

ofgem E-Serve

Offshore Transmission

First Transitional Tender Information Memorandum

September 2009



RBC Capital Markets®

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Glossary of Abbreviations

Abbreviations used in this Tender Information Memorandum, unless otherwise defined in this Tender Information Memorandum, have the following meaning:

Authority	The Gas and Electricity Markets Authority
BAFO	Best and Final Offer
BSC	Balancing and Settlement Code
BSUoS	Balancing Services Use of System
CUSC	Connection and Use of System Code
DCUSA	Distribution and Connection Use of System Code
DECC	Department of Energy and Climate Change
DEFRA	Department for Environment, Food and Rural Affairs
EA 2004	Energy Act 2004
EA 2008	Energy Act 2008
EU	European Union
FEPA	Food and Environmental Protection Act 1985
GB	Great Britain
ITT	Invitation to Tender
Km	Kilometre
MVA	Megavolt Ampere
MW	Megawatt
MWh	Megawatt hour
NETS	National Electricity Transmission System
NETSO	National Electricity Transmission System Operator
NGET	National Grid Electricity Transmission plc
nm	Nautical Mile
O&M	Operation & Maintenance
Ofgem	The Office of Gas and Electricity Markets
OFTO	Offshore Transmission Owner
PQ	Pre-Qualification
PSIM	Project Specific Information Memorandum
QTT	Qualification to Tender
RBC	RBC Capital Markets
REZ	Renewable Energy Zone
RPI	Retail Price Index
SHETL	Scottish Hydro Electric Transmission Limited
SPT	Scottish Power Transmission
STC	System Operator – Transmission Owner Code
TNUoS	Transmission Network Use of System
UK	United Kingdom of Great Britain & Northern Ireland

1.0 Introduction

Ofgem launched the first round of competitive tenders for offshore electricity transmission owner (“**OFTO**”) licences with the publication of its Pre-Qualification (“**PQ**”) document on 22 July 2009. This first round of tenders, known as the first round transitional tenders, will identify offshore transmission licensees to own and operate transmission assets which have been, or are being, constructed by the developers of the relevant offshore wind generation projects. The first tender process will grant licences for nine projects with a combined asset value in the region of £1.1 billion.

Successful bidders will receive a transmission licence and an entitlement to an associated 20 year revenue stream in return for purchasing the transmission assets from the offshore wind generator and operating them in accordance with the obligations of the licence. Importantly, the revenue stream will be dependent upon transmission asset availability, rather than actual utilisation. Ofgem may choose to extend the revenue stream beyond the initial 20 years, depending on the ongoing need for the transmission assets and the generator’s requirements.

To provide potential bidders with information about the opportunities available at the Qualification to Tender (“**QTT**”) stage of this first tender round, separate project-specific information memoranda (“**PSIM**”) are available for each project. This document, referred to as “Tender Information Memorandum”, provides an overview of aspects of the regime common to all projects, and should be read in conjunction with the PSIMs.

A full data room will be made available at the Invitation to Tender (“**ITT**”) stage to those Qualifying Bidders that are shortlisted following the conclusion of the QTT stage.

1.1 Process documents

Ofgem has made available a number of documents to Qualifying Applicants for this QTT stage. The main documents are:

- The QTT Document;
- The Tender Information Memorandum (this document);
- The Project Specific Information Memoranda; and
- Tender guidance documents.

1. The QTT Document

The formal QTT Document provides those participants invited to submit a response (“**Qualifying Applicants**”) to the QTT stage with guidance and instructions regarding the QTT process, as well as the full list of QTT questions Qualifying Applicants must respond to. For the avoidance of doubt, the QTT document takes precedence over this document and the PSIMs.

2. The First Transitional Tender Information Memorandum

This document provides background information and guidance regarding the QTT stage including:

- Investment highlights;
- An overview of the tender process;
- Confirmation of those projects that have met Ofgem’s qualification and tender entry criteria (“**Qualifying Projects**”) for this first tender round; and
- Further background information on the regulatory framework.

3. Project Specific Information Memoranda

Accompanying this document are PSIMs for each Qualifying Project in this tender round. These documents have been produced by Ofgem based on information provided by the developers of the Qualifying Projects and analysis undertaken by Ofgem and its consultants. The documents are provided to assist Qualifying Applicants to develop their detailed QTT submissions. Information provided includes:

- Project specific investment highlights;
- An overview of the transmission assets including details of the current project sponsors, proposed boundary points, network design, and details of the assets proposed to be transferred;
- Commercial and contractual arrangements including contractual strategy for procurement of the assets, proposed interfaces between the developer and OFTO, Operations and Maintenance (“O&M”) approach, insurance and decommissioning; and
- The expected timing of asset transfer.

4. Tender guidance documents

Tender Guidance documents containing further information will be released by Ofgem during the QTT stage covering:

- Process to asset transfer;
- OFTO special licence conditions (including the availability and performance regime); and
- OFTO of last resort process.

Furthermore, existing industry documents, such as the System Operator-Transmission Owner Code (“STC”) and the Connection and Use of System Code (“CUSC”) are available on each Code Owner’s website. The Appendix to this document provides the relevant website addresses.

1.2 First round transitional projects

Qualifying Projects in this first tender round are at different stages of development. This is reflected in the level of detail provided in the PSIMs, with the more advanced projects typically having more detailed PSIMs.

An overview of the Qualifying Projects is provided in Table 2.

1.3 Timetable

The timetable for the QTT stage up to QTT submission is as follows:

Table 1 – Timetable	
Key Stage / Event	Date
Qualification to Tender document made available to Qualifying Applicants	24 September 2009
Qualifying Applicants return signed Confidentiality Agreement(s)	25 September 2009
Information Memoranda made available to Qualifying Applicants following return of signed Confidentiality Agreement(s)	30 September 2009 onwards
Clarification questions to Ofgem (if required)	28 September 2009 to 12 October 2009
Deadline for Qualification to Tender Submission	27 October 2009
Clarification of QTT Submission by Ofgem (if required)	26 October 2009 to end November 2009
Notify Qualifying Applicant and publish Qualifying Bidder shortlist	By 14 December 2009

1.4 Submission and queries

QTT Submissions and all queries regarding the first transitional tender should be submitted through the Ofgem tender portal at <https://ofgem.bravosolution.co.uk>.

2.0 Investment Highlights

2.1 Strong political and regulatory support for offshore transmission

Ofgem has a proven track record of regulatory stability. On the back of the UK Government's commitment to renewable energy and, in particular, the very significant expansion of the UK's offshore wind industry, the independent ownership and operation of offshore transmission in Great Britain enjoys strong political, regulatory and stakeholder support. Ofgem and DECC have been developing the regime for several years, and have consulted widely and regularly on each stage of the development of the regime, taking into account respondents' views.

2.2 First mover advantage

The transitional regime provides potential bidders with an unprecedented opportunity to enter the GB regulated electricity transmission sector. Successful bidders in the transitional regime will be well placed to participate in the much larger 'enduring' regime proposed for those Crown Estate Round 2 projects which do not meet the necessary pre-conditions before the Go-Live date for the regime, and for Crown Estate Round 3 projects. It is expected that the aggregate value of the transmission assets needed for Round 3 is approximately £10 – 12 billion.¹

2.3 Robust and transparent competitive process

To ensure that each stage of the tender process is as fair and transparent as possible for all participants, Ofgem has developed its tender process in accordance with best practice principles. The process is designed to:

- Deliver fit for purpose transmission infrastructure to connect offshore generation;
- Provide certainty and best value to consumers through the competitive process; and
- Attract new entrants to the sector.

2.4 Regulated revenue stream for a minimum 20 year period

The 20-year revenue stream bid by each successful bidder will be incorporated into its transmission licence, and will be fixed, subject to agreed adjustment mechanisms. The revenue stream will be availability based and, unlike onshore regulated networks, will not be subject to an automatic periodic review. The revenue stream will not be exposed to any revenue or performance shortfalls from the in the operation of the offshore wind farms connected to the transmission assets. In the event that the wind farm ceases to operate, the National Electricity Transmission System Operator's ("NETSO") obligation to pay the OFTO will continue. Furthermore, the revenue stream will be fully indexed to the Retail Price Index ("RPI").

Performance availability targets will be established for each Qualifying Project on a case by case basis, informed by the design of the transmission assets, recommended maintenance programmes and developer requirements. However, for the purpose of the QTT stage, Ofgem has assumed a default availability target of 98% based on the performance of operational subsea cables. This is a level which has generally been exceeded by interconnectors and other major electricity transmission lines whose performance is reported in the public domain.

At least 18 months prior to the end of the 20 year revenue stream period, the Authority will assess whether there is likely to be an ongoing need for the offshore transmission assets and will determine the most appropriate course of action, taking into account its statutory duties at the time. These options would include:

¹ According to a study entitled 'Round 3 Offshore Wind Farm Connection Study' prepared for The Crown Estate by National Grid and Senergy econnect in late 2008).

- the extension of the revenue stream and incorporation into the licence (i.e. a traditional price-controlled approach);
- a further tender; or
- revocation of the licence.

For some projects, the OFTO will also have the opportunity to earn additional revenue through the provision of services such as reactive power compensation.

2.5 Creditworthiness of revenue stream counterparty

The OFTO's revenue stream will be paid by the incumbent NETSO which is the entity responsible for the operation of the transmission system in Great Britain and offshore. This system operator role is held by NGET. NGET recovers its costs (including payments it will be required to make to OFTOs) through charges met by users of the National Electricity Transmission System ("**NETS**") and ultimately consumers. NGET has a licence obligation to maintain an investment grade credit rating. NGET is currently rated A- by Standard & Poor's, A3 by Moody's and A- by Fitch Ratings.

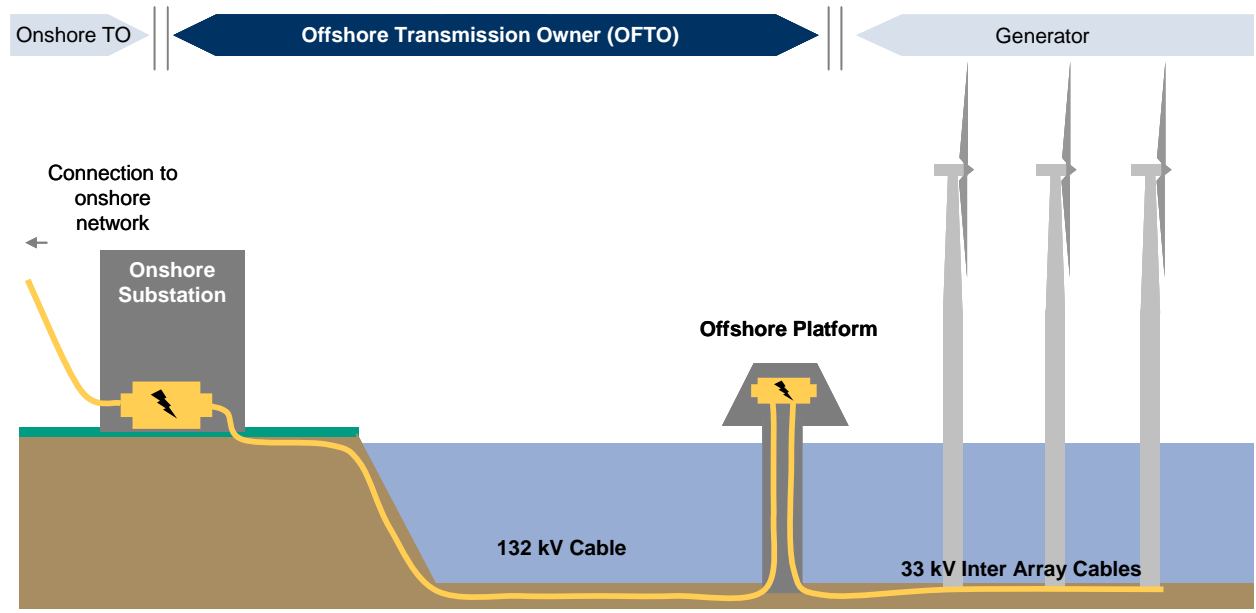
Furthermore, when carrying out its functions, Ofgem must have regard to the need to ensure that licence holders are able to finance the activities which are the subject of statutory obligations placed upon them.

3.0 Overview of the Investment Opportunity

3.1 The transmission assets

The OFTO will own the transmission assets between the offshore point of connection with the generator and the point of connection with the onshore transmission operator. This will include the cables and associated connection equipment. Figure 1 contains a generic diagram of what the transmission asset base to be transferred to the OFTO is likely to comprise. The PSIMs contain details of the individual assets and ownership boundaries that have been defined by the developer.

Figure 1 – Diagram of the Generic Ownership Breakdown



3.2 The revenue stream

Transmission licences will be granted to OFTOs based on a competitive tender process for each transmission asset. Ofgem will determine the outcome of the tender process based on a number of criteria, including the revenue stream bid submitted.

The 20-year revenue stream² bid for the successful bidder will be incorporated into its transmission licence, and will be fixed, subject to agreed adjustment mechanisms and indexed to the RPI. In the event that the wind farm ceases to operate, the obligation of NGET, in its capacity as NETSO to pay the OFTO will continue.

Importantly, the revenue stream will be based on asset availability rather than asset utilisation. This means that as long as the asset is available to transmit electricity to the onshore grid, the OFTO will be entitled to its revenue stream. However, the OFTO will be subject to an operational incentive to ensure that minimum availability of the transmission assets is maintained. In addition, an operational performance security package to ensure continued operational performance will be required in the later stages of the 20 year period.

The revenue stream will ultimately be contained in the special conditions to the OFTO licence granted by the Authority to the successful bidder. The model special licence conditions can be found via the following link:

² For Barrow and Robin Rigg, the 20-year revenue stream will be contingent upon these projects extending their current leases with The Crown Estate. Further information is set out in the respective PSIMs.

<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=90&refer=Networks/offtrans/pdc/cdr/cons2009>.

Ofgem will publish guidance on the special licence conditions during the QTT stage of the process.

3.2.1 Availability and performance

Performance availability targets will be established for each Qualifying Project on a case by case basis, informed by the design of the transmission assets, recommended maintenance programmes and developer requirements. However, Ofgem has assumed a default target availability of 98%, taking into account planned and unplanned outages.

3.2.2 Planned and unplanned outages

Due to the weather conditions during winter, all scheduled maintenance is expected to be carried out during spring and summer. NGET has responsibility under Grid Code and STC for coordinating transmission outages with planned outages on generator and distribution systems.

3.3 A revenue stream bid based on the Estimated Transfer Value

Ofgem, with input from its external advisors, has undertaken an exercise to calculate economic and efficient costs of developing and constructing the transmission assets (the “**Estimated Transfer Value**”) for each of the nine first round transitional projects. This is the summation of the estimated costs to completion and commissioning of the transmission asset including:

- estimated capital cost to completion of the transmission asset, including design costs and risk contingency;
- estimated capitalised interest costs associated with the financing of the design and build of the transmission assets up to commissioning;
- estimated relevant allocation of development costs attributable to the transmission assets incurred by the developer; and
- relevant economic and efficient costs associated with the tender process.

The preliminary Estimated Transfer Values for each project were set out in the Preliminary Information Memorandums. These Estimated Transfer Values for have been updated in the light of information provided by the developers and further analysis by Ofgem. The total Estimated Transfer Value for all 9 projects that have qualified for the first transitional tender process is in the region of £1.1 billion (see table 3 for further details). Further information is provided in the accompanying PSIMs.

At the QTT stage, Qualifying Applicants are required to provide their indicative revenue stream in their submissions. The QTT Document sets this out in further detail. At the ITT stage, Qualifying Bidders will be required to bid a revenue stream, calculated on its required return on investment on the Estimated Transfer Value (which will be the price at which a prospective OFTO must assume, for the purposes of the tender, it will acquire the relevant assets) and the ongoing cost of financing, maintaining, managing and decommissioning the relevant transmission asset.

3.4 The Final Transfer Value

Once assets are constructed and the details of the asset transfer have been agreed, Ofgem will undertake its final assessment of the economic and efficient cost of developing and constructing the transmission assets (the “**Final Transfer Value**”). For projects operational before Go-Live, Ofgem intends to undertake its final cost assessment prior to asset transfer and licence grant.

For projects which are commissioned after the Go-Live date, the asset transfer and licence grant will need to occur on commissioning. As such, Ofgem intends to undertake its final cost assessment some time after asset transfer and licence grant.

The revenue stream of the OFTO will be adjusted by Ofgem for any differences between the Estimated and Final Transfer Values. Where the Final Transfer Value is determined prior to asset transfer, the

adjustment to the OFTO's revenue stream will be reflected in the revenue stream at licence grant. Where the Final Transfer Value is determined after asset transfer the adjustment to the OFTO's revenue stream to take account of any differences between the Estimated and Final Transfer Values will be dealt with through an adjustment mechanism in the licence.

More information on this will be set out in the tender guidance document on the process to asset transfer.

3.5 The OFTO licence

The Offshore Transmission Licence sets out the obligations and activities of the OFTO. Under the licence, Ofgem intends that an OFTO would be entitled to the revenue stream for a 20 year period during which there is no automatic periodic price review. The revenue stream would reflect the revenue bid of the OFTO during the tender process, which should be sufficient to meet the obligations and activities of the OFTO.

The OFTO will invoice the NETSO a monthly charge based on its allowable revenue stream in accordance with the terms of the STC. The NETSO is then required to pay the OFTO in accordance with the STC provisions. After 20 years, extended further revenue stream may be set, or the licence may be revoked or re-tendered.

Under the terms of the licence, the OFTO may also be required to offer up to 20% of the Final Transfer Value in providing extra transmission capacity over and above what it is contractually required to provide on the day that the licence is granted, should there be a user application to the NETSO for additional capacity at the offshore connection point. This requirement may occur at any point over which the licence is held.

Under the terms of the licence, the OFTO may also be appointed as an OFTO of last resort. This would potentially require an OFTO to take on the assets and obligations in respect of another project (subject to satisfying the Authority that it is capable to undertake those obligations without unduly impacting on its ability to undertake its existing obligations and activities). The process for appointing an OFTO of Last Resort is set out in standard condition E21 and explained further in the OFTO of Last Resort guidance document that will be published shortly.

3.6 Codes and Standards

There are a number of industry codes and standards that underpin the electricity market in GB. The industry codes include the Balancing and Settlement Code ("**BSC**"), the Connection and Use of System Code ("**CUSC**"), the System Operator-Transmission Owner Code ("**STC**"), the Grid Code, the Distribution Code and the Distribution Connection Use of System Code ("**DCUSA**"). Electricity transmission licensees are required to design and operate transmission systems (including offshore transmission systems) at least to the minimum requirements set out in the NETS Security and Quality of Supply Standard ("**SQSS**").

Offshore generators connected to an offshore transmission system are required to comply with CUSC, BSC and Grid Code. OFTO's are required by the transmission licence to comply with the NETS SQSS and the STC. The STC requires OFTOs to comply with a limited number of Grid Code requirements.

The Grid Code also reflects the requirement for an OFTO to ensure that its offshore transmission system complies with the NETS SQSS.

Each of these documents have recently undergone a detailed review to identify changes appropriate for offshore transmission. Changes to these documents were implemented by the Secretary of State on 24th June 2009. The Appendix to this IM provides a more detailed overview of these documents.

3.7 Ownership boundary at offshore connection point

Developers of first round transitional projects have completed detailed designs for their offshore project in advance of tender commencement. Ahead of tender commencement, Ofgem and the NETSO have encouraged developers to define the ownership boundary arrangements for the offshore connection point. The proposed ownership boundary arrangements may differ from the default arrangements as set out in the CUSC, in which case they would be subject to the NETSO's agreement. Each of the PSIMs has detailed information on the ownership boundaries.

The NETSO has offered modified contracts to developers of each of the first round transitional projects to specify offshore grid entry points. These offers reflect the terms of the existing agreement in place with the developer and the onshore network licensee.

Ofgem is of the view that developers of first round transitional projects would only require an amendment to the identified ownership boundary arrangements (and an offer from the NETSO to agree to vary existing contractual agreements) in circumstances whereby they can demonstrate that an unforeseen event has occurred during, and as a consequence of, the tender process.

If there are other reasons for amendments to the contractual terms agreed between the developer and NETSO, Ofgem considers that these would be managed through the process defined in the CUSC for the modification of bilateral agreements for connection to and use of the NETS.

3.8 Reactive power

Offshore generators connected to and/or using the offshore transmission system will be required to meet the Grid Code voltage and reactive power requirements that apply at the point of connection. The STC and Grid Code define obligations in respect of reactive power capability range requirements at the onshore interface point, between the offshore transmission system and onshore network and at the offshore connection point respectively. As a default, the OFTO is responsible for providing a defined reactive power capability range at the onshore interface and to provide voltage control facilities. The default requirement for the offshore generator is to be capable of operating at unity power factor at the offshore connection point. Variation from these default arrangements is permitted by agreement with NGET. This is a potential opportunity for the OFTO to earn additional revenue.

3.9 Redundancy

Any offshore transmission system should be designed according to the planning criteria as defined in the NETS SQSS. The criteria present the minimum security and associated redundancy requirements and cover all elements of an offshore transmission system including the offshore transmission circuits and equipment on the offshore platform, the offshore transmission circuits between one offshore platform and another or from the offshore platform to the point of connection onshore. The criteria set the consequences, expressed in terms of a level of power loss, of various types of contingencies such as an outage of a single offshore transformer or transmission circuit, busbar section or busbar section circuit breaker on the offshore transmission system. For example, a planned outage or a fault outage of a single transformer circuit should not result in the loss of more than 50% of the offshore wind farm capacity or 1000MW (e.g. so called normal infeed loss risk), whichever is the smaller.

A level of redundancy in offshore transmission systems is highly project specific with almost no project designed with full redundancy with respect to security of connection. That is, in most cases, wind farm output would need to be constrained in the event of any subsea cable or offshore transformer outage. Any offshore transmission system should be designed according to the planning criteria as defined in the NETS SQSS.

3.10 O&M guidance

Several developers have indicated that they intend to offer an O&M service to those Qualifying Applicants that are shortlisted following the completion of the QTT stage (“**Qualifying Bidders**”). Where O&M plans have been developed, some indication of likely scope has been provided in the PSIM. Conversely, where O&M plans are still being developed, the information provided in the PSIM may be limited to the intention to make an offer. However, for the purposes of preparing a response to Section 3 of the QTT questionnaire, Qualifying Applicants should form their own view of expected O&M costs.

4.0 Tender Process for the Grant of the OFTO Licence

4.1 Overview

The steps to be taken by Ofgem in selecting an OFTO for each Qualifying Project are summarised in the following paragraphs.

OFTO licences will be granted using the existing regulatory structure, amended as required for the offshore context. However the tender process has been designed to draw on the UK Government's Public-Private Partnership 'best practice', for example that adopted for the Private Finance Initiative.

4.2 Stages of tender process

The tender process follows a number of defined stages:

4.2.1 Pre-Qualification

The outcome of the Pre-Qualification ("PQ") stage was a long list of qualifying applicants who are now being invited to participate in the next stage of the process, the QTT stage. This 'long list' of Qualifying Applicants is published on Ofgem's website at:

<http://www.ofgem.gov.uk/Media/PressRel/Documents1/Offshore230909.pdf>

4.2.2 Qualification to Tender

The second stage, QTT, will involve a detailed evaluation of each bidder's proposed approach to becoming an OFTO in respect of each project for which it intends to bid. Bidders will be scored based on their responses against a detailed set of criteria including in respect of their approach to financing and their operational and managerial proposal. The requirements for responding to this part of the tender process is set out in the QTT Document, The evaluation criteria and scores are also set out in this document.

The QTT stage for the first tender round commenced on 24 September 2009. The deadline for QTT submissions is 27 October 2009.

Ofgem anticipates that up to five bidders for each project will be invited to submit formal bids in the next stage of the process, the ITT stage.

4.2.3 Invitation to Tender

The main purpose of the ITT stage is to permit Ofgem to identify a preferred bidder for each project, based on a fair and transparent competition. Each project will be subject to a separate tender.

At ITT stage a full data room for each project will be made available to shortlisted bidders, populated by Ofgem with information predominantly provided by the offshore developer. The final contents of the data room are expected to include, without limitation, all contracts, leases, warranties, details of assets and liabilities, investment and operating plans, sea-bed surveys and evidence of compliance with all applicable legislation, regulations, etc, in each case relating to the transmission assets. It is also expected that the data room will include sufficient information relating to the relevant generation project to enable potential OFTOs to make an informed investment decision.

Tenders received from shortlisted bidders in the ITT stage will also be scored. The most important element of tenders in respect of each project will be the fixed revenue stream each bidder requires to compensate it for the cost of acquisition, financing and operation of the transmission assets over the initial 20-year revenue period.

Qualifying Bidders may be able to bid for more than one project, subject to the Qualifying Bidder being on more than one shortlist. In these instances, separate bids will be required to be submitted on a project-by-project basis. Bidders will also be permitted to submit 'variant' bids for any combination of projects for which they have been shortlisted, identifying the economic effect of any synergies or economies of scale that might be achievable.

4.2.4 Best and Final Offer

Where it is not possible to identify a clear preferred bidder after the ITT stage, Ofgem has reserved the right to ask a small number of bidders to submit their best and final offer (“**BAFO**”) before making its final selection.

The BAFO stage is not mandatory and will only be applied if considered necessary by Ofgem.

4.2.5 Preferred Bidder

Following either the ITT stage or a BAFO stage, Ofgem will announce the Preferred Bidder for each Qualifying Project. It will also identify the outstanding conditions that the Preferred Bidder must meet before it is confirmed as the Successful Bidder. Following a standstill period, Ofgem would expect to grant the licence to the Successful Bidder.

4.2.6 Process to asset transfer

Ofgem has established a standard process by which each project will achieve final transfer of the transmission assets and successfully complete the grant of the OFTO licence for a successful OFTO.

The key milestones in the process are:

- Preferred Bidder
- Successful Bidder; and
- Licence grant, asset transfer and contractual completion

Each project will require its own detailed programme, which will be released at the ITT stage. At this stage, Ofgem has established guidance which will be further developed on a project specific basis. This tender guidance document incorporates detailed information regarding the Estimated Transfer Value and any necessary adjustments as a result of arriving at the Final Transfer Value.

For the purpose of its bid, the Estimated Transfer Value equates to the price that the preferred bidder should assume it must pay the developer to acquire the commissioned transmission assets.

Further information will be provided in the tender guidance document on the process to asset transfer.

4.3 Sale and Purchase Agreement

Ofgem has determined that the appropriate mechanism to effect the asset transfer is by means of a Sale and Purchase Agreement (“**SPA**”). A generic model SPA has been published by Ofgem which can be found, along with associated commentary, via the following link:

<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=2&refer=NETWORKS/OFFTRANS/OTT/TE NDOCS>.

Developers are currently using this model to create project specific SPAs to reflect the specific requirements and circumstances of their qualifying projects. These will be available as part of the documentation released at the ITT stage of the tender process.

Qualifying Applicants are required to provide comment on this model SPA as part of their response to the QTT Questionnaire.

5.0 Qualifying Projects

5.1 The first transitional tender

Table 2 identifies those projects which have qualified as transitional projects and have met the necessary tender entry conditions for first tender round, and sets out their Estimated Transfer Values and expected asset transfer date. Further detailed information is available in the PSIMs.

Table 2 – Qualifying Projects				
Project	Developer(s)	Estimated Transfer Value	MW	Expected Asset Transfer Date
Barrow	DONG Energy, Centrica	£36.5m	90	June 2010
Robin Rigg	E.On	£57.3m	180	June 2010
Gunfleet Sands I & II	DONG Energy	£48.2m	164	June 2010
Sheringham Shoal	StatoilHydro, Statkraft	£182.1m	315	April 2011
Ormonde	Vattenfall	£101.1m	150	March 2011
Greater Gabbard	SSE/Airtricity, RWE Innogy	£316.6m	504	Nov 2010 ³
Thanet	Vattenfall	£163.1m	300	June 2010
Walney 1	DONG Energy	£101.8m	178	Oct 2010
Walney 2	DONG Energy	£105.0m	183	Aug 2011
TOTAL		£1.111.7m	2,064	

Figure 2 illustrates the location of these Qualifying Projects.

³ Qualifying Applicants should be aware of the specific arrangements for Greater Gabbard. Further information is set out in their PSIM.

Figure 2 – Map showing location of projects that have qualified for the first transitional tender

1	Barrow
2	Robin Rigg
3	Gunfleet Sands I & II
4	Sheringham Shoal
5	Ormonde
6	Greater Gabbard
7	Thanet
8	Walney 1
9	Walney 2



5.2 Qualification criteria

All projects identified in Table 2 have demonstrated that they have met the qualifying project and tender entry criteria set by Ofgem.

5.2.1 Qualifying Project conditions

All Qualifying Projects have demonstrated that they have entered into a bilateral connection agreement with the NETSO, or entered into an agreement or accepted an offer of an agreement, with the electricity distributor responsible for the distribution system to which the transmission assets are or are intended to be connected. In addition they have;

- obtained all necessary consents and property rights for the transmission assets to be constructed and maintained;
- completed construction of, or entered into all necessary contracts for the construction of the transmission assets; and
- secured financing to construct the transmission assets (“financial close” or equivalent, such as final investment decision and/or board approval).

5.2.2 Tender Entry conditions

Over the summer, all Qualifying Projects were required to meet a number of other conditions set by Ofgem in accordance with the regulatory framework for offshore electricity transmission. In particular, Qualifying Projects:

- provided information to Ofgem to enable it to issue an Information Memorandum and establish a data room;
- provided a written warranty to Ofgem that the information provided is to the best of its knowledge true, accurate and complete in all material respects;
- populated Ofgem’s model SPA to reflect the specific requirements and circumstances of the project, and provided an undertaking that it will work with Ofgem to finalise this document as soon as is reasonably practicable; and
- provided a number of other undertakings to Ofgem, specifically to:

- provide information and documentary updates where necessary to enable Ofgem to update the data room;
- respond to queries from Ofgem and respond to clarifications submitted by bidders within reasonable timeframes;
- transfer any property, rights or liabilities in or relating to the transmission assets to the successful bidder, in accordance with the SPA; and
- if applicable, put in place an appropriate internal information barrier to prevent information passing between the team working on the project and any bidding team.

6.0 Regulatory Framework and Contractual Structure

6.1 Ofgem

Ofgem is the independent regulator of the gas and electricity markets in Great Britain.

Since taking powers in the Energy Act 2004, the Government has worked with Ofgem to establish an offshore electricity transmission licensing regime to regulate the conveyance of electricity along high voltage lines offshore (defined in the EA 2004 as those with a nominal voltage of 132 kV or more) and associated plant and equipment which connect offshore generating stations to the onshore electricity network.

6.2 Overview of the regulatory framework for offshore electricity transmission

The offshore electricity transmission regime has been developed and refined with stakeholder input over the past four years, and the consultation process for the design of the regulatory regime culminated in a final statement published in June 2009. The regime has been designed to ensure connection to the onshore grid in a timely and cost effective manner, whilst maintaining the integrity of the system as a whole and achieving best value for electricity consumers.

Ofgem expects that some Qualifying Applicants may not have had significant experience of this framework and as such, this section provides a diagrammatic overview of the key relationships. Further detail is provided in the Appendix to this IM.

In the GB electricity industry, the regulatory framework is set out in a number of instruments including primary legislation, secondary legislation, licences, industry codes and technical standards. Figure 3 summarises this framework.

Figure 3 – Regulatory Framework

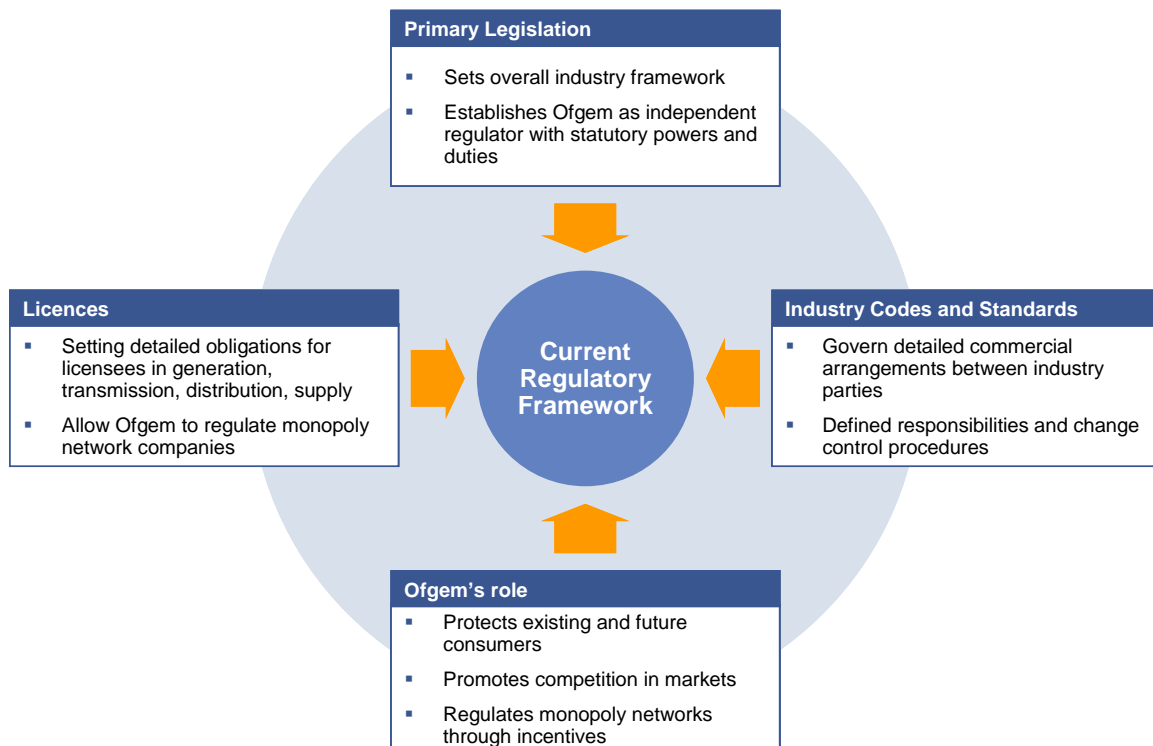
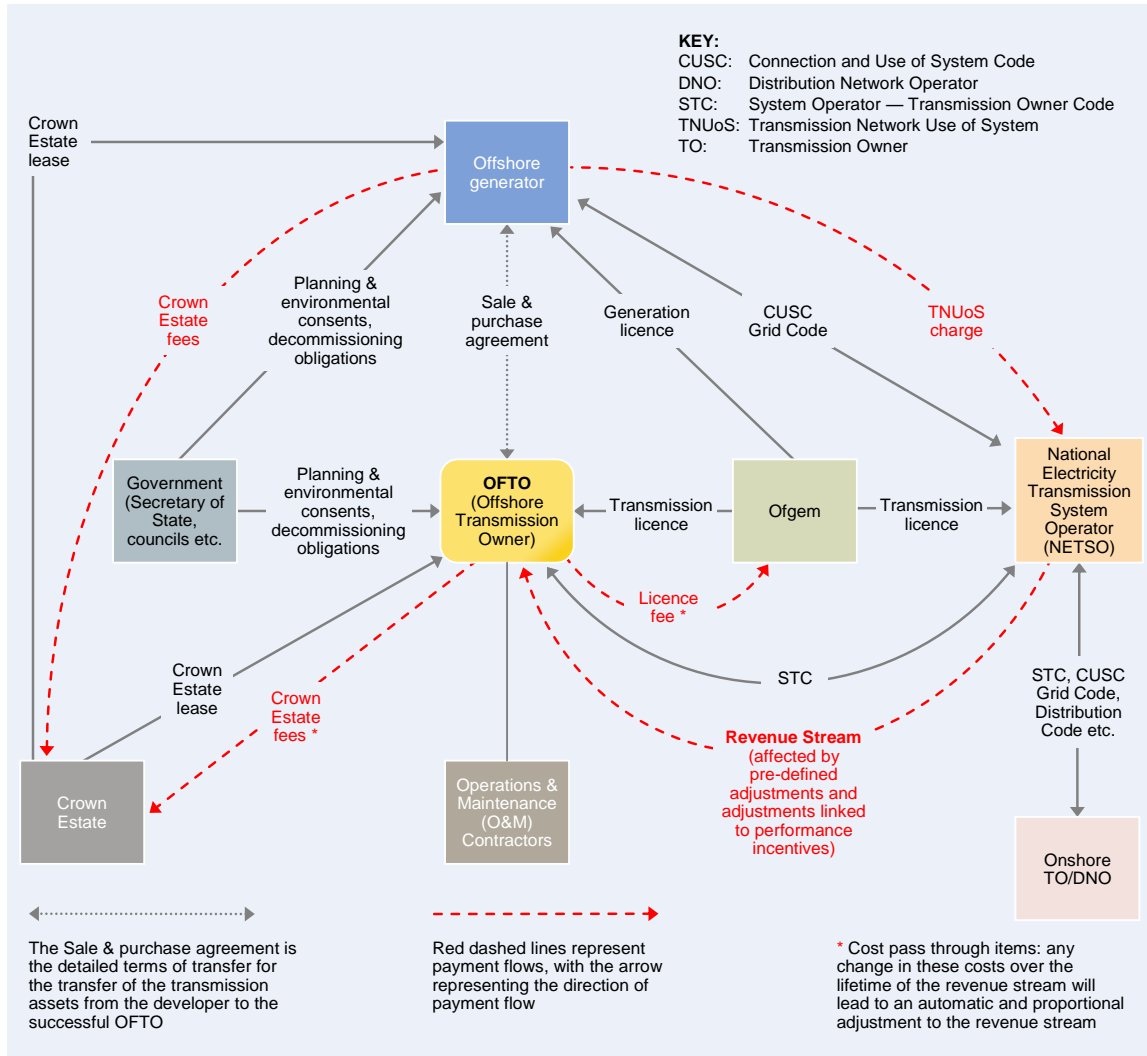


Figure 4 provides an outline the contractual structure governing OFTO activities, identifying contractual counterparties.

Figure 4 – Key Parties and Outline Contractual Structure



Appendix: Regulatory Regime in more depth

Introduction

The regulatory framework for the GB electricity industry is set out in a number of instruments. These include primary legislation, secondary legislation, licences granted by the Authority, industry codes and technical standards.

UK primary legislation

The key pieces of UK legislation which are applicable to the OFTO opportunity are as follows:

Electricity Act 1989

The Electricity Act 1989 (the “**Electricity Act**”) is the primary piece of legislation for the electricity industry in Great Britain. Three key elements of the Electricity Act are:

- 1) It provides for the Authority's principal objective and general duties,
- 2) It outlines the way in which the Authority must carry out its functions.
- 3) It provides for the granting and modification of licences to transmit, distribute, generate and supply electricity in Great Britain, including the competitive tender process for transmissions licences for OFTOs.

Energy Act 2004

The Energy Act 2004 (“**EA 2004**”) amended the Electricity Act to facilitate the introduction of the offshore electricity transmission regime, including the extension of the prohibition on the transmission of electricity to the offshore environment without a licence. Section 92 of the EA 2004 enables the Authority to make regulations to facilitate the making of a determination on a competitive basis of the person to whom an offshore transmission licence is to be granted. It also enabled the Secretary of State to designate changes to relevant industry codes and the standard licence conditions of the Transmission Licence to accommodate offshore electricity transmission. The Energy Act 2004 also extended the electricity transmission system operator role offshore.

The EA 2004 applies a special insolvency regime to entities which operate or own essential energy infrastructure known as an ‘energy administration’. The objective of an energy administration regime is to secure that essential energy infrastructure (such as electricity transmission systems) is, and continues to be, maintained and developed as an economical system in the event of financial failure. These arrangements would apply to OFTOs. The details of energy administration are set out in Part 3 Chapter 3 of the EA 2004.

Energy Act 2008

The Energy Act 2008 (“**EA 2008**”) amended the Electricity Act to introduce the ability for the Authority to make a property transfer scheme (in respect of the transitional regime) where commercial negotiations for the transfer of assets between parties fail. They also include provisions for the Authority to recover its costs for running these tenders.

UK secondary legislation

Tender Regulations

The Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations 2009 provide the legal framework for running the tender process. In summary, they provide:

- 1) A requirement for tenders to be run from a date set by the Authority in each year;

- 2) A requirement on the Authority to publish certain information and tender documentation;
- 3) A requirement on bidders to respond within specified timeframes;
- 4) A requirement on the Authority to assess bids in accordance with pre-determined criteria;
- 5) The requirements needed prior to the identification of a Preferred Bidder;
- 6) A requirement on the Authority to put in place appropriate tender rules ; and
- 7) A requirement on the Authority to publish its methodology for recovering its costs of running the tender process.

Relevant EU legislation

Third Package

A package of legislation on EU gas and electricity markets (commonly referred to as the “**Third Package**”), entered into force on 3 September 2009. This follows adoption by heads of state and national energy ministers at the EU Council of Ministers meeting on 3 July and publication in the EU Official Journal on 14 August 2009. The objective of the Third Package is to liberalise further EU energy markets. One of the areas covered by the Third Package is unbundling which essentially involves the separation of electricity generation and/or supply from transmission. The Third Package envisages a number of options for unbundling. The default position is that of **full ownership unbundling**, the provisions for which are set out in Article 9.1 of Directive 2009/72/EC (the Electricity Directive). One element of this model is that the same person or persons cannot “*directly or indirectly exercise control over an undertaking performing any of the functions of generation or supply, and directly or indirectly exercise control or exercise any right over a transmission system operator or over a transmission system*” (and vice versa). The concept of “*any right*” is set out in Article 9.2 and includes the power to exercise voting rights, to appoint members of the supervisory board, the administrative board or bodies legally representing the undertaking or holding of a majority share. Alternatively, the **Independent System Operator (ISO)** model and the **Independent Transmission Operator (ITO)** model (set out in Article 9.8 and also Article 13 and Chapter V of the Electricity Directive respectively) *may* apply to an OFTO where, on 3 September 2009, the transmission system belongs to a vertically integrated undertaking. Finally, an OFTO may be eligible to apply for a derogation to full ownership unbundling if it can be demonstrated that their arrangements on 3 September 2009 guarantee more effective independence of the transmission system operator than those provided for by an ITO model.

The Third Package requires that Ofgem certify, by March 2012, all “Transmission System Operators”, which definition would appear to include OFTOs (this is a point on which representations are invited and which Ofgem will consider further in due course), as compliant with full ownership unbundling, or *potentially* one of the alternative models set out above. Ofgem will be consulting on the various issues in due course. This certification process will necessarily be run separately to the tender process and will follow different timescales. It is important to note that any decision taken by Ofgem to shortlist a bidder or to grant a licence at the end of the tender process should not be taken as a decision on certification. It is for all qualifying applicants to satisfy themselves that they are compliant with one of the models set out above to reduce the risk of a certification decision being taken which is not compatible with the outcome of the tender process.

Green Package

The EU has introduced four new directives (commonly referred to as the “**Green Package**”) that are designed to address the EU’s environmental priorities. These directives are due to be implemented by Member States by 5 December 2010.

The new Renewables Directive sets out binding targets for the deployment of renewable energy by each Member State. The new Directive requires Member States to provide renewable generation with either priority access or guaranteed access to the grid. It also provides for increased flexibility in how Member States reach their target. For example, Member States will be allowed to engage in statistical transfers of renewable energy production between them and to undertake joint projects together which can count towards their targets.

The Green Package is also made up of a directive on the EU Emissions Trading Scheme (“ETS”) for 2013 onwards (phase 3). Under this phase, there will be full carbon auctioning from 2013 for the power sector (with exclusions for newer Member States). Non-power installations will be required to purchase 20% of the required allowance in 2013, rising to 70% in 2020.

Utilities Directive

Once an OFTO is appointed, it will need to satisfy itself of the application of the Utilities Directive and, as appropriate, its ongoing compliance with it.

Roles of key parties

Ofgem/the Authority

Ofgem is the office that supports the Gas and Electricity Markets Authority, which is the regulator for the gas and electricity markets in Great Britain. Protecting consumers is Ofgem’s first priority and it does so by promoting competition where appropriate, and regulating network monopolies where it is not. These monopoly companies are typically subject to an RPI-X form of regulation, with periodic reviews occurring every five years.

The offshore electricity transmission regime represents a departure from Ofgem’s typical form of network regulation, with licences granted by means of a competitive tender process with revenue streams for 20 years.

Ofgem E-Serve has been recently established to deliver a number of programmes and schemes on behalf of the Government, including the offshore electricity transmission regime. Ofgem E-Serve is a part of Ofgem.

Department for Energy and Climate Change (“DECC”)

DECC is the Government department responsible for implementing energy policy in the UK, and holds overall responsibility for the UK’s strategy on renewable energy. DECC has worked with Ofgem over a number of years to design and implement the new regulatory regime for offshore transmission, taking key decisions along the way. This has included with respect to Ofgem running the competitive tender process and making the necessary amendments to codes and licences to implement the offshore electricity transmission regime.

The Crown Estate

As landowner of the seabed and areas of foreshore by virtue of the Crown Estate Act 1961, The Crown Estate’s permission is necessary to place structures on or pass cables over the seabed and its foreshore.

In addition to permission from the landowner, potential developers also require statutory consents from a number of Government departments responsible for the offshore wind development process. Only when all the necessary statutory consents are obtained will The Crown Estate grant a lease for development. The Crown Estate issues leases for the development of sites within the 12 nautical mile (“nm”) territorial limit, whilst the EA 2004 gives it rights to issue leases for development beyond the territorial limit within Renewable Energy Zones (“REZ”) out to 200nm.

Round 1 and 2 offshore wind projects were generally granted full term leases of 22 and 40 years, respectively, although for the largest round two projects (with a potential installed capacity of 500MW or more) full term leases for 50 years were granted. On 6th July 2009, The Crown Estate announced that all wind farm operators will be given the opportunity to extend their lease terms to 50 years.

The existing Crown Estate leases that have been granted are in a combined form which covers both the offshore windfarm site and the cable route to shore. With the introduction of the offshore transmission regulatory regime, it will be necessary for these leases to be separated. The Crown Estate has written to developers setting out their proposed approach for managing this transition. They have indicated that they would expect to replace the existing lease agreements at the point of asset transfer between the developer and the OFTO such that new separate lease agreements are held, one covering the windfarm site and the other covering the cable.

Department for Environment Food and Rural Affairs (“Defra”)

Defra have proposed amendments to the Deposits in the Sea (Exemptions) Order 1985 to reflect the Offshore Transmission regime. The proposal considers a requirement for new Offshore Transmission Owners to obtain a licence under Part II of the Food and Environment Protection Act 1985 for the deposit of subsea cables connected to offshore wind turbines. The closing date for responding to this consultation is 26 October 2009. The consultation can be viewed at www.defra.gov.uk/corporate/consult/offshore-cable-licenses/index.htm.

Ofgem intends to respond to this consultation separately.

National Electricity Transmission System Operator (“NETSO”)

NGET is the system operator for transmission system in GB and offshore areas. Currently the NETS is made up of three onshore transmission systems. NGET owns and maintains the transmission network in England and Wales. There are also two transmission owners in Scotland, SPT in the south and SHETL in the north.

Offshore generator

Generators are the owners and developers of the offshore wind farm projects. Throughout Ofgem’s consultations on the new regime generators have been given the opportunity to provide responses. During the first transitional tender round, generators will be responsible for constructing the transmission assets to connect the offshore infrastructure to an onshore network. They will contract with the NETSO for a connection to the NETS at an offshore connection point and will be responsible for paying charges to the NETSO for the ongoing use of the transmission system. These transmission assets will be transferred to the new OFTO upon completion at the transfer value determined by Ofgem.

Industry framework documents

Introduction

In addition to the applicable legislation and licences, the regulatory requirements for electricity transmission within the NETSO’s area are contained within detailed industry codes and technical standards. These are collectively known as the ‘Industry Framework Documents’. There are provisions contained in the relevant licences which oblige the licence holder to comply with (and in some cases have in force) the requirements of these documents. These documents may evolve over time, and there are governance arrangements in place to ensure that any changes are made in a transparent and consistent way.

Bidders will be required to satisfy themselves of the requirements of each relevant industry code and technical standard. Each of the applicable codes is summarised briefly in the following sections.

Balancing & Settlement Code

The Balancing & Settlement Code (“**BSC**”) defines the commercial arrangements for electricity balancing and settlement within the NETSO area. Parties to the BSC include NGET, trading parties, interconnector administrators and suppliers. The BSC sets out the detailed arrangements for:

Balancing – allows each party to the BSC to advise the NETSO of its terms for making a change to its forecast export to or import from the NETS close to real time. The energy balancing aspect allows parties to make submissions to the NETSO to either buy or sell electricity into/out of the market at close to real time in order to keep the system from moving too far out of phase.

Settlement – provides for the reconciliation of actual exports (from generators) and imports (from suppliers) with the forecast, contracted position. The settlement aspect relates to monitoring and metering the actual positions of generators and suppliers (and interconnectors) against their contracted positions and settling imbalances when actual delivery or offtake does not match contractual positions.

Metering – specific standards are defined for equipment used to record electricity flows for use in the settlement processes.

The BSC is owned by Elexon and a copy of the document can be found on Elexon's website:

<http://www.elexon.co.uk/bscrelateddocs/bsc>

Connection and Use of System Code

The Connection and Use of System Code (“**CUSC**”) is a legal document that constitutes the contractual framework for connection to or use of the NETS. Key parties to the CUSC include the NETSO, generators, Distribution Licensees and suppliers (although this is not an exhaustive list). The CUSC defines arrangements for:

- Connection – The CUSC sets out arrangements that define the stages for connection. These include: application; connection; and termination of a connection agreement.
- Use of system – The CUSC sets out arrangements that define the stages for application to, and termination of, a use of system agreement, including the different types of transmission access products available to user's of the NETS.
- De-energisation and disconnection – The CUSC sets out arrangements that cater for de-energisation and disconnection of the system for safety issues and non payment reasons.

The CUSC is owned by NGET. A copy of the document is on NGET's website:

<http://www.nationalgrid.com/uk/Electricity/Codes/systemcode/contracts/>

A summary of the CUSC prepared by NGET can be found at:

<http://www.nationalgrid.com/uk/Electricity/Codes/systemcode/cuscsummary/>

Distribution and Connection Use of System Agreement

The Distribution and Connection Use of System Agreement (“**DCUSA**”) is a multi-party contract between Distribution Licensees, suppliers and generators which constitutes the contractual framework for the connection to and use of the electricity distribution network. It replaced numerous bilateral contracts to provide a consistent approach to the relationship between these parties within the electricity industry.

The DCUSA is owned by DCUSA Limited. A copy of the document can be found on DCUSA Limited's website:

<http://www.dcusa.co.uk/Public>

Grid Code

The Grid Code is a technical code which sets out, among other things, the planning, connection conditions and testing requirements for the management of the NETS. It is designed to permit the development, maintenance and operation of the NETS. Parties to the Grid Code are NGET and all users of the NETS. OFTOs will be obliged by the STC to comply with specific sections of the Grid Code.

The Grid Code is owned by NGET. A copy of the document can be found on NGET's website:

<http://www.nationalgrid.com/uk/Electricity/Codes/gridcode/gridcodedocs/>

System Operator – Transmission Owner Code

The System Operator – Transmission Owner Code (“**STC**”) defines the obligations and responsibilities of the NETSO and transmission licensees that provide transmission services to the NETSO. Current parties to the STC are NGET, SP Transmission Limited and Scottish Hydro-Electric Transmission Limited. Each OFTO, as a new Transmission Licensee, will be required to accede to the STC in accordance with its Licence.

The STC makes provision for certain interactions between the Transmission Licensees and the NETSO as follows:

- The provision of transmission services by the Transmission Licensees to the NETSO;

- Directions from the NETSO to configure the NETS;
- Transmission outage planning;
- Joint transmission investment planning;
- Governance of the STC and amendments to it (including accession to the STC); and
- Dispute resolution.

The STC is owned by its current parties. A copy of the document can be found on NGET's website:

<http://www.nationalgrid.com/uk/Electricity/Codes/sotocode/Library/>

A summary of the STC prepared by NGET can be found at:

<http://www.nationalgrid.com/NR/exeres/005F0E90-234C-4DBB-BCAB-7F3700E92347.htm>

NETS Security and Quality of Supply Standard

The NETS Security and Quality of Supply Standards (“**NETS SQSS**”) set out a coordinated set of criteria and methodologies that Transmission Licensees must use in the planning and operation of the NETS. The criteria presented in the NETS SQSS represents the minimum requirements for the planning and operation of the NETS. Additional criteria, for example covering more detailed and other aspects of quality of supply, are contained in the Grid Code and the STC, which should be read in conjunction with the NETS SQSS. A copy of the document can be found on NGET's website:

<http://www.nationalgrid.com/uk/Electricity/Codes/gbsqsscode/DocLibrary/>

The OFTO Licence

Overview

The Electricity Act prohibits certain activities unless the person carrying out that activity is licensed (or has been granted an exemption from having a licence). Ofgem grants licences for these activities in accordance with the Electricity Act, specifically:

- Transmission of electricity;
- Distribution of electricity;
- Generation of electricity;
- Supply of electricity; and
- Operation of an interconnector

A licence is formed of three elements:

- The Terms (these are set by the Authority and are set out in Schedules to the licence);
- The Standard Conditions (which may be common to all licensees, or certain classes of licensee, for example Electricity Transmission licensees) ; and
- The Special Conditions (which are conditions specific to each individual licensee)

The standard licence conditions and draft special conditions of the OFTO licence are available on Ofgem's website: <http://www.ofgem.gov.uk/Networks/offtrans/pdc/cdr/cons2009/Pages/Cons2009.aspx>. An overview of certain key conditions is provided in the following section.

Terms

The terms of the licence are set out in separate schedules to the licence. An overview of these is provided below:

Schedule 1: Specified Area

The specified area for the OFTO licence is Great Britain, the territorial sea adjacent to Great Britain and any Renewable Energy Zone.

Schedule 2: Revocation

Schedule 2 sets out the reasons for which the Authority may revoke an OFTO licence. These include:

- where the licensee agrees in writing with the Authority that the licence should be revoked;
- if the licensee fails to pay any financial penalty by the due date; and
- if the licensee has ceased to carry on, or has abandoned, the transmission business, or if the licensee has a receiver or the whole or any material part of its assets, has an administration order made in relation to it, passes any resolution for winding up or becomes subject to an order for winding up by a court of competent jurisdiction.

Standard conditions

Standard conditions typically cover the obligation of licensees. The transmission licence is currently divided into five sections, A to E. The transmission licence obligations have been grouped into sections that reflect that there are now three different types of transmission licensee. In summary:

- Section A contains general obligations that apply to all types of transmission licensee;
- Section B contains obligations that apply to both types of onshore transmission licensee;
- Section C contains obligations that apply to transmission licensees with system operator responsibilities;
- Section D contains obligations that apply to onshore transmission licensees that do not have system operator responsibilities; and
- Section E contains obligations that apply to offshore transmission licensees that do not have system operator responsibilities.

For the purpose of offshore transmission only sections A and E are applicable. Qualifying applicants need to be aware of the entire package of standard conditions, however attention is drawn to the following:

Standard Condition E6: Prohibition of Cross-Subsidies

Standard Licence Condition E6 prevents the OFTO from giving (or receiving) a cross subsidy to (or from) any other of its businesses or affiliates.

Standard Condition E7: Restriction on Activities and Financial Ring Fencing

Standard Condition E7 ensures the principal activity of the entity is transmission and that it operates on a “stand alone” basis.

Standard Condition E11: Credit Rating of Licensee

Standard Licence Condition E11 requires that the OFTO either holds an investment grade credit rating, or else proposes alternative financial arrangements to the Authority which demonstrate sufficient financial standing.

Special conditions

Special conditions are conditions that apply only to an individual licensee. They are grouped based on the particular purpose they serve:

- Section A includes “mechanical” parts of the licence, including definitions and implementation provisions for the offshore transmission regulatory regime;
- Section B details the geographic area in which they are licenced

- Section C sets out the obligations relating to operation and management of the licensee's business, including, and the business separation and compliance requirements;
- Section D outlines the regulatory reporting requirements; and
- Section J specifies the revenue entitlement of the licensee, and the elements that affect it, namely revenue adjustments and performance incentives.

Qualifying Applicants need to be aware of the entire package of special conditions, however attention is drawn to the following:

Special Condition C2: Separation and Independence of Transmission Businesses

Special licence Condition C2 requires the OFTO to be a managerially and operationally independent entity, with a dedicated management and board. Under C2, the OFTO will be required to submit a statement to the Authority as to how it intends to effect business separation in accordance with its licence obligations.

The purpose of C2 is to ensure that the OFTO is afforded sufficient management and operational resources to fulfil its licence obligations, particularly where it is part of a corporate group, and that clear lines of accountability for the licensed entity are in place.

Special Condition J2: Restriction of Transmission Revenues: Revenues from Transmission Owner Services

Special Licence Condition J2 is the condition that sets out the annual revenue allowance that the transmission owner may earn from its transmission owner services. This revenue allowance will be determined through the tender process.

The condition also includes a correction factor that allows for any errors in payment to be compensated.

Special Condition J3: Restriction of Transmission Revenues: Allowed Pass Through Items

Special Licence Condition J3 sets out the items that can be passed through into the OFTOs revenue stream in the event of cost change. To reflect our policy proposals the condition includes cost adjustment terms relating to changes in the following costs:

- Ofgem Licence Fees – these are any additional costs that the OFTO may incur as a result of Ofgem changing the licence fee.
- Network Rates - these are any additional costs that the OFTO may incur as a result of change in network rates.
- Crown Estates Lease - these are any additional costs that the OFTO may incur as a result of the Crown Estates changing the lease fee.
- Decommissioning - these are any additional costs that the OFTO may incur as a result of change to Government decommissioning requirements.
- Income Adjusting Event – this is a general term that allows for an adjustment to be made to the revenue stream in exceptional cases where the Authority has deemed a change in the income stream is required (i.e. adjustments made to deal with the occurrence of an “unknown unknown”).

Special Condition J4: Restriction of Transmission Revenues: Annual Revenue Adjustment

Special Licence Condition J4 sets out the terms for the predefined adjustment mechanisms. These include:

The Performance Incentive – this allows for adjustments to the revenue stream that are required as a result of operational performance.

The Incremental Capacity Incentive – this allows for additional payments to be made to a licensee who has delivered additional capacity as a result of an amendment to a generator's Connection Agreement.

Special Condition J10: Excluded Services

Special Condition J10 sets out the services that may be undertaken by the licensee in addition to its revenue controlled activities (e.g. certain subcontracting).

Changes to licence conditions

Requirements on licensees may evolve over time, and there are processes in place to modify licence conditions where a need arises. Modifications can be made to the licence conditions of the electricity transmission licence under certain sections of the Electricity Act 1989. Modifications made under Section 11A modify the standard conditions of the licence and therefore, once implemented, apply to all licences of that type. Modifications to the special conditions of a particular individual licence can be made under a different mechanism, which is under Section 11 of the Electricity Act 1989.

Modifications under Section 11A can be made if a certain proportion of all licence holders agree to such a change, whereas modifications under Section 11 require the individual consent of the licence holder who is having its licence modified.

The Authority is required to carry out a 28 day statutory consultation prior to making any modifications under either Sections 11A or 11.

Enforcement provisions

All licensees must ensure that they have systems and procedures in place that will enable them to comply with the conditions of their licence. Failure to comply with a condition of the licence may result in formal enforcement action by Ofgem. The outcome of any enforcement action may result in the Authority imposing a financial penalty on the licensee, which may be up to 10% of the licensee's applicable turnover.

System charging

Transmission charging

Assets that facilitate connection to the NETS are (normally) owned, built and maintained by the relevant Transmission Licensee, the cost of which is recovered through various charges which the NETSO charges to all parties that connect to and use the NETS (e.g. generators and suppliers). These charges comprise connection charges, Transmission Network Use of System ("TNUoS") and Balancing Services Use of System Charges ("BSUoS") charges.

The methodology in respect of connection charges payable by a party wishing to connect to the NETS can be found at:

<http://www.nationalgrid.com/NR/ronlyres/4811E6E0-3AA5-468F-9ADC-740FE9424180/24473/GBCCMI4R0FINAL.pdf>.

The methodology in respect of use of system charges payable (both TNUoS and BSUoS) can be found at:

<http://www.nationalgrid.com/NR/ronlyres/BC5D87D0-4682-4C56-9375-7B932A1BD726/24713/UoSCMI4R0FINALBSUoS.pdf>.

Distribution charging

Each Distribution Licensee charges for connection to and use of its distribution system. They are required by their Electricity Distribution Licences to prepare a methodology in respect of the connection charges payable by a party seeking connection to its distribution system and a methodology in respect of the use of system charges payable by a party that uses its distribution system.

These methodologies are available on the relevant Distribution Licensee's website.

Decommissioning

Sections 105 to 114 of the Energy Act 2004 introduce a decommissioning scheme for offshore wind and marine energy installations. Under the terms of the Act, the Secretary of State may require a person who is responsible for one of these installations to submit (and eventually carry out) a decommissioning programme or the installation.

Installations consented after June 2006

For installations consented after June 2006, the Secretary of State will require the offshore transmission operator to submit a decommissioning programme for approval within three months of acquiring the transmission equipment and cables.

The proposal should be prepared in line with the Guidance on the Decommissioning of Offshore Renewable Energy Installations under the Energy Act 2004:

<http://www.berr.gov.uk/energy/sources/renewables/policy/offshore/decommissioning/page43348.html>

issued by DECC. When the Secretary of State is satisfied that a suitable decommissioning programme is in place with the owner of the transmission equipment he will relieve the former owner of his obligations to decommission that equipment by amending the decommissioning programme in respect of the generating station. There will therefore be a period during which the person under decommissioning obligations in respect of the generating station is likely to also be under obligations in respect of the transmission equipment at a time when he does not own the equipment in question.

Installations consented before June 2006

Offshore renewable energy installations which were consented before June 2006 should have decommissioning obligations to the Crown Estate as part of their lease of land upon which the installation and associated transmission equipment and cabling rests. It is anticipated that when title to the offshore transmission equipment passes to the new owner they will acquire the relevant sections of the leasehold of the relevant land and with that leasehold will come the obligations to decommission. It is therefore anticipated that existing decommissioning plans in place for developments will remain valid with new owners. Replacement plans should not need to be submitted if lease terms are revised or re-issued by Crown Estates.