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Our Ref: 20/10
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Date: 10 February 2010

Dear Colleague,

Offshore Electricity Transmission – Consultation on draft Tender Regulations 2010

Purpose of this letter

The purpose of this letter is to:

- provide an overview of the legal framework for changing the regulations¹;
- seek feedback on the changes we are proposing to make to the regulations in order to implement the policy positions as set out in the consultation document we published in December on the enduring regime (the December document)²;
- seek feedback for the changes we are proposing to make to the regulations for the second round of transitional tenders (and other administrative changes); and
- set out next steps in order to bring the new regulations into effect later this year.

Background

Ofgem and the Department of Energy and Climate Change (DECC) have developed and introduced a new regulatory regime for offshore electricity transmission. A key part of the new regime is that offshore electricity transmission licences will be granted following a competitive tender process run by Ofgem.

The new offshore transmission regulatory regime reached an important milestone in June 2009 with the Government commencing a number of relevant sections of the Energy Act 2004 (known as "Go Active"). The commencement of section 92 of the Energy Act 2004 inserted section 6C to the Electricity Act 1989 (the "Act") which enables the Authority to make regulations to run a competitive process to grant offshore electricity transmission licences. Shortly after Go Active, we launched the first transitional³ tender round to identify Offshore Transmission Owners ("OFTOs") for approximately £1.1 billion worth of transmission connections to offshore wind farms.

The December document set out detailed proposals for the enduring regime including how these proposals could be incorporated into the regulations. We also set out that in updating the regulations we would also take the opportunity to make changes to the regulations to improve the process for the second transitional tender round, as well as making general administrative improvements.

¹ The Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations 2009

² Offshore Electricity Transmission: Consultation on the Enduring Regime, 157/09, 18 December 2009

³ Under the transitional arrangements, developers of offshore generation projects are able to construct the transmission assets before they are transferred to the OFTO identified through the competitive tender process. The developer will be remunerated for transferring these transmission assets by the OFTO at a value determined by the Authority.

Legal framework for the regulations

Section 6C of the Act enables the Authority to make regulations which are appropriate for facilitating the making of a determination on a competitive basis of the person to whom an offshore electricity transmission licence is to be granted. The making of these regulations is not subject to a specific parliamentary procedure but the approval of the Secretary of State is required before they can come into effect. The current regulations came into effect on 2 June 2009 following a consultation process in which stakeholder feedback was sought on two occasions (July 2008 and March 2009).

The process for changing the regulations is the same as when they were first made, and so will follow the process outlined above. For reasons of administrative ease, we intend to revoke the existing regulations (referred to in the remainder of this letter as the "2009 Regulations") and replace them with new regulations (the "2010 Regulations").

Proposed changes to the 2009 Regulations

Enduring Regime

The December document seeks feedback on a number of 'minded to' positions on issues including:

- Qualifying Project and Tender Entry conditions;
- Remuneration of pre-construction costs;
- Tender specification;
- Tender timescales; and
- Bid evaluation

We intend to change the 2009 Regulations in respect of the enduring regime to reflect the policy proposals set out in the December document. It is important to note that the draft 2010 Regulations demonstrate how the proposals in the December document could be reflected into the regulations. However, it will only be possible to conclude the drafting of the 2010 Regulations once the final policy positions are announced in May. As such, stakeholders should be aware that the 2010 Regulations will be amended by us alongside the finalisation of policy positions. To this end, we have added the changes for the enduring regime in square brackets.

Transitional Regime and Other Administrative Changes

We are also making a limited number of changes to the 2009 Regulations for the second round of tenders in the transitional regime. These changes seek to improve the regulations reflecting lessons learned from the running the first round of tenders. Similarly, we are also making a limited number of administrative changes that will affect both transitional and enduring tenders.

Overview of Key Changes

Set out below is a high level reference to the key changes we intend to make to the 2009 Regulations:

- the insertion of a mechanism to assess the costs of pre-construction works for projects tendered under the enduring regime;
- the insertion of a mechanism to transfer any pre-construction works undertaken by developers of projects tendered under the enduring regime;
- changes to both the transitional and enduring developer entry conditions set out in Schedule 2 to the draft 2010 Regulations;

- a requirement on developers to provide updated cost information to the Authority until such time as the assets are available for use for the transmission of electricity. This applies to projects tendered under the transitional regime and enduring regime; and
- an ability for the Authority to use this updated cost information to update cost estimates or assessments for pre-construction works.

We are also proposing for the 2010 Regulations to provide a mechanism for us to determine whether to adopt a Qualification to Tender stage for the enduring regime at the time when we commence the tender process. Whilst we set out in the December document that we would move to a single stage qualification for the enduring regime, on balance we consider that it would be appropriate to confirm the stages at the outset of the competition based, amongst other things, on projects coming forward. We would welcome any specific feedback on this issue by **24 February**, before the closure of the consultation on the draft 2010 Regulations.

Annex 1 to this letter contains a detailed table of all the proposed changes, including the rationale for the changes. Annex 2 contains the draft 2010 Regulations and Annex 3 contains the draft 2010 Regulations in track change (against the 2009 Regulations).

Next steps

Responses to the December document are due shortly and we will use these to further develop policy positions for the enduring regime. We expect to announce our decisions on the enduring regime in May this year. During this period, we will amend the draft 2010 Regulations, as appropriate, to reflect any changes in policy positions. We will publish the final 2010 Regulations after the announcements are made on final policy positions. In order to ensure that stakeholders are informed of progress in the development of the 2010 Regulations, we will endeavour to set out how any issues raised in response to the December document impact on the development of the 2010 Regulations via our website.

Responding to this consultation

We are seeking feedback from stakeholders on all aspect of the draft 2010 Regulations, in particular on the translation of the policy positions set out in the December document into the regulations.

As set out above, we are seeking feedback on the specific issue of the qualification stages by the **24 February**. Responses on the draft 2010 Regulations should be received no later than **10 March 2010**. All responses should be sent to:

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Unless marked as confidential, responses will be placed in the Ofgem library and published on the Ofgem website. Any questions on the document should be directed to Diana Kennedy at diana.kennedy@ofgem.gov.uk in the first instance.

Yours faithfully,



Robert Hull
Managing Director, Commercial, Ofgem E-Serve