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Andrew Mcintosh
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Via email

22nd June 2018

This letter has been redacted for publication. The contents that have been omitted to protect the interests of National Grid are denoted by [*].

Dear Stuart,

Viking Link – Timing of the Final Project Assessment in the cap and floor regime

Viking Link is a 760 km HVDC electricity interconnector project to connect Bicker Fen in England and Revsing in the southern part of Jutland in Denmark. The interconnector is being developed by National Grid Viking Link Limited (NGVL) and Energinet, the Danish TSO. Linking the British and Danish transmission systems will bring significant benefits to GB consumers; including access to more affordable energy, increased security of supply and facilitating a more efficient use of low carbon energy.

NGVL submitted the Viking Link Initial Project Assessment (IPA) to Ofgem in September 2014 and Ofgem granted Viking Link a cap and floor in principle in July 2015. In late 2015 and early 2016 we engaged Ofgem on Viking Link changes since the IPA. Most notably, we proposed an increase in interconnector capacity from 1.0 GW to 1.4 GW. In June 2017, as part of its Window 1 interconnector projects update, Ofgem approved this increased capacity.

In this letter we follow up on the meeting that we had with Ofgem on 18th May 2018, in which we discussed the timing of the Final Project Assessment (FPA) for Viking Link. The FPA is a regulatory requirement in the cap and floor regime. At the FPA stage, Ofgem assesses the efficiency of the project costs and sets the cap and floor values in principle. We were encouraged to learn at the meeting that Ofgem has been considering the benefit of providing

flexibility to Window 1 projects on the timing of their FPA submission if they can demonstrate significant progress towards development.

Our view is that Ofgem would be in the best position to assess the efficiency of the Viking Link project costs if our FPA submission takes place after we award the Engineering, Procurement and Construction (EPC) contracts related to interconnector cables, converters and GB civils. These project items represent a very significant proportion of the total project costs. Through our 2017 and 2018 engagement with the supply chain we have cost estimates for these elements of the project. However, until we award EPC contracts there remains uncertainty in areas such as cable market conditions, metal prices and foreign exchange rates. Therefore, any costs included in an FPA submission prior to EPC contract award would be subject to change.

The remainder of the letter is structured as follows: we begin by presenting a summary of the Viking Link development programme, which demonstrates the progress so far and discusses its current status. We then provide our current cost estimates, [*]. After that, we return to the question of the optimal timing of the Viking Link FPA, taking into consideration our most recent project timeline and the current cap and floor regulatory timetable.

Development programme summary

High level project timeline
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The development phase started in October 2013 with the signing of a cooperation agreement between National Grid and Energinet, and is now in its final stages. Completion of this phase is dependent on the granting of planning consent, the National Grid Board's Final Investment Decision (FID) and EPC contract award. We discuss all of these factors in this section, after providing an overview of the development phase.

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Development phase overview
We are developing Viking Link as a 1.4GW interconnector, a 40% increase in capacity from the IPA assumption of 1.0GW. We discussed this change with Ofgem in late 2015 and early 2016. Ofgem publicly approved this change in June 2017, with its social welfare analysis showing that with this increased capacity Viking Link will deliver £328m in GB social welfare (at 2013 prices), even after taking into account additional Window 2 interconnector projects.

Our work on route planning was relatively advanced at the time of our IPA submission. In 2015 and 2016 we continued assessing and refining options, and in 2017 we submitted our planning and marine applications. The project has already been granted offshore permits

outside of GB and onshore consent for works in Denmark, which includes the converter station. GB planning consent is at an advanced stage but it has not yet been completed for reasons that we explain in the next page. [*].

We have made significant progress on our tendering of EPC contracts for cables, converters and GB civils. We have undertaken four rounds of bid negotiations for cables and converters, and one round for GB civils. [*].

Planning, consents and licenses

We are seeking planning permission for the GB onshore section of the Viking link through the Town and Country Planning Act 1990. There are four GB Local Planning Authorities (LPA) involved in providing planning permission. Our engagement with them began in 2015.

We sought views on potential sites for a landfall point and a converter station with LPAs, statutory and non-statutory consultees, parish and town councils as well as local residents during the Phase 1 consultation which was held in April and May 2016. We carefully considered comments and feedback from this phase of consultation and in August 2016 we confirmed our preferred locations for the landfall point and converter station.

In September and October 2016 we held our Phase 2 consultation with the parties listed above to ask for their views on cable route corridor options connecting the preferred landfall point and the converter station. In March 2017 we confirmed our preferred cable route corridor, which we followed up with further stakeholder engagement.

We submitted individual planning applications to the four relevant LPA in August 2017. We then submitted supplementary information, comprising additional survey data, in November 2017.

Between February and May 2018 each planning application was heard by the LPA at their respective Planning Committees. All four planning applications had a Planning Officer recommendation to approve. Three of the Planning Committees endorsed their Planning Officer recommendation and resolved to approve our application.

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Final Investment Decision

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EPC contracting process

The Viking Link procurement strategy takes into account the project scope, the available technology choices and the supply market outlook. The combination of those factors meant that we did not consider it likely that a turnkey solution for the project would deliver the most cost efficient solution. We therefore designed the procurement process to award separate contracts for cables, converters and cable civil works.

We began our engagement with the relevant supply markets in 2016. We held several industry days that answered supplier questions and helped us refine our procurement strategy. Discussions with the supply chain were of particular benefit for evaluating the capacity constraints in the cable market caused by the concurrent development of several interconnectors. [*].

In 2017 we started our formal procurement activities, starting with cables and converters.[1] In February and March 2017 we issued Pre-Qualification Questionnaires (PQQ) to those cable and converter suppliers that responded to our contract notice. The PQQ was designed to ensure that tenderers had suitable SHEQ[2] standards, technical capability, production capacity to meet our commissioning date and financial stability to meet the needs of such a large project.

We received supplier bids for both cables and converters in August, October and November 2017 and in January and February 2018. In between bid rounds we held technical and commercial meetings to gain a clearer understanding of the offers, raise and resolve technical issues and negotiate the risk allocation within the conditions of the contract. [*].

The GB civils PQQ process began in August 2017. We received bids in December 2017 and in the first two months of 2018 we held meetings with the bidders to discuss the technical and commercial aspects of their propositions. In May 2018 we received updated bids, which we are currently evaluating.

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Cost assessment summary

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[1] We run the procurement of cables and converters as separate contracts that progress in parallel.

[2] SHEQ stands for Safety, Health, Environment and Quality.

Timing of the Final Project Assessment for Viking Link

The cap and floor regime represents a significant and positive regulatory innovation. The regime seeks to promote efficient investment in interconnectors, placing a reasonable balance of risk between investors and customers. Most importantly, the regime ensures that GB consumers benefit from the development of interconnectors.

Viking Link will deliver significant benefits to GB consumers; Ofgem's 2017 analysis estimated that the interconnector will provide £328m in GB social welfare. Over the last four years the project team has been working relentlessly towards moving from project development into construction. We have made significant progress on project design and planning, achieving offshore permits outside of GB and onshore consent for works in Denmark. We have also reached an advanced stage in the procurement of cables and converters, having already received five rounds of supplier bids.

Unfortunately, for circumstances outside of our control, GB planning consent has been delayed. This has had an impact on our EPC contract award timescales, as we cannot commit to EPC contracts until we have certainty over planning consent.

If we were to submit an FPA in 2018 as per the current regulatory timetable, it would contain cost estimates that would be subject to change within the project development phase. In other words, Ofgem would be undertaking an assessment of the efficiency of cost figures that almost certainly would be different after EPC contract award.

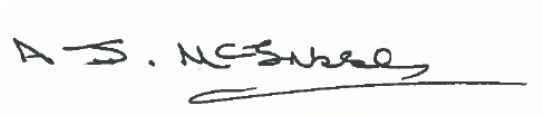
We kindly request Ofgem to allow our FPA submission to take place after EPC contract award, at which time we will have more certainty in areas such as consenting, cable market conditions, metal prices and exchange rates. The exact timing for our EPC contract award is dependent on the resolution of the planning consent situation, [*].

We are mindful that Ofgem, while recognising the practical challenges faced by interconnector developers, wishes to ensure that interconnector projects progress in a timely manner. We will continue to provide Ofgem with quarterly project updates on Viking Link via the National Grid Interconnectors Holding Portfolio Report. We are also prepared to produce updates to the content of this letter at mutually agreed times during the remaining of the project development phase. In addition, we stand ready to work closely with Ofgem to minimise the time between our EPC contract award, the FPA submission and Ofgem's FPA decision.

We would welcome the opportunity to discuss, at your earliest convenience, the views and proposals contained within this letter. To arrange a meeting please do not hesitate to contact Ruben Pastor-Vicedo at Ruben.Pastor-Vicedo@nationalgrid.com.

Kind regards,

Andrew McIntosh



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