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By email to: offshorelicensing@ofgem.gov.uk

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Dear James,

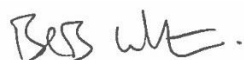
Response to Ofgem's "OFTO Tender Process – Consultation for Future Tender Rounds"

We welcome the opportunity to respond to Ofgem's consultation on future tender rounds for the OFTO tender process. The consultation paper is right to set out the context for the review and highlight the development of the OFTO sector, which has matured. Indeed, the entire offshore sector has matured since the OFTO regime was introduced in 2009, with more players, larger projects and greater ambition. Prices for offshore generation have fallen dramatically, driven in part by the transition to Contracts for Difference from the Renewables Obligation and the Final Investment Decision Enabling for Renewables (FIDER), from over £155/MWh to just £57.50/MWh in the latest auctions. The CfD regime has successfully incentivised developers to find the most efficient way to build offshore wind farms, and is a very different regime from, in particular, the Renewables Obligation.

This is one of the reasons that developers have not opted to pursue the option to outsource the design and build of the offshore transmission to third parties – maintaining control and cost of the development of the offshore transmission is a crucial part of keeping costs down, and ultimately beneficial to consumers. With this competitive pressure and focus on cost reduction, developers are doing all they can to cut costs, and it is no longer absolutely clear that the regime is the best way to deliver value for the consumers of today and tomorrow. With more experience in the sector and changing economics, we support the request for a wider review of the OFTO regime in the Offshore Wind Sector Deal prospectus.

Please see our specific responses to the consultation questions attached.

Yours sincerely



Barnaby Wharton
Head of Policy, RenewableUK

Annex

Question 1: Have we identified (in Chapter 1) the right drivers for possible change to the OFTO tender process? Are there other drivers for change we should consider?

It is important that there is competition in the market to bring forward the best bids. The market is at risk of becoming consolidated, with only a handful of significant players. Given the capital requirements and complexity of projects, this should not be a surprise. We would therefore welcome changes that enable more companies to bid in. However, competition in the market should not be pursued for its own ends. Efforts in this regard should enable companies that have the expertise necessary to manage the transmission asset to bring forward high quality bids (which can then be enforced at PB stage). We would not support changes to the regime that could enable low quality, inexperienced, or thinly capitalised bidders winning. The bidding process must be robust and ensure that cost balances, not trumps, quality of asset management.

The drivers for change identified in the consultation document are correct in being among the most significant for the OFTO regime and wider offshore wind industry. In coming years, we will see larger wind farms further offshore. These developments may require different and innovative approaches to operation and maintenance. It is essential that the tendering process brings in OFTOs that have both the capability to manage complex infrastructure, and also requires them to do so properly.

It is also worth noting that developments in the market, such as floating wind, may see more small wind farms developed in the near term, though these will likely be further offshore, in more difficult conditions, and may require a different set of skills to operate and maintain.

Question 2: Are the objectives of our review appropriate? Are there any other objectives that we should consider?

We agree that the objectives of the review are appropriate for the tendering process. However, many of our members are concerned that the focus of the review is skewed heavily towards the needs of the bidder. While we agree that the bidding process should be as efficient as possible, this should not be at the expense of scrutiny of bidders' capability to effectively and efficiently manage large and complex infrastructure assets. Generators rely on secure offshore transmission assets to export their power, and as offshore wind increases its share of the energy mix, consumers will also increasingly rely on this as a source of low carbon and low-cost power.

In addition, keeping transmission costs down for consumers is extremely important, but we urge Ofgem to have regard to value as well as price. Having robust OFTOs is as important as cost for overall value for money and may not always be the absolute cheapest option, and establishing which bidder will be the most robust is not necessarily easy. The review should uphold robustness as an equal priority to price. Ofgem's assessment in Table 3 in the consultation is that a more complete focus on price only rather than price and robustness at ITT being a positive for consumers by keeping costs as low as possible. We disagree that this offers the best outcome for the consumer.

While this review is welcome, as the Offshore Wind Sector Deal has suggested, we believe that a wider review of the OFTO regime and the lessons learned after nearly ten years of operation would be appropriate. This should look at the balance of risk and cost between the OFTO and generator, and how costs to consumers can be minimised over the lifetime of the assets.

Question 3-5: With respect to the existing tender process arrangements; the moderate change package; and, the significant change package:

Our members do not support either the moderate change or the significant change packages as they are described in the consultation. We support some aspects of the proposals where they can offer a more level playing field during the OFTO transaction, but do not support changes which reduce the robustness of Ofgem’s assessment of bidders’ technical and financial suitability to own and manage the transmission assets responsibly over the whole licence period.

Any changes to the bidding process should be focussed on better assessing the robustness of both finances and technical capability of the bidder party(s). The ability to manage and operate the offshore transmission asset by the prospective OFTO should be considered the entire way through the bid assessment process, and we do not believe that final Preferred Bidder (PB) status should be considered on price alone under any circumstances. While, under the proposed changes, minimum technical requirements are assessed early in the process, by focussing later solely on prices, there is an incentive for a “race to the bottom” focus on the minimum threshold, as Ofgem recognises in the consultation document (paragraph 3.19). Furthermore, OFTOs can be highly leveraged thinly capitalised vehicles. Marginal increases in costs could therefore lead to the risk of insolvency. Therefore, focussing on price alone, not quality of the bid holistically, could potentially lead to higher risks for the generator who relies upon the asset to export and sell its power and for the consumer who relies on the asset for access to low-carbon, cheap power.

Simplifying the bidding process should focus on reducing duplication at EPQ and ITT stages and improving efficiency of the process, but not at the expense of thoroughness. Any company which bids that has the ability to manage the OFTO should be able to progress through the bidding process and relaxing the limit on bidders through the process should support competition and delivery. Having said that, these are crucial parts of the UK’s infrastructure, valued at hundreds of millions of pounds in some cases, and it is reasonable to expect those bidding to purchase them to be able to manage a complex and robust bidding process. It is recognised that the OFTO bidding process is longer than other comparably-sized infrastructure projects. However, we believe that Ofgem should prioritise ensuring that any changes to the bid process are suitably robust for selecting a suitable OFTO whilst also considering ways to make the process shorter if possible. Any changes to shorten the process must complement robustness, not compromise it.

Members report to us that they are concerned about the PB making changes to their offer once they have been appointed. Ofgem should be selecting the best overall offer, and this should be done transparently. Changes to the offer once PB has been selected undermines confidence in the bid process and lack of transparency or certainty in what will finally be provided during the bidding process increases risk for the developer, and ultimately increases the cost of capital and price of energy in the CfD regime. We therefore welcome the Bid Bond proposal, though it would be useful to understand how it would work in greater detail. It should incentivise OFTO bidders to make a “best and final” offer earlier in the process, rather than attempting to change details of bids once they are in the more influential position of the PB at a later stage.

The existing tender process has a weighting of 60:40 for the TRS value and “robustness” respectively. As noted above, we would like Ofgem to consider if this is the best balance to identify the best bidders, and we would not support Ofgem watering down the 60:40 weight. We propose that Ofgem consider evenly weighting the criteria (50:50) to send a clear message to bidders that robustness is as important as price. This is particularly important as projects become more complex and further offshore.

The impact of enabling all bidders to engage in the data room will significantly increase the volume of requests to developers and associated costs, who are trying to reduce costs for the benefit of consumers through the CfD auction process. We are therefore not supportive of any changes to the process which would see the Developer simultaneously negotiating with multiple bidders.

Question 6: Are there other packages of change that we should consider that would better deliver against the objectives?

As highlighted throughout this response, a focus on the ability to manage and maintain the OFTO assets is vital. We fundamentally believe that any changes made must improve the ability of the regime to meet objectives (i) and (ii) as described in paragraph 2.2. Where changes can improve the ability of the regime to meet objectives (iii) and (iv) that is desirable, but these objectives are less important to the overall robustness of the process. Ofgem should consider bringing in technical experts during the bidding process to assess bids technical aspects, where those skills do not exist in house. We would also urge Ofgem to consider, as part of the OFTO license, regular audits of OFTOs' performance against the commitments to manage the assets.

Question 7: With respect to the other tender process changes considered that could apply to either the current tender process or any of the potential packages for change:

- a) Does Vendor Due Diligence (VDD) in practice reduce the total cost of a tender process? Are there any benefits in broad VDD? Are there benefits in a more focussed approach to VDD (for example a Certificate of Title)? Under what conditions and to what extent would bidders base their bid on VDD?
- b) Are there other cost-effective ways in which the bidder data room could be improved to the benefit of all parties? Are there specific ways to further standardise the structure?
- c) What changes, if any, should we consider to our current bond spread methodology? Would an appropriate pain/gain share mechanism for bond-financed bids allow us to fairly assess bond and bank-financed bids on the same committed finance basis?
- d) Do you consider that we could adequately rely on a more confirmatory approach to questions? Are there particular documents or questions we could consider not requiring the bidder to produce, but instead confirm? Are there particular documents/requirements that are better left to the PB stage?

We have no issues with Ofgem allowing bidders to make declarations in the early stages of the bidding process where these declarations do not compromise Ofgem's ability to assess the suitability of the bidder to be able to operate and maintain the transmission asset from an expertise and technical perspective. The declarations would need to be proven at PB stage.

We would support a standard structure for the data room to enable bidders to have a better understanding of how to navigate the information provided and reduce the number of requests for information. There should be adequate consultation on the agreed structure and it should be accompanied by a limit on the number questions bidders are able to submit to the developer.

Question 8: Do you think the approach of Ofgem, developers, and bidders to the tender process will need to change as projects become larger, further from shore and more expensive? What do you see as challenges from this change?

As projects become larger and further from shore, so will the OFTOs and the inherent complexity of the projects and the bids. Ofgem will need to ensure that it is putting the necessary resources into managing more complex bidding processes. It will also mean that there may be fewer bidders with

the skills and financial backing to take these projects on. Ofgem must work to support companies to keep the process competitive, but accept that there may be fewer bidders.

Undoubtedly the technical robustness and suitability of the OFTO becomes increasingly important as projects become larger, further from shore and more expensive. RenewableUK members believe that Ofgem should impress upon the bidders the importance of maintaining the asset to a high standard by adjusting the assessment of the TRS : robustness from 60:40 to 50:50.

Question 9: With respect to end of revenue term arrangements, where there continues to be a need for the OFTO, what factors should be taken into account when making decisions on OFTO revenue at the end of the normal 20-year term? When should we begin to make these decisions?

The door should be left open for life extension. We suggest that Ofgem refrains from being too prescriptive about review processes and timing, and rather refers to best available practice current at the time. We would welcome further consultation/information from Ofgem on this particular topic in the next 12 months. We would particularly be keen to understand the legal implications of re-tendering considering that current OFTOs are being paid decommissioning costs as per their bid in the TRS.

Question 10: Is there demonstrable evidence that we should consider changing the default revenue period away from 20 years for future projects? If so, what would be the most appropriate revenue period?

Default periods away from the 20-year life span should be done on a case by case basis, and project lifespans will increasingly depend on local conditions. Developers and generators would be best placed to determine the life span of different parts of the offshore wind farm and the associated transmission assets.