Date: 24 February 2012

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Dear Giedre

Offshore Electricity Transmission: Consultation on tender exercises under the enduring regime (Ref:178/11)

Thank you for providing the opportunity comment on this latest offshore transmission consultation and inviting ABB to speak at the recent stakeholder workshop.

About ABB

ABB (www.abb.com) is the global market leader in electricity transmission technology, having pioneered key developments in both HVAC and HVDC over many years. The ABB Group of companies operates in around 100 countries and employs about 130,000 people worldwide. In the UK and Ireland, ABB employs around 2,600 people and continues to invest in jobs and facilities to help build a Greener Britain. We are committed to developing and deploying the latest technologies to support the growth in sustainable energy production and consumption.

ABB is an active player in the European market for offshore transmission infrastructure. We have an excellent track record in the development of offshore connections and interconnectors in Scandinavia and North West Europe. ABB is providing the HVAC electrical systems and equipment to connect near shore wind farm developments, including Phases 2 and 3 of the Thornton Bank project in Belgium. We are also a recognised world leader in HVDC technologies, which is being used to build a number of high capacity links to connect remote offshore wind farms. ABB is currently using HVDC Light technology to connect a number of remote offshore wind farms off the German coast. This includes the project to build the world's largest single offshore wind connection, the 900MW Dolwin 2 project, which will be the first project to use ABB's pioneering Gravity Based Self-Installing offshore platform.

ABB is building on years of project experience to expand our offering to the UK offshore renewable market. We have committed to an ongoing programme of investments that will expand and upgrade existing European manufacturing facilities to support the growing demands for electrical infrastructure across the entire European market. ABB also continues to make significant investments in UK jobs and skills development to support the delivery of marine renewable projects in the UK.

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Consultation response

Offshore wind generation is an important element of UK government policy. The growth of the offshore renewable sector has the potential to secure local jobs, establish key skills and support economic growth while meeting the UK's binding renewable energy and carbon reduction targets. The offshore transmission regulatory framework is a key enabler for the development of offshore renewable generation. Nevertheless, it is important that policy initiatives are not viewed in isolation and that a holistic approach is adopted to ensure that UK consumers gain the best value overall.

Throughout the development of the offshore transmission enduring regime, ABB has highlighted the need for a simple and robust regulatory framework to ensure that the UK's offshore renewable energy potential is realised. The global transmission market is experiencing a sustained period of rapid growth. The UK is currently competing in global markets for capital, transmission equipment and skills as several countries embark on ambitious investment programmes to deliver electrical networks for the 21st century.

ABB considers that the OFTO regime must provide a framework that is sufficiently attractive throughout the entire value chain in order to deliver a sustainable offshore renewable sector in the UK. Substantial investment in manufacturing capability and skills will be needed to develop a supply chain that has sufficient capability to meet global demand. ABB is supportive of Ofgem's desire to ensure fair and effective competition across the offshore transmission market. Nevertheless, we are concerned that the proposals for supply chain interaction under the proposed OFTO build model will create unnecessary additional interfaces, increasing costs, deterring necessary supply chain investment and increasing consumer risk.

ABB is actively engaging with key industry players to ensure that we are able to meet the requirements of their projects in a socially and environmentally responsible manner. We consider that the OFTO framework must be sufficiently flexible and pragmatic to enable the offshore industry to deal with new challenges as larger and more complex projects are developed. Such an approach will enable key lessons to be learned, which will ultimately help drive down costs in the longer term.

ABB fully supports the aim of delivering best value for current and future electricity consumers. The OFTO framework must therefore achieve an appropriate allocation of risks and rewards if this objective is to be achieved. We consider that the drive to deliver a low risk offshore transmission sector, while successfully attracting transmission investment, has led to a disproportionate increase in risk to offshore generators and is imposing unnecessary costs to society as a whole. The further emphasis placed on delivering low cost, lean electrical systems under the OFTO build model is likely to increase generator's exposure to transmission failure risk with increased costs to consumers. We urge Ofgem to reconsider the overall balance of risks and rewards to ensure that best value can be delivered to current and future consumers.

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ABB considers that coordinated transmission development will be critical to the long term future of the offshore renewable sector in the UK and Europe. It is important that measures are introduced that incentivise and enable coordination of infrastructure. We therefore look forward to contributing to the debate on offshore transmission coordination when the consultation is published later this month.

For ease of reference, we have included detailed responses to some of the specific questions on the OFTO build model in a separate appendix.

ABB remains strongly in support of the development of the UK offshore wind sector and the wider growth of the green economy. We are keen to work with Ofgem to assist in further developing these proposals to ensure that we have a robust enduring OFTO regime.

We trust that these comments are helpful in informing your thinking. Please do not hesitate to contact me should you require any clarification to our comments.

Yours sincerely

[By email]

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Appendix 1: Responses to Specific Questions

Q2.1 Do you have any views on the approach outlined in paragraph 2.8, namely to focus on a single OFTO build option and not to develop the early OFTO build option further at this stage?

The offshore transmission sector is still in its infancy. The first OFTO tender process is still ongoing with only four projects granted licences and limited operational experience. We therefore agree with the proposal to focus on a single OFTO build model and not to develop the more complex early OFTO model at this stage.

Q3.8 Do you agree that ensuring procurement is undertaken by the OFTO through the tender process would be the most economic and efficient approach?

The benefits of the competitive licensing framework for offshore transmission systems are clearly understood, particularly for generator build projects. ABB recognises that the OFTO regime has been extremely successful in attracting new entrants and new sources of low cost finance during the first transitional tender round.

We understand the desire to ensure effective competition across the supply chain. ABB considers that much of the benefit from design and innovation will be solutions developed and delivered by the supply chain, regardless of whether the client is a Generator or an OFTO. We believe that the creation of the optimum climate for open and robust competition at the tier 1 supply chain level is vital to achieving best value for the consumer.

Procurement by a single party is a well understood approach, and has been proven to facilitate effective competition within the supply chain leading to innovation and ultimately efficient investment on behalf of the consumer. However, we have significant concerns over the parallel procurement processes which would be required by multiple prospective OFTO's within the OFTO build model as currently proposed. We believe that such an approach will result in unnecessary additional costs and risks, and ultimately will not deliver value to the consumer.

The cost to support a procurement process for large transmission schemes is significant. In a market where both resource and manufacturing capacity are constrained, supply chain organisations must optimise the use of resources to maximise their commercial opportunities. The proposals are likely to add complexity and risk to the supply chain, which is likely to lead to a dilution of competition with supply chain companies choosing to participate in fewer projects, providing more conservative proposals, greater conditionality and less innovation in the initial submission bids.

Q3.9 What are your views on whether there are supply chain constraints associated with the manufacture and delivery of some key offshore transmission assets? If there are constraints, do these vary significantly in relation to project design?

The global transmission market is experiencing a period of sustained growth, both for AC and DC equipment, which is placing upwards pressure on lead times for equipment manufacturing and

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installation facilities. In addition, there is a limited amount of skilled power engineering and project management resource available in the market today. Tennet has recently publicised the challenges in delivering high capacity, offshore transmission connections in Germany. Supply chain constraints have been identified as one of the main factors in their request to extend the statutory period for delivering German projects from 36 months to 50 months. With several North Sea countries embarking on major offshore wind programmes such challenges may become more common across Europe, including in the UK.

Q3.10 What are your views on the examples of alternative approaches for supply chain engagement under OFTO build outlined in this chapter? Q3.11 Are there any other approaches we should consider under OFTO build to enable the supply chain to be engaged in time to ensure project delivery timescales are met, whilst maximising opportunities for competition through the tender process?

Early supply chain engagement is critical to ensure that the project can be properly scoped and to maximise the likelihood that consents would be secured. This will also be the case where supply chain capability is limited, such as VSC HVDC systems or 220kV AC systems. It is also true that proactive suppliers will seek to engage with the generator community at an early stage to obtain a better understanding of their project requirements and timescales.

Any procurement process which provides clarity and timely placement of firm commitments against capacity is welcome. Even once firm commitments have been made, it is not uncommon for supply contracts to be modified or novated. We consider that the current contracting framework is sufficiently flexible to changing client needs, while mitigating the financial exposure of the supplier of responding to change. For example, novation of contracts is broadly acceptable where the new counter party satisfies our contracting requirements (such as demonstrating an appropriate financial standing) to ensure that we can understand our risk exposure and manage it appropriately.

We are concerned by the proposed alternative approaches set out in the consultation, as they would appear to place a significant burden on the supply chain without firm commitment from the procuring parties. Further extending OFTO build engagement processes to include early discussions on indicative terms with generators adds further burden to the supply chain with additional commercial uncertainty. We consider that the arrangements are likely to lead to greater commercial risk and risk management cost, and therefore the poorer the value to the consumer.

In our opinion, non-binding indications of terms or commitments to capacity are not a sustainable option for the supply chain and it is an approach unlikely to be supported by responsible suppliers. Moreover, we are extremely concerned that such arrangements would also create the opportunity for speculation and false promises from less responsible players. We believe that this could undermine confidence in the OFTO process, damage the reputation of the supply chain as a whole, and incentivise suppliers to support other markets that can provide firm commitment and certainty.

Q3.12 Should there be any restrictions on interactions between parties, either before or during a tender exercise in order to ensure fair and effective competition and best value for consumers?

It is very important that each part of the competitive process is fair and transparent. It is important that Stakeholders do not have any potential conflict of interest when participating in the process, for example when an offshore wind project development partner is acting as a supply chain party to an OFTO bidder. Without appropriate safeguards, there is a major risk that the competitive process will be distorted. We note that Ofgem put in place legal requirements on National Grid to prevent them from gaining an unfair commercial advantage from their role as National Electricity Transmission System Operator. We consider that similar measures are required to ensure that Ofgem can run an effective licensing competition.

Where a technologically advanced solution is proposed, it is unclear how much of the detail can be presented by an OFTO within their bid submissions in order to allow a full and robust evaluation against more traditional approaches. It is also unclear how Ofgem would/could demonstrate the knowledge and capability to fully and properly assess the solution being put forward. It is very important that the OFTO evaluation process is suitably robust and that the technical evaluation criteria are clear and well understood. We consider that the current process is not sufficiently transparent to enable the supply chain to fully participate in the process.

Q3.23 What are your views on the proposals for involving generators in evaluation of bids? In particular, what key technical aspects of bids would be most important for generators to evaluate?

As set out in our response to question 3.12, we believe that appropriate safeguards are required to ensure that there is a fair and transparent competitive process. As a technology developer, it is important that intellectual property rights are protected. The risk that a competitor may get access to intellectual property by participating as an offshore wind development partner is a major concern for ABB and one which may become a barrier to ABB participating in the delivery of certain projects.

Q3.25 Are there areas on which you think allowing variant bids under OFTO build would add value to the process and to consumers?

As noted above, the availability of supply chain resources is likely to be an issue for rapid offshore wind development that is being proposed. We consider that steps should be taken to minimise the burden of the OFTO process on the supply chain. We are concerned that variant bids will only serve to tie up valuable resources with limited additional benefits.

Q3.26 What are your views on generators recovering efficiently incurred pre-construction costs at the point at which the transmission construction works are completed?

We consider that pre-construction costs should be funded at the point of licence grant (which is the point of transfer for rights and liabilities to the OFTO). To impose a requirement that the wind farm

developers only receive payment several years after transferring those rights and liabilities is irrational.

Q5.3 What are your views on whether running a separate tender exercise for each phase within a site/zone would best meet the objectives of the enduring regulatory regime?

It is important that the regulatory regime minimises the number of commercial and operational interfaces. We do not consider that it is in the best interests of consumers for a regime that might lead to multiple OFTOs when there is certainty over future phases of development. Looking at many of the Round 3 development areas, it is likely that there will be an ongoing programme of construction. This means that the initial development in phase 2 might already be under construction as phase 1 fully completes. Under those circumstances a single tender that covers both development phases might be more appropriate than multiple tenders, particularly if those phases form part of a coordinated meshed system.