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Initially by email
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Dear Giedre

Balfour Beatty Capital acting as agent for the Balfour Beatty Group Limited ("Group"), is pleased to respond to your consultation dated 16 December 2011 "Offshore Electricity Transmission - Consultation on tender exercises under the enduring regime" (the "Consultation"). We have been appointed preferred bidder on the Thanet project, are part of the consortium appointed as preferred bidder on the Greater Gabbard project, and are currently bidding for the Transitional Round 2A projects.

Following our review of the Consultation, our main points are:

- Retaining the early OFTO option – We believe there is merit in retaining the early OFTO build option. The early OFTO option may be the best model to use in developing a coordinated network especially with managing issues such as anticipatory investments. We do not believe that it is in the best interest of the industry to discount the early OFTO model at this point in time until the offshore transmission coordination project is complete.

- Triggering an OFTO tender under the OFTO build option and appointment of a preferred bidder – We believe that one of the key considerations for the developer in selecting the build option for transmission assets will be the perceived timely delivery of the transmission assets by the generator's connection date under an OFTO build versus a Generator build. The trigger date for an OFTO build and the appointment of a preferred bidder should therefore be such that there is adequate time for an OFTO to procure and construct the transmission assets by the connection date. For certain projects this may mean appointing the preferred bidder prior to the planning consent being granted.

- Advantages of appointment of preferred bidder before planning consent – The preferred bidder can begin finalising the supply chain contracts which would allow for a quicker financial close once planning consent is achieved. This means that equipment orders can be placed earlier and therefore optimise the delivery timetable under OFTO build.

- Managing planning consent risk - We recognise that the planning consent is a key risk but this has to be balanced with the timely delivery of the transmission assets under the OFTO build option. There are various mechanisms that can be incorporated to manage this risk. For example, the Authority could specify a set contingency that bidders are required to include in their bids for managing planning consent risk. To the extent this contingency is not needed, the TRS is reduced.

- Managing supply chain constraints – Our preference is for the OFTO to undertake all the supply chain procurement. There should be no restrictions for interaction between parties either before or during a tender exercise, especially with equipment manufactures. However, based on our experience to date, equipment suppliers are not willing to enter detailed negotiations with or undergo detailed design for several parties only one of which will be appointed the preferred bidder. If the manufacturers are allowed to form exclusive agreements with bidders, this will seriously affect the ability of other bidders to compete. Equally, it is very expensive for OEMs to develop variant designs for different bidders, so the risk is that bidders' solutions are based on the same major elements.

  Therefore it is our view that to ensure effective competition and best value for consumers the bidders at ITT stage should be limited to two. We believe this number will ensure the supply chain engages with bidders at the ITT stage and allow for innovative variants to be developed.

The attached appendix contains the responses to the questions raised in the Consultation. We would be pleased to discuss in further detail with you.

Yours faithfully

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APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME

CHAPTER 2 – THE ENDURING REGIME

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?

Yes. Balfour Beatty does not believe that it is in the best interest of the industry to discount the early OFTO model especially given the ongoing discussions on the coordinated network development, which are yet to be finalised and for which, an early OFTO model may be best suited.

We have however structured the responses in this response assuming a late OFTO build.

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APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

CHAPTER 3 – OFTO BUILD OPTIONS

Q3.1 What are your views on the proposed arrangements for triggering a tender exercise?

We believe that one of the key considerations for the developer in selecting the build option for transmission assets will be the perceived timely delivery of the transmission assets by the generator's connection date. The trigger date for an OFTO build and the appointment of a preferred bidder should therefore be such that there is adequate time for an OFTO to procure and construct the transmission assets by the connection date. For certain projects this may mean appointing the preferred bidder prior to the planning consent being granted.

Q3.2 What are your views on whether our proposal on generator security will ensure the appropriate level of commitment from a generator?

The security should be sized such that the generator remains committed to the process.

Q3.3 Do you agree with our proposed approach to the tender specification for an OFTO build tender exercise?

The proposed approach appears to fix the electrical and mechanical design and as such does not appear to allow for variant bids and/or innovative approaches. There should be room in the tender specifications to allow for the OFTO to deliver a variant design.

Q3.4 Are the proposed arrangements for pre-construction works the most appropriate for investors and generators?

Yes.

Q3.5 What other information, if any, in addition to that referred to within the tender specification and pre-construction works sections, would be needed within the data room for the project?

We would suggest that the generator include technical assessments of the status of major equipment design and development as part of the tender specification pack to ensure that the technology proposed is feasible.

APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

Q3.6 What do you think would be the best approach to ensuring bidders have access to and confidence in a seabed survey undertaken by the generator?

Q3.7 With reference to the approach to seabed surveys outlined within paragraph 3.22, what might be the best approach to developing an independent generic survey specification that would be acceptable to both generators and potential bidders?

We agree that a mechanism for potential bidders plus the developer to agree on a survey specification devised by a third party would be a reasonable approach. This mechanism should not introduce any delay into the process. The survey should be undertaken by an independent party. It should be comprehensive, detailed and also be adapted for the unique locational issues. It should also have been recently undertaken.

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?

Yes.

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?

Based on our experience to date, equipment suppliers are not willing to enter detailed negotiations or undergo detailed design for a party who may not be the preferred bidder. We believe that this can be mitigated by limiting the amount of ITT bidders to two.

Q3.10 What are your views on the examples of alternative approaches for supply chain engagement under OFTO build outlined in this chapter?

Our preference is for the OFTO to undertake all the supply chain procurement.

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?

Yes. Considering appointing the preferred bidder earlier; potentially before the planning consent date as this will ensure the supply chain is engaged in time to ensure project delivery timescales.

APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

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?

Certain key elements, such as DC converters and EHV DC cables are produced by very few manufacturers worldwide. If the manufacturers are allowed to form exclusive agreements with bidders, this will seriously affect the ability of other bidders to compete. Equally, it is very expensive for OEMs to develop variant designs for different bidders, so the risk is that bidders' solutions are based on the same major elements. As noted in Question 3.9, equipment suppliers are not willing to enter detailed negotiations or undergo detailed design for a party who may not be the preferred bidder. Therefore it is our view that to ensure effective competition and best value for consumers the bidders at ITT stage should be limited to two.

Q3.13 Do you agree that the current 20 year revenue stream provides the best value to consumers under the enduring regime (OFTO build or Generator build)? If not, what alternatives should we consider?

The 20 year revenue period is tested and bankable. For OFTO build option, as per the Generator build, the 20 year revenue period should commence from the date of commissioning of the transmission assets.

Q3.14 What are your views on our proposed treatment of risk relating to: - delay to licence grant?- weather delay?

Agree that they should be an element of risk sharing. Indexation mechanism should be also be considered for risks outside the OFTO's control such as FX risks, steel prices, commodities, insurance at start of operations etc

Q3.15 Are there other areas of risk which would be more efficiently managed (for consumers) through a risk sharing mechanism rather than factored into bidders' TRS bids? If so, can you suggest how these risks might be shared?

We would suggest the decommissioning costs of the OFTO assets should be considered a pass through cost as there is potential for the asset life to be extended (as the asset life is greater than the 20 year revenue period) or for a second OFTO put in place at the end of the 20 year revenue period.

APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

Q3.16 Is the current approach to recovering bid costs appropriate for OFTO build? If not, what alternative approach to recovering bid costs would you recommend?

ITT bidders under the OFTO build are likely to incur higher bid costs. An incentive for bidders would either be to limit the bidders at ITT and/or allow ITT bidders receive a reimbursement of a proportion of their related ITT costs. However including several bidders at the ITT stage does not address supply chain issues.

Q3.17 Are there any aspects of the current transitional arrangements or within the proposals for OFTO build, including revenue term, bid requirements and risk profile, which may prevent access to certain sources of finance in the enduring regime?

The projects under the enduring regime are significantly larger than the transitional regime as such it is likely that entities with strong balance sheets would be required during the construction period. The Authority should consider including within the enduring regulatory regime mechanisms or structures that would be attractive to external funders and also do not differentiate between the OFTO build and Generator build. For example, under the Generator build, the funding would be required for a shorter period as the transmission assets would have to be sold to an OFTO post construction. For OFTO build, longer term funding would be required which introduces different risks to the OFTO build which the developer, under the Generator build is not exposed to.

The transitional arrangements essentially provide developers with a guarantee that they are able to recover the higher of 75 per cent of the ex-ante cost estimate or 100 per cent of the efficiently incurred ex-post cost assessment from the OFTO. The Authority should consider including a variant of this mechanism into the OFTO build option.

Q3.18 Do you have any comments on the issues associated with incorporating a refinancing gain share mechanism and how such a mechanism could be structured?

The risk profile of a refinancing mechanism must be clearly addressed especially the down side risk and this will be dependent on the commercial and regulatory structures in place under the OFTO build or the Generator build option.

APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

Q3.19 Do you have any preferences from amongst the options outlined for how the PQ stage should operate?

Our preference is option 1 with a two year validity period. To address Ofgem's concern of limiting competition across the bidder community, a PQQ window could be run once a year for new entrants.

Q3.20 Are there any other ways that a PQ stage might operate in order to meet the objectives set out at the start of the 'Tender stages and timings' section?

No.

Q3.21 Do you have any preferences from the options outlined for how the ITT stage might operate?

Q3.22 Are there any other ways that the ITT stage might operate to ensure its efficiency and effectiveness?

We believe that the three options presented increases developers' concerns that the transmission assets will not be delivered to meet their timetable and as such a Generator build would be preferred. We would therefore suggest the preferred bidder be appointed before planning consents date to minimise delay risk.

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?

It is very important that the generator can test the proposed reliability, availability and flexibility of the bidders' proposed designs. We welcome the generator's input in informing the evaluation criteria and commenting on the technical sections of the bid including: physical interface to generator's equipment, design philosophy, grid compatibility, control and protection systems, switching philosophy, flexibility and redundancy.

APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

Q3.24 What are your views on the proposals for involving NETSO in evaluation of bids? In particular, what key technical aspects of bids are most important for NETSO to evaluate?

We welcome NETSO's input in informing the evaluation criteria and commenting on the technical sections of the bid including: design philosophy, grid compatibility, grid code compliance, control and protection systems, reliability, flexibility and redundancy. NETSO also has a role to play in verification of system fault levels, power flows and network stability.

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

It is important that the OFTOs under the OFTO build option should be allowed to put forward variant bids especially in the technical specification. Variant bids allow for innovation and potential for a better risk/reward trade off.

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?

Efficiently incurred pre-construction costs should be recoverable.

Q3.27 Do you have any early views on the appropriateness of design incentives for transmission asset lifecycle design, eg transmission availability, quality of installation and transmission losses?

Agree that transmission availability should be included in the design incentives. The OFTO incentives should cover minimising the system losses over the lifetime of the asset. Quality of installation incentive is not required as the OFTO is already incentivised through the tender process itself (which provides competitive costs) and the availability incentive mechanism (which ensures high availability)

Q3.28 What are your views on whether the current approach to indexation, and in particular the proportion of the TRS subject to indexation, provides the best value to consumers? How might any alternative approaches be managed?

The indexation mechanism as it stands is well understood by the market and does not need to be adjusted.

APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

Q3.29 Do you agree that additional delivery incentives for OFTOs are not necessary?

Yes.

Q3.30 What are your views on what approach to decommissioning of assets would provide best ongoing value to consumers?

See response to Question 3.15.

APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

CHAPTER 4 - A GENERATOR BUILD OPTION

Q4.1	What are your views on whether there are benefits under Generator build to the generator undertaking the seabed survey against a comprehensive generic survey specification agreed by industry?

See response to Questions 3.6 and 3.7.

Q4.2	Do you agree with the approach that Ofgem continues to run tender rounds for groups of projects, not necessarily limited to one per year, or would you recommend an alternative approach?

Yes.

Q4.3	Do you think there are further efficiencies we could make to the tender process and the transaction procedures for Generator build which would increase their efficiency and provide greater certainty to bidders and funders?

Further efficiencies in the tender process and transaction procedures could be achieved by:

i. Removing the QTT process and having an enhanced PQQ which is valid for a time period;

ii. Limiting the number of ITT bidders;

iii. More developer bidder interaction;

iv. Keeping preferred bidders on hold until the construction of transmission assets is complete.

Q4.4	Are there any changes to the information supplied in the data room which would improve the efficiency of the process for Generator build?

The information supplied in the data room should be as detailed and comprehensive as possible and should be based on industry standards.

APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

Q4.5 What are your views on the benefits of involving generators in evaluation of bids as outlined in this section?

Unlike the OFTO build option, it is our view that generator involvement is not required in the evaluation of bids under the Generator build option as the OFTO is not undertaking the construction of the transmission assets.

Q4.6 Do you have any suggestions on amendments which would improve the efficiency of the process for finalisation of transfer documentation and which would maximise value to consumers?

Suggestions and amendments include:

i. During the ITT stage, producing key issues lists instead of full mark-ups thereby reducing advisers fees;

ii. Each draft transfer agreement deals with the "splitting" of construction contracts in a slightly different way – an agreed template wording would reduce the amount of time required to consider the approach taken on a project by project basis;

iii. Standardisation of warranty packages across projects;

iv. Completion of confirmatory due diligence should only commence once the transmission assets have been constructed or close to completion.

Q4.7 What do you consider might be the implications of a share sale approach as opposed to a transfer of assets as has been seen to date?

A stand-alone special purpose vehicle ("SPV") set up to specifically enter into separate leases and contracts for the construction of the transmission assets could simplify the process of transferring the benefit of the relevant construction contracts to the successful OFTO.

If the share sale approach was adopted then the mechanics of licence grant would need to be considered – would the licence be awarded to the SPV (which owns the transmission assets) notwithstanding that it will be owned by the developer prior to financial close?

In addition the tax implications of share/asset sales would need to be reviewed and considered in the context of stamp duty, availability of capital allowances, etc. Given the commercial issues are common to the share sale and asset transfer approaches, it is likely to be the tax analysis and residual liabilities which would inform the preferred approach.

APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

Q4.8	Do you agree that the current split between costs priced into the TRS and those allowed as pass throughs provides best value for consumers?

See response to Question 3.15.

Q4.9	Are there any aspects of the current arrangements for transitional tender exercises or within the changes we have proposed above, including revenue term, bid requirements and risk profile, which may prevent access to certain sources of finance under Generator build?

See response to Question 3.17.

Q4.10	Do you have any comments on the issues associated with incorporating a refinancing gain share mechanism for Generator build and how such a mechanism could be structured?

See response to Question 3.18.

APPENDIX: RESPONSE TO THE CONSULTATION ON THE ENDURING REGIME (CONT.)

CHAPTER 5 – PHASED OR STAGED CONSTRUCTION OF TRANSMISSION ASSETS

Q5.1	Are you satisfied with the practical relevance of our definition of the terms 'phase' and 'stage'?

Yes.

Q5.2	What are your views on the measures we propose to determine whether a stage or phase within a site/zone qualifies for a single tender exercise?

The measures proposed by the Authority appear sensible.

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?

We agreed that separate tender exercises should be run for each phase especially if the duration of each phase is long. However, each phase would have to be designed on a stand alone basis. Interfaces between the various phases should be minimised. It is important to recognise that the final overall network must incorporate features which deliver maximum reliability and operational robustness. This will inevitably mean some interconnection between phases and each tender exercise will need to be designed to take account of this.