

# Guidance

## Draft Guidance on the Definition of Uninsurable – Appendix H

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This document is issued under amended standard conditions E12-A1 ('Definitions and Interpretation') and E12-J1 ('Restriction of Transmission Revenue: Definitions') of the Offshore Transmission Owner (**OFTO**) Licence. It provides the definition of Uninsurable for the purposes of amended standard condition E12-J3 ('Restriction of Transmission Revenue: Allowed Pass-through Items').

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## Introduction

### Context and related publications

1.1. The Authority grants OFTO Licences through competitive tenders. OFTO Licences impose obligations, incentives and entitlements on the OFTO. This includes the right to a regulated revenue stream in return for providing transmission services.

1.2. Certain events or circumstances that were not predicted at licence grant may result in increased or decreased costs or expenses. Under the OFTO Licence, the Authority may adjust the OFTO's revenue for certain costs that may arise but are difficult to predict as part of the bidding process. These costs are passed through to consumers. One of those revenue adjustment mechanisms is the income adjusting event (**IAE**) mechanism. Amended Standard Condition (**ASC**) E12-J3 ('Restriction of Transmission Revenue: Allowed Pass-through Items') of the OFTO Licence defines the circumstances which may be considered income adjusting events (**IAEs**) by the Authority.

1.3. In November 2018, following consultation, we published a decision document<sup>1</sup> setting out our intention to modify the IAE revenue adjustment mechanism in ASC E12-J3. In August 2020, we published a statutory consultation ahead of making those modifications to existing and future Licences.

1.4. Where an IAE occurs in the context of asset failures caused by latent defects, in particular in circumstances of 'uninsurability', ASC E12-J3 will provide protection where the relevant IAE definition has been met, including that the OFTO is unable effectively to mitigate the effects of latent defect risk including, through no fault of its own, that risk becoming 'uninsurable'. This guidance document sets out the meaning of 'uninsurable'.

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<sup>1</sup> The decision is available at: [https://www.ofgem.gov.uk/system/files/docs/2018/11/iae\\_response\\_-\\_final\\_0.pdf](https://www.ofgem.gov.uk/system/files/docs/2018/11/iae_response_-_final_0.pdf).

## Your feedback

1.5. We believe that consultation is at the heart of good policy development. We are keen to receive your comments about this guidance. Please send any general feedback comments to [offshorelicensing@ofgem.gov.uk](mailto:offshorelicensing@ofgem.gov.uk).

## 1. Defining Uninsurable

### Uninsurable and related terms

1.1. Amended Standard Conditions E12-A1 and E12-J1 ('Restriction of Transmission Revenue: Definitions') of the Electricity Transmission Licence set out that:

*"Uninsurable"* for the purposes of amended standard condition E12-J3 (Restriction of Transmission Revenue: Allowed Pass-through Items), has the meaning set out in the Guidance on the Definition of Uninsurable, being a document of that name issued by the Authority and updated by the Authority from time to time, following consultation;

1.2. For the purposes of ASC E12-A1 and ASC E12-J3, the meaning of "Uninsurable" is:

*"Uninsurable"* means that the Authority determines either that:

- (a) Insurance is not available to the licensee in respect of all or part of its Transmission Assets in the Worldwide Offshore Transmission Asset Insurance Market with reputable insurers of good standing in respect of a Risk; or
- (b) the Insurance premium payable for insuring that Risk is at such a level that the Risk is deemed as not being insurable in the Worldwide Offshore Transmission Asset Insurance Market with reputable insurers of good standing.

Where:

- (c) a "Risk" means the physical loss or damage requiring replacement or rectification of Transmission Assets, which is caused by a Latent Defect resulting from material workmanship design plan or specification;
- (d) "Insurance" means the indemnity which would normally be covered by an Operational All Risk insurance policy with a LEG 3/06 exclusion, or equivalent, which includes indemnity

*for the full cost of replacement or rectification of the Offshore Transmission Assets (but not improvement) rendered necessary by damage which is the consequence of a Latent Defect;*

*(e) a "Latent Defect" means a flaw in Offshore Transmission Assets, which:*

- i. is an actual defect in material workmanship design plan or specification, not the damage resulting from the defect; and*
- ii. existed but which would not have been apparent to an efficient licensee in the position of the licensee at the time the Offshore Transmission Assets were transferred to it;*

*(f) "LEG 3/06" means the London Engineering Group Unique Market Reference for the Model "Improvement" Defects Wording;*

*(g) "Worldwide Offshore Transmission Asset Insurance Market" means all insurers who, after an exhaustive search, would reasonably be understood by an efficient licensee, in the position of the licensee, to be participating in the business of insuring offshore transmission assets (to be determined by the Authority in its absolute discretion); and*

*(h) "Offshore Transmission Asset/s" means the transmission system to which the licensee's Offshore Transmission Owner Licence relates as set out in Annex B to amended standard condition E12-B1 (Transmission System Area) in the licensee's Offshore Transmission Owner Licence.*

## 2. Modifying the guidance

### Future Consultation

2.1. The OFTO regime continues to grow and evolve. With this in mind, it may be necessary into the future to update our definition of Uninsurable as included in this guidance. We confirm that prior to any substantive changes being made to this guidance, we will undertake a further consultation in accordance with our consultation policy published on the Ofgem website.<sup>2</sup>

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<sup>2</sup> Available at: <https://www.ofgem.gov.uk/consultations/our-consultation-policy>.