred Bidder needing to have “*necessary land arrangements, both offshore and onshore*” in place requires clarification. Elsewhere Ofgem’s proposals require the developer to obtain consents and leases – and by default these will need to include both onshore and offshore substation sites. It is difficult to see how the Preferred Bidder can be expected to be responsible for these as well. This applies equally to documents in Annex 2 and Annex 3.

Annex 2 - Draft Template Qualification Document (Ref: 21/09d)

Warwick believes that the time spent on the pre-qualification and qualification processes should be reduced to enable greater time to prepare tender returns. Much of the information requested would normally be covered at the ITT stage. A longer duration for the ITT would allow greater possibility of prices being “firm”. The proposed 6 month timescale to respond to an ITT, hold clarification discussions and for Ofgem to select a preferred appears woefully inadequate for the enduring regime without bidders including significant risk and uncertainty premiums.

Item 1.4.3

This states that “All prequalified Applicants (the “Bidders”) for a Project will be invited to tender for that Project.” Please check this since it seems more likely that this should state “qualified” not “prequalified”.

Item 2.3.2 Evaluation Criteria

For the enduring regime the OFTO will be responsible for design, construction and operation of the network as well as all necessary funding. The lack of any evaluation criteria regarding engineering competence for the design and construction stages is a notable omission. This should be corrected.

Section C Financial and Economic Information

It seems likely that at least some OFTOs will be special purpose vehicles. Given this much of the historical information requested may have little relevance. It is also unreasonable to suppose that project insurances will be in place at this stage.

Section G Consortium Structure and Information

In terms of subcontracting (Items G5 and G8) it seems unlikely that key sub-contracts will be in place at this stage in the process. Asking for details of these and agreed terms therefore seems unnecessary.

Annex 3 - Draft Template Invitation to Tender Document (Ref: 21/09e)

Important Notice

Similar comments apply to this as to the equivalent statement in the Prequalification Document. In addition the condition that bidders may not engage in any publicity for the duration of the Transmission License without Ofgem’s agreement appears both unreasonable and unmanageable. Warwick believes alternative wording is required.

Item 1.4 Overview Of Tender Process

There should not be a requirement to include the names of those parties that have qualified to bid for the project. This information would potentially comprise competition, e.g. in the instance where only one or two parties have qualified. As such names of qualifying bidders should remain confidential between each bidder and Ofgem.

Item 1.4.4 Preferred Bidder

The reference to the Preferred Bidder needing to have “necessary land arrangements, both offshore and onshore” in place requires clarification. Elsewhere Ofgem’s proposals require the developer to obtain consents and leases – and by default these will need to include both onshore and offshore substation sites. It is difficult to see how the Preferred Bidder can be expected to be responsible for these as well.

Item 1.4.7

There are real concerns that the period of time allowed of 6 months is inadequate. It would have been more helpful if Ofgem could have populated the timetable with an illustrative

example. Looking at the number of tasks on the timetable it reinforces the view that there is insufficient time allowed in the process.

Item 2.9.2 The Great Britain Security and Quality of Supply Standard (GBSQSS)

Since OFTOs will also be governed by this document ownership of the GBSQSS should be extended to include all OFTOs. There is no reason to limit ownership to the Onshore TOs. The ownership and participation within governance procedures for all other relevant applicable codes should also be extended to include OFTOs.

Item 2.11.2 Decommissioning

The issue of decommissioning requires clarification. The life of the OFTO network may exceed the initial 20 year license the meaning of decommissioning costs becomes questionable. Decommissioning costs are a potentially significant risk for the OFTO and this aspect of the regime requires clarification. It may be simpler to exclude decommissioning from the initial License regime and hold a separate tender at the appropriate time when there is greater certainty over timing.

Item 3.2 Technical Overview

A major point of concern is the extent to which the OFTO network needs to be designed in advance of the tender process. The consents will require substation locations, cable routes and landfall points to be determined in advance. This will most likely need to be done by the developer. Hence the scope for innovative solutions will be restricted before the tender round commences.

Notwithstanding the above limitations it will be impossible to compare prices on a level playing field since the technical solutions proposed by OFTOs may differ significantly. Ofgem appears to wish to compare standardised cost models but the technical solution chosen, and its associated performance may profoundly affect costs. For example a very efficient system design may lead to cost savings which outweigh inefficiencies elsewhere in a bid. It may then be the case that if the same (optimum) system design were considered by another bidder that significant cost savings could be achieved. The proposed process allows no means of identifying and realising the most cost effective design. This fundamental flaw in the process is likely to increase costs to generators and demand customers alike.

Warwick believes that the issue of technical design, and its effect both on future network performance (and possible extension) is key to the entire Offshore industry. There is currently no mechanism in the entire process (tender or otherwise) to achieve design optimisation.

A further difficulty in comparing OFTO bids is that there are no industry standards – other than the high level ones included in the industry codes. For the Onshore network it is straightforward for the TOs to optimise the overall network design. Suitable detail of scope can then be included during the tender stage. Contract award to the lowest cost solution is only possible because the technical scope is tightly defined. Such bid comparisons will not be possible in the OFTO regime.

There is also no equivalent common design process in the Offshore regime. This appears to be another major flaw in the tender process since it will not be possible to compare bids on a level playing field – or indeed have all bidders compared on the most cost effective design.

Item 3.2.2 Assets to be Transferred

For transitional projects the SPA is a major concern. The ITT is reliant upon this being in place however even Ofgem believes that this will be “*challenging*”. As noted elsewhere Warwick does not believe it credible that SPAs will be available in a timely manner for all

transitional projects. This impacts the viability of the Go Active and Go Live dates or indeed the tender process and license award for some if not all transitional projects.

Item 3.3.3 Change

There appears to be no means by which an OFTO can mitigate against Regulatory change – e.g. changes to technical, code and legal requirements. For Onshore regimes risk management is possible due to the Regulatory Review process. The lack of review is likely to lead to increased costs being included by OFTOs. Furthermore OFTOs may fail to allow for factors which significantly influence (increase) future costs to allow for code changes. This could lead to financial failure of the OFTO in the worst case. The emphasis by Ofgem on lowest cost bids increases the likelihood of successful bidders having included lesser amounts for risk mitigation. Hence this feature of the regime will tend to increase the risk of future OFTO failure – which would be to the detriment of all concerned.

Item 4.2 Shortlisted Bidders

The publication of bidders names is only likely to reduce competitive drivers and lead to increased prices. Warwick does not agree with this publication. It is notable that this comment has been made previously and ignored without any explanation or justification being offered in the consultation document for the proposed approach.

Appendices

These appear to show that parts of financial modelling requirements are relatively well developed in comparison to the technical requirements of the ITT. Warwick is concerned that lack of clear technical input to preparation of the ITT will lead to potentially inefficient OFTO designs being tendered. The fact that Ofgem has indicated a new proposal that NGET should assist in tender assessment does little to address this problem. The technical content in the ITT is key to being able to compare tenders fairly and also in arriving at least cost solutions. Ofgem is therefore requested to clarify:

- Technical content included in the ITT;
- How this technical content is to be developed on a project by project basis;
- What resources are available to Ofgem to carry out these critical tasks?

In relation to this Warwick made similar comments in response to the previous consultation submitted in November 2008. It is disappointing that little progress appears to have been made in these key areas since

Appendix 6 - Key Provisions in the Sale and Purchase Agreement

It is clear from the scope of issues covered by this Appendix that agreeing the SPA with the developer is going to be a major task. Furthermore the potential OFTO may want to negotiate on some of the issues raised; e.g. ownership schedules, access arrangement and CDM responsibility for the shared Offshore Substation. It does not seem credible that SPAs will be in place for transitional projects prior to the 1st tender round commencing.