

Offshore Electricity Transmission: Cost Recovery Methodology for the Second Transitional Tender Round

Version 1.2

Tender Document

Publication date: 20 March 2013

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Overview:

The regulatory regime for offshore electricity transmission enables the Authority to grant Offshore Transmission Licences on the basis of a competitive tender process. Ofgem is responsible for managing this process.

This document sets out the Cost Recovery Methodology for the calculation and recovery of Ofgem's costs in relation to Tender Exercises in the second transitional Tender Round which will lead to the granting of Offshore Transmission Licences.

Context

Electricity generated from offshore renewable sources is expected to make an important contribution towards the UK achieving its renewable energy targets by 2020. Fit for purpose offshore electricity transmission infrastructure is required to transfer the electricity generated offshore to the onshore network and ultimately to consumers. It is important that this infrastructure is developed in a timely, secure and cost-effective manner. It should also provide best value to present and future electricity consumers, while reflecting the requirements of generators and ensuring that, as far as possible, offshore infrastructure develops in a co-ordinated manner.

The Department of Energy and Climate Change (DECC¹) and Ofgem² have developed a regulatory regime for offshore electricity transmission. It was consulted on extensively and refined over four years, culminating in a final statement published in June 2009³.

A key part of the regime is that Offshore Transmission Licences can be granted following a competitive tender process run by Ofgem, with the Successful Bidder becoming the Offshore Transmission Owner (OFTO). The result will be that the generating assets (offshore wind farms) will be owned and operated by the generator, whilst the Offshore Transmission System, which connects the offshore wind farms to the onshore transmission system, will be owned and operated by the OFTO Licensee.

The Offshore Transmission Licences will place certain rights and responsibilities on OFTOs, including the right to a regulated revenue stream for a period of 20 years in return for the provision of Transmission Services.

Associated documents

These Tender Rules apply to the second transitional Tender Round (Tranche B) and should be read in conjunction with the following documents:

- The Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations 2010⁴
- The Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations 2013⁵
- Tender Rules for the Second Transitional Tender Round (v1 – 17/11/10)⁶
- Tender Rules for the Second Transitional Tender Round (Tranche B) (v1 – 20/03/13)⁷

¹ And its predecessors, the Department for Trade and Industry and the Department of Business, Enterprise and Regulatory Reform

² The Gas and Electricity Markets Authority is the regulator of gas and electricity markets in Great Britain. Ofgem is the Office of Gas and Electricity Markets, which supports the Authority in performing its statutory duties and functions. It is the Authority which is responsible for exercising the relevant statutory powers.

³ www.ofgem.gov.uk/Networks/offtrans/pdc/cdr/cons2009/Documents1/Main.pdf

⁴ <http://www.legislation.gov.uk/uksi/2010/1903/contents/made>

⁵ <http://www.legislation.gov.uk/uksi/2013/175/contents/made>

⁶ <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=7&refer=Networks/offtrans/rttt>

⁷ <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=7&refer=Networks/offtrans/rttt>

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Executive Summary

The Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations (“Tender Regulations”) set out the legal framework and powers for Ofgem to run a competitive tender process for transitional projects.

In accordance with the Tender Regulations, Ofgem publishes a cost recovery methodology for each tender round which provides an overview of the costs we would recover during a tender process, as well as detail on the payments we would require from participants to recover these costs.

This document sets out the Cost Recovery Methodology for the calculation and recovery of Ofgem’s costs in relation to Tender Exercises in the second transitional Tender Round which will lead to the granting of Offshore Transmission Licences. This includes the details of the costs which Ofgem incurs in administering Tender Exercises, the methodology for recovering these costs and details of how and when payments must be made by Developers and Bidders.

Cost Recovery Methodology

Chapter Summary

This chapter provides an overview of the Cost Recovery Methodology including details of what Ofgem's costs are.

Introduction

- 1.1. Section 6C of the Electricity Act 1989 (the "Act") enables the Authority to make regulations to run competitive tender processes for the grant of Offshore Transmission Licences. The Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations 2010 (the "2010 Regulations ") came into effect on 29 July 2010 and revoked The Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations 2009 in their entirety. The Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations 2013 (the "2013 Regulations ") came into effect on 22 February 2013.

Application of Tender Regulations 2010 and Tender Regulations 2013

- 1.2. The 2010 Regulations apply to current tender exercises that met the qualifying project requirements set out in the 2010 Regulations by 31 March 2012.
- 1.3. The 2013 Regulations came into force on 22 February 2013. The 2013 Regulations set out the tender process framework for granting an offshore transmission licence, including how Ofgem will run future tenders under both the generator build and OFTO build options. Current tender exercises being run under the 2010 Regulations will remain subject to the 2010 Regulations, except for the Qualifying Project in Tranche B of the second transitional Tender Round, which became subject to the 2013 Regulations from 22 February 2013.
- 1.4. In accordance with regulation 2 of the 2013 Regulations⁸, where the Authority has not given notice in relation to the payment for the ITT stage of a tender exercise by 22 February 2013, the process for grant of an OFTO Licence for that qualifying project will be subject to the 2013 Regulations.
- 1.5. For the purpose of this Cost Recovery Methodology document, the term 'Tender Regulations' shall refer to either the 2010 Regulations or the 2013

⁸ Regulation 2(1) of the 2013 Regulations identifies the exact point in the process as the notice by the Authority to the bidders of the amount payable in relation to the invitation to tender stage for that project.

Regulations, as applicable. Where in the text a particular reference in the 2010 Regulations is specified the correct reference under the 2013 Regulations has also been identified.

- 1.6. The Tender Regulations provide the legal framework for the process which Ofgem will run for the grant of Offshore Transmission Licences. The rules of this process are set out in the Tender Rules. For Qualifying Projects in the second transitional Tender Round which continue to be governed by the 2010 Regulations, the applicable Tender Rules remains version 1 issued in November 2010⁹. For the Qualifying Project in the of the second transitional Tender Round (Tranche B) which will be governed by the 2013 Regulations from 22 February 2013 onwards, the applicable Tender Rules will be the Tender Rules for the Second Transitional Tender Round (Tranche B)¹⁰ published alongside this Cost Recovery Methodology.
- 1.7. By accepting and participating in a Tender Exercise, each Bidder and Developer agrees to be bound by, and to comply with, the rules and requirements set out in the Tender Regulations and in this Cost Recovery Methodology.

Cost recovery principles

- 1.8. Section 6D of the Act¹¹ contains key provisions with regard to the offshore transmission regime, specifically in terms of Ofgem's powers to fully recover its direct and administrative support costs associated with running a Tender Round. Specifically, the Act enables the Authority to:
 - secure a financial commitment from Developers in respect of any potential liability the Developer may have. This commitment is referred to as the "security";
 - secure payments from Developers and Bidders to cover Ofgem's costs of running a Tender Exercise. These payments are referred to as "payments"; and
 - in respect of offshore projects in the Transitional Regime, request a payment from the Developer to cover costs incurred in relation to assessing the Indicative Transfer Value, and from the Successful Bidder to cover costs associated with determining the Final Transfer Value.

⁹ Offshore Electricity Transmission: Tender Rules for the Second Transitional Tender Round, November 2010:

<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=7&refer=Networks/offtrans/rttt>

¹⁰ Offshore Electricity Transmission: Tender Rules for the Second Transitional Tender Round (Tranche B), March 2013:

<http://www.ofgem.gov.uk/Networks/offtrans/rttt/Pages/rttt.aspx>

¹¹ Inserted by section 44 of the Energy Act 2008.

Electricity Act 1989: http://www.opsi.gov.uk/acts/acts1989/Ukpga_19890029_en_1.

Energy Act 2008: <http://www.legislation.gov.uk/ukpga/2008/32/contents>.

- 1.9. The principles set out in this Cost Recovery Methodology apply in respect of the second transitional Tender Round. In accordance with regulation 9(4) of the 2010 Regulations, Ofgem published the first version of this Cost Recovery Methodology prior to the commencement of the Tender Round.
- 1.10. The principles set out in this Cost Recovery Methodology will be kept under review in light of any material changes in circumstances, and may be subject to change, for example if there is a material change to the forecast of the anticipated direct costs incurred in relation to a Tender Exercise.

Ofgem's Costs

Tender set-up costs

- 1.11. The Act does not state explicitly when costs may start to be recovered. However, under normal Government practice¹², set-up expenditure may be incurred and hence is recoverable under Section 6D of the Act.
- 1.12. Set-up costs relating to preparation for the Tender Round include (but are not necessarily limited to):
- Tender project staff costs;
 - External expert advice;
 - Legal costs (internal and external);
 - IT Systems; and
 - Ofgem overheads.
- 1.13. It is anticipated that full recovery of initial and ongoing set-up costs relating to establishing the framework for running Tender Rounds in the Transitional Regime will be completed within the first few Tender Rounds.
- 1.14. Set-up costs that arise for Tender Rounds to be held in the enduring regime will be recovered from the initial enduring Tender Rounds to the extent they are not recovered elsewhere.

Ongoing tender costs

¹² HM Treasury: *Managing Public Money*: http://www.hm-treasury.gov.uk/psr_mpm_index.htm

- 1.15. The Act gives Ofgem the ability to seek payments and security from the Developer and payments from the Bidders in a Tender Exercise, in order to recover its full costs in respect of running the Tender Round. Tender costs include the costs which are incurred in relation to a Tender Exercise in respect of a specific Qualifying Project, and an appropriate proportion of costs incurred in relation to the Tender Round as a whole.

Tender Exercise Costs incurred in relation to a Specific Qualifying Project

- 1.16. The direct costs (for example, external expert advice, advertising, etc.) which are incurred in relation to a Tender Exercise for a specific Qualifying Project will be allocated to a specific stage of the Tender Exercise. Staff costs will be apportioned to each stage based on a general time apportionment methodology. Any other relevant costs (for example bank charges) will also be allocated to a specific stage. A contingency amount will be included to provide for additional costs arising from uncertainty and unpredictable events such as tender re-runs and legal challenge to the process. The level of contingency is based upon the optimism bias indicated in the supplement to the Green Book guidance issued by HM Treasury¹³.
- 1.17. Payments made by Bidders and Developers will be based on a forecast of these anticipated costs. The forecast costs will be reviewed at least annually to reduce the risk of significant over/under recovery over time. This may result in a change to this Cost Recovery Methodology, as set out in paragraph 1.10. As described in paragraphs 1.39 to 1.43, an aggregation exercise at the end of the Tender Round will ensure that costs for Bidders and Developers will reflect actual tender costs incurred and any excess payments received will be repaid in accordance with the Cost Recovery Methodology.

Costs incurred in relation to the Tender Round as a whole

- 1.18. In respect of the Tender Round as a whole, there will be a recovery of Ofgem's overheads. The overhead calculation is a single percentage on direct costs to recover indirect costs, i.e. general overheads. General overheads cover Ofgem's administrative support functions such as accommodation, HR, IT, Facilities Management, Finance etc.
- 1.19. The fixed overhead rate for each Tender Round will be reviewed at least annually to reduce the risk of significant over/under recovery over time. This may result in a change to this Cost Recovery Methodology, as set out in paragraph 1.10.

Cost estimates and assessments

- 1.20. Under the Tender Regulations Ofgem shall undertake an estimate and assessment of the economic and efficient costs which ought to be, or ought to

¹³ http://www.hm-treasury.gov.uk/data_greenbook_index.htm

have been, incurred in connection with developing and constructing the transmission assets that will be transferred from the Developer to the Successful Bidder in respect of a Qualifying Project. This process will enable the Authority to determine the transfer value for these assets. The Tender Regulations also enable Ofgem to recover its costs of undertaking these exercises¹⁴.

- 1.21. For the estimate of economic and efficient costs (the "Indicative Transfer Value"), the Developer will be liable for costs after Ofgem has undertaken the estimation¹⁵. This amount will be recoverable by the Developer as part of the final cost assessment.
- 1.22. For the assessment of economic and efficient costs (the "Final Transfer Value"), the Successful Bidder will be liable for costs after the Tender Exercise has been held¹⁶. These costs will be recoverable via an adjustment to the terms of the project specific version of the OFTO's Licence. An estimate of the costs payable by the Successful Bidder associated with determining the Final Transfer Value will be provided to the Successful Bidder during the Preferred Bidder stage.
- 1.23. Costs include (but are not necessarily limited to):
 - Tender project staff costs;
 - Consultancy costs;
 - Legal costs (internal and external); and
 - Ofgem overheads.

VAT

- 1.24. Ofgem will not be required to charge VAT on the amounts to be recovered. Running the Tender Round is a statutory service and therefore outside the scope of VAT.

Payments and Security

- 1.25. The Act enables Ofgem to require Bidders and Developers to pay for the costs that Ofgem incurs in relation to the Tender Round and, in the case of Developers, provide security in respect of any potential liability the Developer may have.

¹⁴ In accordance with regulations 4 and 5 of the Tender Regulations

¹⁵ In accordance with regulation 5(1) of the Tender Regulations

¹⁶ In accordance with regulation 5(2) of the Tender Regulations

1.26. The payment and security details for the second transitional Tender Round are set out in Schedule 1.

Cost Consequences of Withdrawal, Cancellation and Disqualification

1.27. The Tender Regulations set out the cost consequences of:

- Withdrawal by a Bidder from a Tender Exercise;
- Cancellation of a Qualifying Project from a Tender Round; and
- Disqualification of a Developer or Bidder from a Tender Exercise.

1.28. For further details on each of these events, please refer to regulations 19 to 22 and Schedules 7 and 8 of the 2010 Regulations or regulations 22 to 26 and Schedules 7, 8 and 9 of the 2013 Regulations (as applicable).

1.29. The cost consequences of each event are described in more detail below. In summary, they ensure that Ofgem will be able to recover its costs where an event has occurred through no fault of its own.

Withdrawal

1.30. If a Bidder withdraws from a Tender Exercise, any payment (including any interest which it may have accrued but excluding any non-refundable payments) which that Bidder has paid to Ofgem in relation to the Tender Exercise will only be repaid to the Bidder where the aggregate of the payments received from the Bidder exceeds the costs incurred.

1.31. If a Developer withdraws from a Tender Exercise for any reason, Ofgem will treat this as an event of cancellation.

Cancellation

1.32. The Tender Regulations set out events where Ofgem may determine to cancel a Tender Exercise. They also allow Ofgem to re-run a Tender Exercise where appropriate. The 2013 Regulations specify the circumstances which may lead to a re-run of a Tender Exercise from those which could only lead to cancellation. If a re-run is unsuccessful in appointing a Preferred Bidder, Reserve Bidder or Successful Bidder, Ofgem may consequently determine to cancel that Tender Exercise.

1.33. If a Tender Exercise is cancelled as a result of an event related to a Bidder set out in

(i) paragraphs 1(b),(c),(d),(e),(f),(g),(h),(i),(j),to (k) or (s) of Schedule 7 of the 2010 Regulations;

or

(ii) paragraphs 1 (c),(d),(e),(f),(g),(h), (i), (j),(k),(l) or to (m) of Schedule 7 or paragraph 1 (a) of Schedule 8 of the 2013 Regulations (as applicable) then:

- the Developer will be repaid (in whole or in part dependent on the costs incurred up until the stage at which the Tender Exercise is cancelled) the payment made to Ofgem under regulation 7(1)(a) of the 2010 Regulations or regulation 9(a) of the 2013 Regulations (including any interest which that payment may have accrued) and Ofgem shall release the security provided by the Developer under regulation 7(1)(b) of the 2010 Regulations or regulation 9(b) of the 2013 Regulations (as applicable); and
- the Bidder(s) will not be entitled to be repaid (in whole or in part) any payment which it has made to Ofgem in relation to that Tender Exercise (including any interest which those payments may have accrued).

1.34. Where a Developer fails to make a payment or provide security, as required in accordance with the Tender Regulations and as calculated in accordance with this Cost Recovery Methodology (unless that failure has been remedied within the period specified by Ofgem in accordance with the Tender Regulations), Ofgem may cancel that Qualifying Project from that Tender Exercise.

1.35. If a Tender Exercise is cancelled as a result of an event related to a Developer, set out in

(i) paragraphs 1(a),(l),(m),(n),(o),(p),(q) or (r) of Schedule 7 of the 2010 Regulations;

or

(ii) paragraphs 1(a) or (b) of Schedule 7 or paragraphs 1 (b)to (i) of Schedule 8 of the 2013 Regulations (as applicable), then:

- the Developer will not be entitled to be repaid (in whole or in part) any payment made to Ofgem (including any interest which those amounts may have accrued) and Ofgem may decide whether to call upon the security provided by the Developer; and
- the relevant Bidder(s) will be repaid (in whole or in part dependent on the costs incurred up until the stage at which the Tender Exercise is

cancelled) any amounts (including any interest those amounts may have accrued) paid to Ofgem.

Disqualification

- 1.36. Where a Bidder fails to make any payment, as required in accordance with the Tender Regulations and as calculated in accordance with this Cost Recovery Methodology, Ofgem may disqualify that Bidder from that Tender Exercise (unless that failure has been remedied within a period not exceeding ten days as specified by Ofgem in accordance with the Tender Regulations).
- 1.37. If a Bidder is disqualified, it will not be entitled to be repaid (in whole or in part) any amount which it has paid to Ofgem in relation to the Tender Exercise (including any interest which those amounts may have accrued).
- 1.38. If a Developer is disqualified, it will not be entitled to be repaid (in whole or in part) any payment made to Ofgem (including any interest which those amounts may have accrued). Ofgem may decide whether to call upon the security provided by the Developer, dependent on the stage of the Tender Exercise that the Developer is disqualified and the costs incurred up until that point.

Aggregation

- 1.39. In accordance with regulation 25(4) and (5) of the 2010 Regulations and regulation 29(5) and (6) of the 2013 Regulations, Ofgem is required to undertake an aggregation exercise as soon as reasonably practicable after a Tender Round is finished, in order to identify whether the Authority's total tender costs have been exceeded. In this case, Ofgem must repay any excess to the relevant party.
- 1.40. Ofgem will undertake an aggregation of:
 - Payments made by the Developer and Bidders which have not been repaid in the event of withdrawal, cancellation or disqualification; and
 - Any security forfeited by the Developer in the event of cancellation (including withdrawal of a Qualifying Project from a Tender Round) or disqualification.
- 1.41. It is not anticipated that there will be any refund of the payments in respect of the cost estimates and assessments described in paragraphs [1.20 to 1.23] of this document, as those payments will be invoiced after the actual costs are known.

- 1.42. Where the aggregation exercise reveals that the total amount of payments made and security provided have exceeded Ofgem's total tender costs, Ofgem shall:
- Repay (in whole or in part) the relevant proportion of any excess payment to the relevant Developer or Bidder (including any interest which those amounts may have accrued); and
 - Release (in whole or in part) any excess drawn down security to the Developer (including any interest where the security provided is a cash deposit).
- 1.43. The aggregation exercise will be audited by Ofgem's outsourced internal audit service provider as soon as practicable after each Tender Round.

Interest

- 1.44. The Act confirms¹⁷ that any repayment is to include an amount representing interest accrued on the whole or part of the payment.
- 1.45. Where the security is to be returned to the Developer, any interest accrued in an escrow account will be returned together with the principal sum.
- 1.46. In terms of Ofgem's own bank account, an Office of the Paymaster General (PGO) interest bearing bank account will be opened. Monies will be drawn down from escrow accounts and paid into the PGO account as they fall due. The interest will be taken into account during the aggregation exercise.
- 1.47. The amount of interest accruing from the PGO account will be calculated with reference to the following:
- PGO interest rate(s);
 - Amount(s) held; and
 - Length of time in account.
- 1.48. A typical PGO interest rate calculation could be as follows:
- Rate 0.3% (example base rate 0.5% less 0.2%) @ refundable amount
£1,000,000 held for 12 months = £3,000.

Additional payments

¹⁷ Section 6D (1)(e)(ii) and (iii) of the Electricity Act 1989.

- 1.49. In accordance with the Tender Regulations, additional payments may be payable, to cover direct costs and overheads associated with the relevant event, in the following circumstances:
- Enquiries to the Authority – as described in regulation 27 of the 2010 Regulations and regulation 31 of the 2013 Regulations; and
 - Changes to bidder groups – as described in regulation 28 of the 2010 Regulations and regulation 32 of the 2013 Regulations.

Financial governance

- 1.50. The procedures for administering the Tender Round will be subject to review by Ofgem’s internal audit function, the Authority Committee for Offshore Electricity Transmission and, more generally, by the Audit Committee. The National Audit Office (NAO) is the statutory external auditor of Ofgem and may also wish to review the procedures for administering the Tender Round. As well as providing an opinion on financial statements, the NAO can also examine and report to Parliament on the economy, efficiency and effectiveness of any public spending.

Schedule 1: Payments and Security

Developer's payment and security

S1.1. Each Developer will be required, before a Tender Exercise is commenced for its Qualifying Project, to:

- make a payment to Ofgem of £50,000; and
- provide Ofgem with security in the form of a letter of credit or a cash deposit for an amount calculated in accordance with paragraph 1.9 below.

S1.2. Schedule 2 sets out Ofgem's standard form letter of credit and form of demand Ofgem would use if it needed to call on the security.

S1.3. The security will be returned to the Developer at the end of the Tender Round where there is no reason for Ofgem to forfeit it.

Bidders' payments

S1.4. Each Bidder is responsible for its own costs of developing and submitting its Submission(s) during a Tender Exercise. In addition, each Bidder, Qualifying Bidder, Preferred Bidder and Successful Bidder will be required to make prescribed payments to Ofgem at the Pre-Qualification stage, the Invitation to Tender stage (based on a sliding scale), the Preferred Bidder stage and the Successful Bidder stage (based on a sliding scale and a potential variable component) respectively.

S1.5. The timing (and other details) of each of the above payments is in accordance with the charging schedule detailed in paragraph S1.8 below:

- each Bidder will be required to pay Ofgem when it submits its Pre-Qualification Submission;
- each Qualifying Bidder will be required to pay Ofgem at the start of the Invitation to Tender stage an amount for each Qualifying Project for which it wishes to submit a tender, based on a sliding scale, subject to an overall cap;
- once it has been confirmed as Preferred Bidder for the relevant Qualifying Project, a Preferred Bidder will be required to make a payment to Ofgem; and

- the Successful Bidder will be required to make a payment to Ofgem, based on a sliding scale and a potential variable component, on the grant of an Offshore Transmission Licence.

Payment Details

S1.6. Deposits made by Developers in respect of cash security are required to be paid into the following dedicated Ofgem escrow account:

Bank: Lloyds TSB

Account Name: Gas and Electricity Markets Authority Offshore Tender

Account Number: 00928001

Sort Code: 30 00 03

As the Tender Exercise proceeds, Ofgem will draw down from this escrow account to cover the costs of running the Tender Round.

S1.7. Payments in respect of Fees should be advised on the Invoice but otherwise are required to be paid into the following Ofgem account:

Account Name: GBS re Ofgem Offshore Tender

Account Number: 12316129

Sort Code: 08-33-00

Swift Code: CITIGB22

IBAN: GB12CITI08330012316129

Charging Schedule

S1.8. The table below sets out the fees and security required during the Tender Exercise.

Process Stage	Participant		
	Developer	Bidder or Qualifying Bidder	Successful Bidder
Developer security	Equal to the sum of the forecast Successful Bidder payment and the forecast for the costs of assessing the Final Transfer Value for the relevant project.	N/A	N/A
Developer payment	£50,000	N/A	N/A
Pre-Qualification stage payment	N/A	£5,000 ²	N/A
Qualification to Tender stage payment	N/A	N/A	N/A
Invitation to Tender stage payment	N/A	Sliding scale, up to £50,000 ³	N/A
Preferred Bidder payment	N/A	£250,000	N/A
Successful Bidder payment	N/A	N/A	Sliding scale ⁴ , from £650,000
Payment for costs of assessing the Indicative Transfer Value and determining the Final Transfer Value ⁵	Circa £100,000	N/A	Circa £100,000
<p>Table notes</p> <p>1 This is a flat charge and is not dependent on the number of projects the Bidder signals its interest in.</p> <p>2 This payment is based on a sliding scale up to a maximum cap of £50,000 per Qualifying Bidder irrespective of the number of projects tendered for.</p> <p>3 This payment is based on a sliding scale to reflect the size and complexity of the asset transfer and a potential variable component as indicated below.</p> <p>4 This is an indication only of the costs associated with the estimate of the Indicative Transfer Value and costs associated with determining the Final Transfer Value for the Developer and Successful Bidder respectively. The payments will be determined on a project specific basis and invoiced after the actual costs are known.</p>			

Sliding Scale Developer security

S1.9. The amount of Developer security required is the sum of the requisite forecast Successful Bidder payment for the project together with the forecast costs associated with determining the Final Transfer Value.

S1.10. Ofgem will directly inform Developers of the required level of security.

Sliding Scale Invitation to Tender Payment

S1.11. The amount each Qualifying Bidder must pay at the Invitation to Tender stage is based on a two-part sliding scale comprised of:

- a fixed fee of £10,000 for each Qualifying Project for which the Qualifying Bidder wishes to submit a tender; and
- a variable fee of £5,000 for each increment of £50m of Ofgem's estimated transfer value of the Qualifying Project.

S1.12. The payment to be made by a Qualifying Bidder at the Invitation to Tender stage will not be more than £50,000 in total, irrespective of how many Qualifying Projects a Qualifying Bidder submits a tender for.

S1.13. For example, to tender for a project with a value of between £100m and £150m, the bidder would pay a charge of £10,000 plus 3 x £5,000 (i.e. £25,000). If the bidder bids for three projects, each with a value of between £100m and £150m, the total charge would be £50,000 (i.e. 3 x £10,000 plus 9 x £5,000, but subject to the total cap of £50,000).

Sliding Scale Successful Bidder Payment

Successful Bidder Payment

S1.14. The amount each Successful Bidder must pay at licence grant will consist of two components:

- a base fee, calculated on a sliding scale to reflect the size and complexity of the asset transfer, which will have an impact on the costs Ofgem bears; and
- a variable fee to reflect additional costs that Ofgem may bear in relation to a particular Qualifying Project in certain circumstances prescribed below. If no such circumstances exist this fee is zero.

Base Fee (Sliding Scale Component)

S1.15. The payment will be from £650,000 for projects with a transfer value of up to £100m, and increase in tiers of £650,000 for projects with transfer values above £100m in £100m increments, i.e.

- £650,000 for projects with a transfer value up to £100 million;
- £1,300,000 for projects with a transfer value between £100 and £200 million;
- £1,950,000 for projects with a transfer value between £200 and £300 million;

- £2,600,000 for projects with a transfer value between £300 and £400 million;
- £3,250,000 for projects with a transfer value between £400 and £500 million; etc.

Variable Fee

S1.16. If one or more of the following events occur in relation to a particular Qualifying Project, Ofgem may need to increase the amount charged as the Successful Bidder payment for that project to reflect the incremental tender costs incurred by Ofgem as a result of the event:

- the tender exercise for the Qualifying Project is re-run from the beginning or a particular stage;
- a best and final offer stage is held in respect of the Qualifying Project;
- any unforeseen circumstances arise in relation to the tender exercise, or a particular stage of the tender exercise, for the Qualifying Project which result in increased tender costs. For example this may arise as a result of a delay to the date for completion of construction of the transmission assets or a delay to the resolution of the Preferred Bidder matters.

S1.17. Ofgem will indicate the estimated level of the payment required from the Successful Bidder at the Preferred Bidder stage, which will include the base fee and any variable fee anticipated at that time. The Successful Bidder payment will be confirmed once the Successful Bidder is appointed prior to the grant of the Offshore Transmission Licence.

Schedule 2: Form of Letter of Credit and Form of Demand

Form of Letter of Credit

To:
Gas and Electricity Markets Authority
9 Millbank
London
SW1P 3GE

(the "**Beneficiary**")

[Date]

Irrevocable Standby Letter of Credit no.[]

At the request of [], [Issuing bank] (the "**Issuing Bank**") issues this irrevocable standby letter of credit ("**Letter of Credit**") in your favour on the following terms and conditions:

Definitions

In this Letter of Credit:

"**Business Day**" means a day (other than a Saturday or a Sunday) on which banks are open for general business in London;

"**Demand**" means a demand for a payment under this Letter of Credit in the form of the schedule to this Letter of Credit;

"**Expiry Date**" means [];

"**Total L/C Amount**" means [];

Issuing Bank's agreement

- 1.1. The Beneficiary may request a drawing or drawings under this Letter of Credit by giving to the Issuing Bank a duly completed Demand. A Demand may not be given after the Expiry Date. A Demand must be received by the Issuing Bank by [] p.m. (London time) on the Expiry Date.

- 1.2. Subject to the terms of this Letter of Credit, the Issuing Bank unconditionally and irrevocably undertakes to the Beneficiary that, within [ten] Business Days of receipt by it of a Demand, it must pay to the Beneficiary the amount demanded in that Demand.
- 1.3. The Issuing Bank will not be obliged to make a payment under this Letter of Credit if as a result the aggregate of all payments made by it under this Letter of Credit would exceed the Total L/C Amount.

Expiry

- 1.4. The Issuing Bank will be released from its obligations under this Letter of Credit on the date (if any) notified by the Beneficiary to the Issuing Bank as the date upon which the obligations of the Issuing Bank under this Letter of Credit are released.
- 1.5. Unless previously released under paragraph 1.4 above, on [] p.m. (London time) on the Expiry Date the obligations of the Issuing Bank under this Letter of Credit will cease with no further liability on the part of the Issuing Bank except for any Demand validly presented under the Letter of Credit that remains unpaid.
- 1.6. When the Issuing Bank is no longer under any further obligations under this Letter of Credit, the Beneficiary must return the original of this Letter of Credit to the Issuing Bank.

Payments

- 1.7. All payments under this Letter of Credit shall be made in pounds sterling and for value on the due date to the account of the Beneficiary specified in the Demand.

Delivery of Demand

- 1.8. Each Demand shall be in writing, and, unless otherwise stated, may be made by letter or fax and must be received in legible form by the Issuing Bank at its address and by the particular department or officer (if any) as shown in the Form of Demand.

Assignment

- 1.9. The Beneficiary's rights under this Letter of Credit may not be assigned or transferred.

ISP 98

- 1.10. 1.10 Except to the extent it is inconsistent with the express terms of this Letter of Credit, this Letter of Credit is subject to the International Standby Practices (ISP 98), International Chamber of Commerce Publication No. 590.

Governing Law

- 1.11. This Letter of Credit and any non-contractual obligations arising out of or in connection with it are governed by English law.

Jurisdiction

- 1.12. The courts of England have exclusive jurisdiction to settle any dispute arising out of or in connection with this Letter of Credit (including a dispute relating to any non-contractual obligation arising out of or in connection with this Letter of Credit).

Yours faithfully,

[Issuing Bank]

By:

Form of Demand

To: [ISSUING BANK]
[Date]

Dear Sirs

Standby Letter of Credit reference [] issued in favour of the Gas and Electricity Markets Authority (the "Letter of Credit")

We refer to the Letter of Credit. Terms defined in the Letter of Credit have the same meaning when used in this Demand.

We certify that the Authority has determined that the sum of £[] shall be forfeited from this security [pursuant to The Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations 2010/any successor regulations]. We therefore demand payment of the sum of £[].

Payment should be made to the following account:

Name: []

Account Number: []

Bank: []

The date of this Demand is not later than the Expiry Date.

Yours faithfully

(Authorised Signatory)

(Authorised Signatory)

For
Gas and Electricity Markets Authority

Appendix 1 - Glossary

"Act" means the Electricity Act 1989 as amended from time to time.

"Authority"¹⁸ means the Gas and Electricity Markets Authority.

"Bidder" means any person or consortium of persons that submits a Pre-Qualification Submission, a Qualifying Bidder, a Preferred Bidder or a Successful Bidder (as applicable).

"Developer" means the person falling within sub-sections 6D(2)(a) and (4) of the Electricity Act that has developed or is developing an offshore generating station who requests that Ofgem commences a Tender Exercise in respect of a proposed project.

"Final Transfer Value" means Ofgem's assessment of the economic and efficient costs which ought to be incurred in connection with the development and construction of the relevant Transmission Assets.

"Indicative Transfer Value" means Ofgem's estimate of the economic and efficient costs which ought to be incurred in connection with the development and construction of the relevant Transmission Assets.

"Invitation to Tender stage" means the period starting from the notification by Ofgem of the amount payable by Qualifying Bidders in relation to the Invitation to Tender stage of a particular Tender Exercise, and including the distribution of Invitation to Tender documentation, tender preparation, submission and evaluation, and ending when either a Preferred Bidder is selected and notified, or a Best and Final Offer stage is commenced.

"Offshore Transmission Licence" means a licence granted pursuant to section 6(1)(b) of the Act in relation to the transmission of electricity in offshore waters, where offshore waters means:

- (a) waters in or adjacent to Great Britain which are between the mean low water mark and the seaward limits of the territorial sea;
- (b) waters within an area designated under section 1(7) of the Continental Shelf Act 1964; and
- (c) waters within an area designated under section 84(4) of the Energy Act 2004.

"OFTO" or "Offshore Transmission Licensee" means the holder of an Offshore Transmission Licence;

"Preferred Bidder" means, in relation to a Qualifying Project, the Qualifying Bidder determined by Ofgem, in its sole discretion and following its evaluation of the Bids received, as the Qualifying Bidder to which it intends (subject to the satisfaction of the conditions specified by Ofgem) to grant the Offshore Transmission Licence.

¹⁸ The Gas and Electricity Markets Authority is the regulator of gas and electricity markets in Great Britain. Ofgem is the Office of Gas and Electricity Markets, which supports the Authority in performing its statutory duties and functions. Whilst the terms "Ofgem" and "the Authority" are used interchangeably in this Cost Recovery Methodology, it is the Authority which is responsible for exercising the relevant statutory powers.

"Preferred Bidder stage" means the period starting at the date of Ofgem's notice of its determination of a Preferred Bidder and ending at the date of Ofgem's notice to the Preferred Bidder has become the Successful Bidder.

"Pre-Qualification stage" means the period starting from the publication of the Pre-Qualification documentation, including the preparation, submission and evaluation of Pre-Qualification Submissions and ending once Ofgem has published the longlist of Qualifying Bidders who have prequalified for the Qualification to Tender stage.

"Pre-Qualification Submission" means a Bidder's response to the Pre-Qualification documentation.

"Qualification to Tender stage" means the period starting from Ofgem publishing the confidentiality agreement in relation to the Qualification to Tender Stage, including the publication by Ofgem of the longlist of Qualifying Bidders who have prequalified for the Qualification to Tender stage, the preparation, submission and evaluation of Qualifying Bidder's responses to the Qualification to Tender documentation and ending once Ofgem has notified the Qualifying Bidders of its selection of Qualifying Bidders to be invited to participate in the Invitation to Tender stage.

"Qualifying Bidder" means a bidder or consortium of bidders invited to submit a Qualification to Tender Submission or an Invitation to Tender Submission.

"Qualifying Project" means an offshore generating project in respect of which Ofgem determines that the Developer has satisfied the Qualifying Project requirements set out in paragraph 2 of Schedule 1 of the Tender Regulations, or which Ofgem determines at its discretion (exercised in accordance with the Tender Regulations) that the Developer will satisfy the relevant Qualifying Project requirements within a period specified by Ofgem.

"Reserve Bidder" means a Qualifying Bidder determined as a Reserve Bidder in accordance with regulation or 16(4) or 17(5) of the 2010 Regulations, or regulation 18(3) or 19(5) of the 2013 Regulations.

"Submission" means a Pre-Qualification Submission, a Qualification to Tender Submission, a Tender and/or a BAFO Submission (as applicable).

"Successful Bidder" means a Preferred Bidder to which Ofgem has determined to grant an Offshore Transmission Licence.

"Successful Bidder stage" means the period starting at the date of Ofgem's notice to a Preferred Bidder that it has become the Successful Bidder and ending at the date when Ofgem publishes a notice confirming its determination to grant an Offshore Transmission Licence to the Successful Bidder for a particular Qualifying Project.

"Tender" means each tender submitted to Ofgem in response to the Invitation to Tender documentation.

"Tender Exercise" means, for the purposes of this document, the competitive process run by Ofgem in order to identify a Successful Bidder to be granted an Offshore Transmission Licence in relation to a particular Qualifying Project.

"Tender Regulations" means the 2010 Regulations or 2013 Regulations, as applicable in accordance with regulation 2 of the 2013 Regulations.

"2010 Regulations" means the Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations 2010.

"2013 Regulations" means the Electricity (Competitive Tenders for Offshore Transmission Licences) Regulations 2013.

"Tender Round" means, for the purposes of this document, the second round of Tender Exercises run by Ofgem, in order to identify Successful Bidders to be granted Offshore Transmission Licences in relation to Qualifying Projects.

"Tender Rules" means the rules (as amended from time to time) for the second competitive Tender Round under the Transitional Regime, first published by Ofgem on 17 November 2011 and subsequently on 20 March 2013 (as applicable).

"Transitional Regime" means a Tender Round for the grant of Offshore Transmission Licences where the transmission assets have been or are being constructed by Developers, and where the Developer meets certain Qualifying Project requirements to the satisfaction of the Authority