



Offshore Transmission Final Consultation
Department of Energy and Climate Change
1 Victoria Street
LONDON
SW1H 0ET

06 May 2009

Dear Sirs,

Response to the Final Joint Ofgem/DECC Regulatory Policy Update on Offshore Electricity Transmission

Thank you for the opportunity to respond to the Final Consultation Regulatory Policy Update on Offshore Electricity Transmission. This response is submitted on behalf of ScottishPower Energy Management Ltd, ScottishPower Generation Ltd, ScottishPower Renewable Energy Ltd and ScottishPower Renewables & Vattenfall Vindkraft Round 3 Joint Venture.

The successful development of offshore wind and fulfilling the potential of wave and tidal stream generation is essential if the UK is to meet its targets for renewable energy and, in particular, meet the objective of 33GW (including 8GW from Rounds 1 & 2) of offshore wind energy by 2020. We support the government's renewable ambitions and will work with it to realise these goals. Offshore generators require a regime that will give them access to a market that is consistent and competitive with the rest of the electricity market.

As stated in our response to the regulatory policy update in February 2008, ScottishPower would have preferred to see an "exclusive multi-zone approach" adopted as this would have delivered more effective co-ordination of projects within each area, ensuring efficient solutions and prompt delivery. In particular, we have concerns that a "non-exclusive" licence may not deliver the most efficient solution where a zone is developed over a number of years. ScottishPower will work within the existing proposals to ensure a timely and orderly introduction of the offshore transmission regime, but we still believe that introduction of an "exclusive multi-zone approach" should be considered in any post-implementation review of the arrangements.

The Construction Security

We note the provisions relating to the provision of a Construction Security by the OFTO to National Grid to ensure that the OFTO does not abandon construction of the project. However, the consultation (6.69) does not make clear how the current cap on Liquidated Damages of £5m has been calculated and whether this would be sufficient to recognise the offshore generator's potential losses from late delivery of the transmission connection.

Performance Targets

As stated in our response to the regulatory policy update in January 2009 we believe that generic availability incentives may not be appropriate to each unique offshore connection and that bilateral negotiation between the generator and OFTO may deliver a more appropriate allocation of risk and reward between the parties and the best overall economic solution. To

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ensure the most efficient sharing of risk between the OFT and the generator is achieved, the generator should be fully involved in the tender process and negotiations from the earliest date.

Inter / Intra Windfarm cabling at 132kV and above

It should be noted that the proposal as currently defined in 3.14 could result in the OFTO becoming involved in the installation and operation of assets to permit the collection of electricity within or between windfarms (which would normally be construed as generator assets) and further consideration should be given to a definition which more clearly defines the connection boundary as being at the point at which electricity is transmitted onshore.

We attach the following responses to the specific questions raised in the consultation document.

Question 1

We would welcome respondents' views on the supply chain and skills capacity. In particular, we would welcome views on the extent to which Ofgem, when granting OFTO licences should take into consideration the policies and processes proposed by each bidder for developing and maintaining the appropriate skills necessary for them to discharge their licence obligations.

ScottishPower shares the concerns over the capability of the supply chain and skills base in the UK to support the ambitious targets for deployment of offshore renewables and welcomes measures to support and promote their development. Consideration of the bidder's policies and process for developing and maintaining the skills required to provide the OFTO service, together with financial strength and access to the necessary physical resources (e.g. access to specialist shipping) should be carried out at the Pre-Qualification stage of the tender process to avoid consideration of bids which cannot deliver the required level of service over the life of the asset.

Question 2

In particular we would welcome any further views on:

- (a) our approach to dealing with predefined adjustments for "known unknowns";**

Refinancing

ScottishPower agrees that benefits achieved from future re-financing of offshore transmission assets should be shared between the OFTO and the generator. However the sharing mechanism should be symmetrical, should continue to provide an incentive on the OFTO to seek to maximise such gains and should complement the full package of incentives placed upon the OFTO on performance and cost targets. Any sharing arrangement should be defined ex-ante and not implemented retrospectively in the OFTO licence.

Incremental Capacity Increases

We welcome the clarification that the 20% limit on incremental investment is based upon the real initial capital cost.

Decommissioning

ScottishPower agrees that OFTOs will have limited control over changes to decommissioning liabilities (set by the Secretary of State) over the life of the assets and that this risk should be shared with the offshore generator through a pass-through mechanism where the incremental cost can be shown to have been incurred efficiently. Any potential increase in decommissioning costs should be disclosed by the OFTO to the generator as soon as the potential liability is identified to enable the generator to make provision for any potential financial impact at the earliest point.

Inflation

ScottishPower agrees that it would be appropriate to index the full revenue stream to the Retail Price Index. This provides certainty and predictability to both the generator and OFTO and provides the option to the generator to hedge cost increases using an appropriate financial instrument. It would also reduce the requirement for the OFTO to build in a risk premium, thus lowering costs to the generator and consumers.

Business rates and licence fees?

As both of these items are outwith the control of the OFTO, we accept that any change in these costs should be passed through to the generator. However, offshore generators would appreciate clarity on whether a materiality test would be applied to increases in these costs and how frequently the re-opening process could be applied.

(b) the OFTO of last resort proposals;

ScottishPower believes that the OFTO of last resort process will be critical to the success or failure of the OFTO regulatory system. The process must be robust, swift to implement and must take into account the commercial risk to the generator as it is most likely to be invoked following a significant failure of an offshore transmission system. In considering the appointment of an OFTO of last resort, Ofgem should have regard to the financial capability of small OFTO's to successfully deliver the transmission infrastructure to some of the larger scale offshore developments. Failure to adequately assess the capability of the OFTO of last resort could result in a cascade of OFTO failures as the burden is increased on the remaining parties. Consideration should be given as to whether OFTOs should be given the option of whether they wish to be considered as an OFTO of last resort. Potential OFTOs may be interested in becoming involved in a single or limited number of offshore connections and may not wish to become involved in a greater number of connections through this process.

(c) business separation requirements

ScottishPower welcomes the clarification provided in the consultation document on the impact of the European Union unbundling requirements. However, ScottishPower remains concerned that Ofgem's interpretation of these requirements will seriously restrict the amount of competition for the construction and operation of offshore transmission assets and that more should be done to encourage rather than restrict the number of potential providers to ensure that the most competitive and efficient solutions are provided to offshore generators. This is particularly important given the current economic situation and the difficulties which potential Offshore Transmission Owners (OFTOs) will face in raising project finance.

Efficiencies could be achieved by offshore generators who bid to construct their own transmission assets. However, the uncertainty involved in the sale of the OFTO vehicle prior to completion of the assets would discourage this, particularly as the generator could be perceived as a "distressed seller" by potential purchasers.

(d) Specifically, we would welcome comments on how clear respondents consider the criteria for an OFTO of last resort direction (as set out in Annexe 1) are and in what ways the criteria could be made clearer.

ScottishPower believes that the criteria for an OFTO of last resort direction are specified clearly in the proposed Licence Conditions (B18 and E21) and this should provide certainty to potential OFTOs of the conditions under which they could be required to undertake this role. Paragraphs 3(b), 4 and 5 of Licence Condition B18 provide some comfort to offshore generators that the capability of the OFTO of last resort to undertake the role will be fully examined. There is also comfort to potential OFTOs and their generator customers that they will not be directed to become an OFTO of last resort where it would potentially be detrimental to their existing operations.

Question 4

We would welcome comments on the activities identified in the Offshore Implementation Plan and feedback on any activities that should be undertaken in the Implementation Period that are not included in the Offshore Implementation Plan.

The publication of the Offshore Implementation Plan confirms the ambitious nature of the timetable and the number of tasks to be completed if the offshore transmission regime is to be delivered on time. The Plan needs to be updated as required to reflect experience with the implementation of the transitional arrangements.

Question 6

We propose that the Secretary of State makes the changes set out in the annexes to this consultation, subject to evidence to the contrary. We would welcome respondents' views.

Given the tight timetable outlined in the Implementation Plan we agree that the changes set out in this consultation should be made. However, the arrangements should be reviewed within 12 months of "Go-Live" to ensure that they are functioning efficiently and delivering offshore transmission infrastructure in a timely and economic manner.

I hope these comments are helpful. If you wish to discuss or clarify any of the points we have raised then please do not hesitate to get in touch.

Yours sincerely,

James Anderson
Commercial and Regulation Manager