

BERR | Department for Business
Enterprise & Regulatory Reform

Offshore Transmission Regulatory Regime

BERR / Ofgem External Communications Workshop

25 January 2008

Introduction

Duarte Figueira

Director, Renewables Deployment Team
BERR

Aims of today

- Provide additional clarity on:
 - the recent Government decisions
 - the scope of further work to be undertaken as set out in Ofgem's Regulatory Policy Update document
 - the key stages and dates in the implementation process
- Encourage discussion
- Answer any questions

Agenda (1)

- **Introduction - Duarte Figueira, BERR**
- **Offshore Transmission – John Overton, BERR**
 - Government Response to Consultation
 - Further Government decisions
 - Q & A
- **Regulatory Policy Update, Robert Hull, Ofgem**
 - Regulatory regime – Colin Green, Ofgem
 - Enduring tender process – Richard Clay, Ofgem
 - Transitional tender process – Colin Green, Ofgem
 - Implementation issues – Colin Green, Ofgem
- **Coffee Break**

Agenda (2)

- **National Grid update – John Greasley, NG**
 - Involvement in Offshore transmission project
 - Connection Application Process
 - Access, charging & compensation
- **Q & A session**
- **Next Steps/Concluding remarks – Duarte Figueira / Robert Hull**
- **Lunch**

Offshore Transmission:
Government Response and Decisions

John Overton

Head of Grid, Renewables Deployment Team

BERR

Government Response to July 2007 Policy Statement (1)

- Policy Statement sought views on:
 - Design of regulatory regime
 - Enduring competitive framework
 - Transitional arrangements
 - Connection application process
 - Number of technical issues
- Closed on 5th September 2007
- Government Response published 10th January 2008

Government Response to July 2007 Policy Statement (2)

- Key proposals in July Policy Statement:
 - OFTOs appointed by competitive tender to design, build, finance and maintain OT networks;
 - Ofgem to make key selection decisions and manage tender process;
 - Annual tender window. Any person meeting pre-qualification criteria could enter tender;
 - Transitional arrangements for projects where generator is already constructing or taking steps to construct OT assets.

Summary of responses and concerns

- Complexity, cost and timing of regime;
- Period of revenue stream;
- Arrangements at end of revenue stream;
- Ability of Ofgem to run tenders;
- Interaction of connection application and tender processes;
- Role of generators in the tender process;
- Annual tender windows;
- Need for OFTO of last resort;
- 75% Ex-ante estimate of RAV.

Government decisions (1)

- That Ofgem will be the body to run the competitive tender process to appoint companies to connect offshore projects
- To enable Ofgem's Authority to recover the costs of running the tender process from participants in the process the Government will seek additional powers in the Energy Bill;

Government decisions (2)

- The Government will also seek time-limited powers in the Bill to enable Ofgem, in limited circumstances, to make a property transfer scheme for transitional projects.

Government decisions (3)

- Timing of new regime now dependent on Energy Bill
- But Go-Active will be as close as possible to our original date of October 2008 (currently expect new date to be December 2008); and
- If the date of Go-Active is delayed, then the date of Go-Live will also be delayed to allow one year for tenders.

Other Issues - OFTO of last resort

- The Government also considers there should be an OFTO of last resort for transitional projects, subject to regulatory safeguards,
- To that end, the Government has asked the Authority to design an appropriate regulatory framework to take this into account.

Other Issues

- Number of issues remain to be discussed with industry;
- Ofgem's Policy Update published 14 January sets out further details and clarification;
- Subject of further work and discussion with industry – starting today;
- Govt's aim to ensure that final package balances interests of generators, OFTOs and consumers.

High-level timetable

- **January 2008** - Publication of Government Response and Ofgem's Consultation Document
- **January - April 2008** - Consultation on draft licence, code and agreement modifications
- **April 2008** - Publication of final policy proposals
- **June 2008** - Consultation on full regime (subject to the completion of consultations on draft licence, code and agreement modifications)
- **September 2008** - Consultation closes
- **December 2008**
 - 'Go-Active' commencement of ss. 90, 91 & 92 of the Energy Act 2004
 - Modifications made to licences and associated codes & agreements
 - First tender process commences, including for those with connections to be adopted
- **December 2009** - 'Go-Live' commencement of ss. 89 & 180 of the Energy Act.

Questions & Answers Session

Regulatory Policy Update: an overview

Robert Hull

Director, Transmission
Ofgem

Where are we in the process?

- **Regulatory Policy Update** – builds upon the Government decisions published in January, specifically that Ofgem will run the competition for the award of offshore transmission licence;
- **Objective of the document** – our policy proposals provide greater detail and clarity on the proposed regime and its implementation for further consultation. Views are sought to inform development of final policy proposals for the regime;
- **Next steps** – we welcome responses and continued industry engagement over the coming weeks and months. The joint final policy proposals document is anticipated for April 2008;
- **Energy Bill** – Government is seeking powers to allow the Authority to recover the costs of the tender process from participants in the tender process and make transfer schemes to facilitate the adoption of transitional assets; and
- **Implementation** – we envisage the new regime will commence as close as possible to December 2008 ('go active' date) so the process for awarding licences can commence. We then expect the new regime would come into force around December 2009 ('go-live' date).

Policy principles for the offshore regime

- In the context of Government renewable targets, to ensure the efficient and effective connection of offshore renewable generation to the onshore Grid;
- A regulatory regime which strikes an appropriate balance between protection of consumers' interests and promoting connection of renewable generation;
- Developing an effective competition for the appointment of OFTO's which will deliver value for money and fit for purpose infrastructure;
- Designing a regime to attract prospective OFTO's by providing sufficient clarity and certainty in terms of risk and rewards;
- Ensuring that industry process operate effectively to support the proposed regulatory framework.

Key proposals from the regulatory policy update (1)

Design of the regulatory regime

- Largely reaffirms the position set out in the Ofgem/BERR joint policy statement:
 - OFTO is appointed by competitive tender and awarded a transmission licence. This will set out the obligations and entitlements of the OFTO, including 20 year revenue stream and performance obligations and incentives;
 - Transmission projects would be re-tendered upon the expiry of the revenue stream or would have revenue entitlement reset;

Design of the enduring OFTO tender process

- Provides further detail on the process building upon the Ofgem/BERR joint policy statement:
 - Tenders would be run by Ofgem;
 - For new projects, triggered by a connection application by an offshore generator, but could be triggered upon signing of the indicative connection offer;
 - For existing projects falling within the enduring process, triggered when variations to existing connection agreements are sought.

Key proposals from the joint policy statement (2)

Transitional arrangements

- Largely reaffirms the position set out in the Ofgem/BERR joint policy statement:
 - Transitional projects that reach full financial close by 'go-active' will enter transitional tender process at that time;
 - Transitional projects that reach financial close after 'go-active' but by 'go-live' can enter a transitional tender process that will begin shortly after 'go-live';
 - Developers can expect to receive 100% of the efficient ex-post cost of their transitional projects;
 - Developers will receive comfort on costs, subject to pre-conditions being met;
 - Energy Bill seeks powers to make transfer schemes to facilitate transfer of assets. We would expect these to be used where terms cannot be commercially agreed.

Other policy proposals

- Charging access and compensation arrangements
- Technical rules

Regulatory regime

Colin Green

Head of Offshore Transmission & Projects
Ofgem

Regulatory regime (1)

Regulatory Regime – builds upon the Ofgem/BERR joint policy statement and informed by stakeholder views:

- Period of the revenue stream:

- Offshore transmission licences would be awarded with specified revocation conditions – enabling the Authority to revoke the notice after a specified period provided appropriate notice given.
- Ofgem proposes a 20 year revenue entitlement that would begin once assets are constructed and operational – implemented through special licence conditions;
- Proposed 20 year revenue entitlement is based upon the expected life of an offshore wind farm;
- End of revenue stream – either re-tender or extend licence term based on demonstrable need

Regulatory regime (2)

• Incremental capacity requirements:

- Need for a mechanism to deal with the requirement for incremental capacity – pre-completion of construction and post construction;
- Pre-completion – expect OFTO to give firm prices for incremental works offshore as part of bid. If requirement for incremental capacity triggers a major variation of the connection agreement onshore then minded to re-run tender;
- Post-construction – expect generator to apply for variation to connection terms that would be notified to Ofgem. Need to consider whether material and therefore trigger tender. Suggest a threshold of 20% would determine materiality.

Regulatory regime (3)

- Other pre-defined adjustments:
 - Continue to believe that on balance pre-defined adjustment mechanisms for changes in costs and exceptional events are difficult to construct robustly. Potential distortion is likely to outweigh the benefit;
 - Ofgem will consider exceptional events however on a case-by-case basis.

Regulatory regime (4)

•Performance obligations and incentives:

- Regulatory policy update seeks views on several aspects of the incentive framework:
- The activities that should be incentivised – availability, reliability, delivery, losses?
- level at which incentives targets might be set and the limits of exposure for an OFTO business;
- Whether targets should be based on annual performance or performance over a longer periods
- Welcome thoughts from industry

•Other areas covered:

- Generator requirements;
- Allocation of risk;
- Regulatory reporting requirements and ring-fencing

Issues for consultation

- **Period of the revenue stream**
 - do you agree with our proposal for 20 year revenue stream and approach to dealing with projects that continue beyond this period?
- **Performance obligations**
 - What is the appropriate scope of incentives?
 - Asymmetric or symmetric incentives?
 - What is the appropriate level exposure for the OFTO?
- **Incremental capacity**
 - The approaches outlined in the regulatory policy update for dealing with incremental capacity?

The background of the slide features a large, white, stylized arrow pointing to the right. Behind the arrow, there is a blurred image of a modern building with a glass facade and a large, orange, abstract shape resembling a stylized 'B' or a flame. The overall color palette is light blue and white.

The competitive tender process

Richard Clay

Senior Manager – Offshore Transmission & Projects
Ofgem

Key objective

- Government has decided that Ofgem should run the competitive tender process for the selection of OFTO licensees
- Our key objective in running the process is:

...“to ensure that the tender process reveals efficient, fit for purpose offshore transmission investment solutions for offshore generation projects.”
- Our proposed framework has been developed in accordance with this.

Tender process (1)

- Proposal is for a four-stage process:
 - Expressions of Interest and prequalification
 - Invitation to Tender
 - Best and Final Offer
 - Selection of Preferred Bidder
- Received broad support in July, and we propose to adopt for selecting OFTOs
- Similar to many other tender processes
 - Certainty for participants
 - Recognisable to other stakeholders

Tender process (2)

- Process triggered by application for connection received by GBSO
 - Clear interaction with the connection application process
- Stakeholders have a role to play in the process, e.g.
 - **Offshore generator** triggering process and will be able to consider variant bids against requirements
 - **GBSO** providing information to bidders during tender

Expression of Interest

- Purpose is to stimulate sufficient interest in offshore projects
- Supported by standardised documentation
- Responses will be assessed in accordance with predefined prequalification criteria, e.g.
 - Technical ability
 - Financial capability

Invitation to Tender (1)

- Purpose is to identify a preferred bidder that will be able to deliver the offshore transmission infrastructure
 - Where more than one preferred bidder is identified, BaFO will take place
- Supported by standardised documentation, e.g.
 - Statement of requirements
 - Standard Licence Conditions
 - Data room guide
- All ITTs will be issued for qualifying projects during the tender window
 - Bidders will have ~3 months to respond
 - Standard format for responses

Invitation to Tender (2)

- Responses will be assessed in accordance with predefined criteria, e.g.
 - Annual revenue stream
 - Technical solution
 - Evidence of key supply chain contracts
- Variant bids will be assessed at this stage
 - We would expect to discuss these first with the generator to understand whether they met their requirements
- Process will yield a preferred bidder

Best and Final Offer

- Optional stage, that is expected to be used only where ITT evaluation yields two or more similar quality bids
- BaFO documentation will be determined on a case-by-case basis
 - Opportunity for bidders to refine bids in specified areas
- Responses will be assessed in same way as at ITT stage

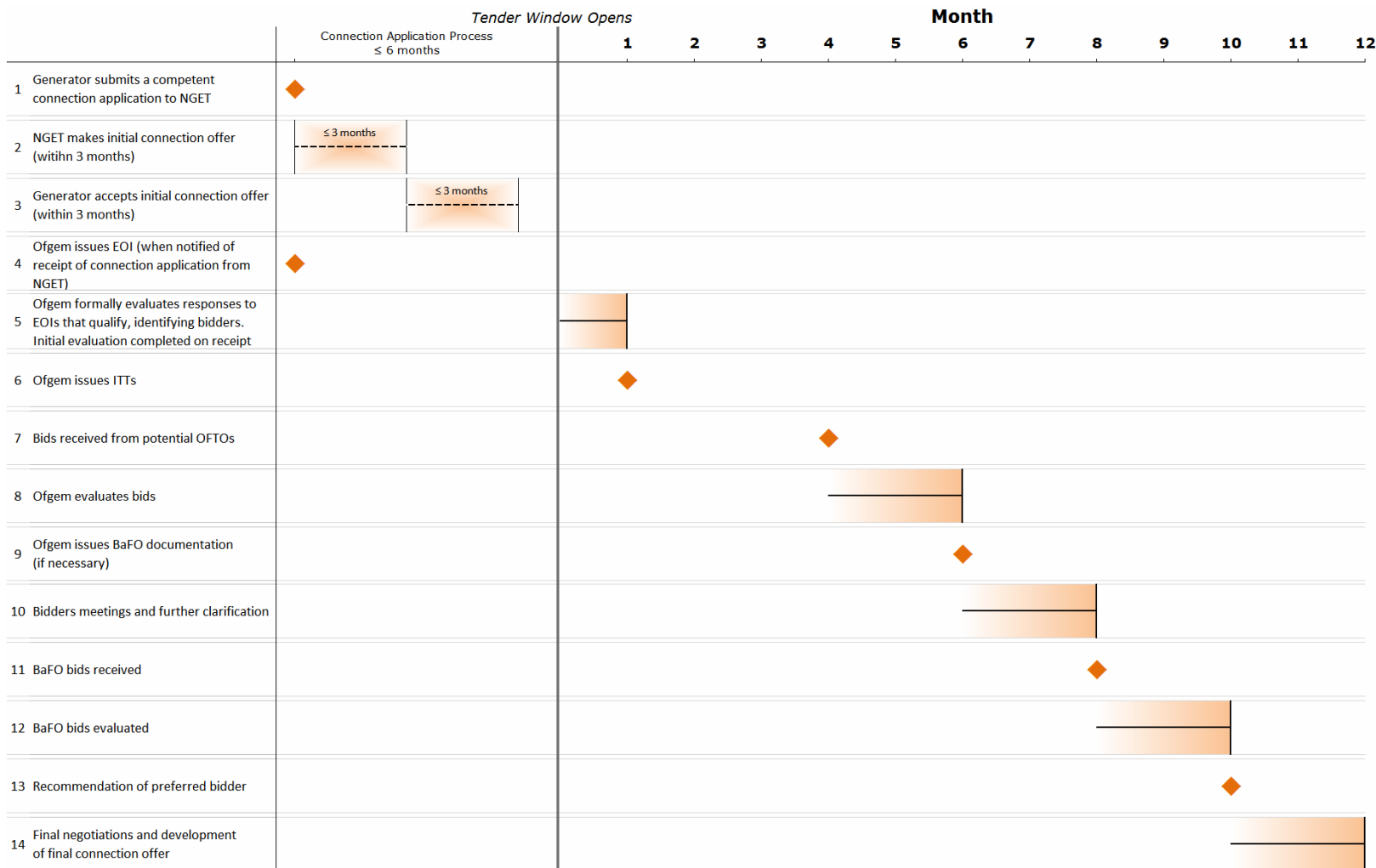
Selection of Preferred Bidder (1)

- Identification of the Preferred Bidder will trigger final negotiations and facilitate development of final connection offer by GBSO
- Preferred Bidder will need to undertake number of activities at this stage, e.g.
 - Undertaking environmental impact assessments
 - Obtaining relevant leases and consents
- We propose that the Preferred Bidder enter into 'agreements in principle' with GBSO at this stage, and provides financial commitment to guarantee costs of construction

Selection of Preferred Bidder (2)

- When all outstanding issues are resolved, we expect the GBSO and offshore generator to enter into connection agreement
- Authority will confirm issue of OFTO licence and approve the revenue stream
- Post licence award, we propose the OFTO, offshore generator and GBSO would coordinate works to ensure delivery of the offshore transmission connection

Tender process timeline



Tender Regulations

- Process will be formalised in new Regulations, made by the Authority
 - Set out the detailed rules of the process
 - Accompanied by guidance for stakeholders
- Regulations will be developed over the course of this year
 - Opportunity for stakeholder involvement

Cost recovery

- Government seeking powers through Energy Bill to allow Ofgem to recover costs of running tenders from participants
 - Not appropriate to finance through normal channels
- We propose to use these powers to require the offshore generator and bidders to provide a mixture of security and cash payments to finance the process
- Bidders expected to pay a fair proportion of costs. Established using a cost reflective methodology. Any excess monies held will be refunded to unsuccessful bidders as process progresses
- Security will revert to provider when process concludes

Issues for consultation

- Overall approach?
- Trigger for the tender process?
- Involvement of stakeholders in the tender process?
- Interaction between the connection application process and the tender process?
- Proposed approach for cost recovery?

Transitional arrangements

Colin Green

Head of Offshore Transmission & Projects
Ofgem

Transitional arrangements (1)

- Regulatory policy update reaffirmed many of the policy proposals for transitional projects previously set out in the Ofgem/BERR joint policy statement.
- Tender exercises will be undertaken for projects that have constructed, are under construction or have reached financial close by either “go-active” or “go-live”;
- Projects will be tendered for adoption once construction complete;

Transitional arrangements (2)

- As a last resort, we would consider awarding the offshore transmission licence to the offshore generator, where an OFTO has not been successfully identified;
- Projects should expect to receive Ofgem's valuation of the full ex-post efficient cost of the transmission system upon adoption.
- Ofgem will provide comfort that the developer will receive no less than 75% of our ex-ante estimate for the project once projects have reached financial close;
- Government is seeking additional powers through the Energy Bill to allow for Transfer schemes.

Pre-conditions for comfort on costs (1)

- Ofgem intends to assess the value of the assets to be adopted by an appointed OFTO.
- Project will be adopted based upon the full ex-post efficient cost.
 - This may be more or less than the ex-ante estimate of costs
- We would expect to provide a letter of comfort once all of the pre-conditions have been met.

Pre-conditions for comfort on costs (2)

- Developers will need to show:
 - It has an onshore connection agreement;
 - It has all necessary property rights to enable someone to operate and maintain the system;
 - Entered into contacts for construction of the offshore transmission assets;
 - Evidence of full financial close (or equivalent);
 - All financial and technical data necessary to undertake an efficiency assessment of the cost of construction
- It is also important that developers set out the commercial terms on which transfer of property rights, liabilities and assets would take place.
- We envisage that the transfer scheme powers would only be activated in exceptional circumstances.

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Implementation of the new arrangements

Colin Green

Head of Offshore Transmission & Projects
Ofgem

Next steps in process (1)

- Proposed refined work-streams based on outputs require to implement the regime:
 - OFTO Licences
 - Consultation document published shortly scoping required changes;
 - Industry work group from late Feb onwards;
 - Consultation on legal text – April 2008.
 - Industry Codes
 - Industry engagement vital;
 - Working group established to consider Embedded Transmission Issues – including changes required to Distribution Code and DCUSA;
 - Invited industry engagement in further development work of Grid Code, GBSQSS and STC;
 - Consultations on text once available.

Next steps in process

- Tender process
 - Tender workshop to be held at Ofgem on 22 February;
 - Draft tender regulations will be consulted upon with Final policy proposals in April;
 - Workshop on draft tender regulations in late May 2008.

Offshore Transmission External Communication Session

National Grid Electricity Transmission Workstream
Update

Friday 25th January 2008

National Grid's Involvement

- ◆ National Grid's role in the development of the offshore electricity transmission arrangements is
 - ◆ Designated as System Operator in August 2006
 - ◆ Extensive role in developing and drafting technical rules
 - ◆ Grid Code
 - ◆ SQSS
 - ◆ SO/TO Code
 - ◆ Leading on development of
 - ◆ The User Connection Process
 - ◆ Transmission Charging
 - ◆ Access and Compensation
- ◆ Deliverables based on the principle that onshore arrangements apply offshore unless good reason not to

Connection Process

- ◆ National Grid has a statutory obligation to offer terms to users for connection to the transmission system
- ◆ The obligation will persist with the introduction of the offshore transmission arrangements
- ◆ This presents a number of challenges relating to
 - ◆ Synchronising with a transmission tender
 - ◆ Incorporating onshore distribution network solutions
 - ◆ User Commitment
- ◆ We have been working with Ofgem and BERR to develop a process which will deliver
 - ◆ Offers of sufficient quality to be taken forward to tender
 - ◆ Flexibility needed to cater for the output of the tender process and offshore design development
 - ◆ Appropriate levels of contractual certainty for users at the various stages of their project

Connection Process

- ◆ Interested parties have been invited to a user connections workshop on **1st February 2008** at National Grid's offices in Wokingham
- ◆ The workshop will cover
 - ◆ the basic offshore connection process (including interactions with the tender process, as appropriate)
 - ◆ a number of scenarios e.g. interactivity
 - ◆ opportunity to discuss key issues/ concerns (as raised by stakeholders)
- ◆ Contact jo.habberley@uk.ngrid.com for more information
- ◆ Please note this session is almost fully booked

Transmission Charging

- ◆ National Grid has been developing its charging methodologies to cater for offshore transmission in line with our obligations to keep the methodologies under review
- ◆ The offshore charging pre-consultation was issued in July 2007
- ◆ Industry responses were reviewed and assessed in the development of transmission charging modification proposal GB ECM-08
- ◆ The transmission charging consultation “Charging arrangements associated with the Offshore Transmission Networks” was issued to CUSC users on 21st December 2007

- ◆ Consultation documents are available on National Grid’s website at

<http://www.nationalgrid.com/uk/Electricity/Charges/modifications/uscmc/>

Transmission Charging

- ◆ The offshore charging consultation covers
 - ◆ Offshore Connection and Use of System Boundary
 - ◆ Offshore Circuit Expansion Factors
 - ◆ Treatment of High Voltage Direct Current (HVDC)
- ◆ Responses are invited by **31st January 2008**
- ◆ Next Steps
 - ◆ We plan to report the outcome of the offshore charging consultation to Ofgem in early spring 2008
 - ◆ Related work on the charging treatment of transmission connection design variations is ongoing
 - ◆ We expect to consult on charging for embedded transmission pending finalisation of key embedded transmission policy areas

Transmission Access and Compensation

- ◆ An industry workshop was held at National Grid's offices in Warwick on 3rd December 2007
- ◆ We presented outline proposals on Access and Compensation, based on the principles established in Ofgem and BERR's July policy statement
 - ◆ Access rights linked to offshore transmission equipment redundancy
 - ◆ Compensation for access restrictions due to offshore events linked to offshore transmission equipment redundancy
 - ◆ Compensation to offshore users used to manage onshore constraints equivalent to onshore users
- ◆ Proceedings of the meeting were documented and circulated to attendees and CUSC parties along with key policy questions

Transmission Access and Compensation

- ◆ Responses are invited by 5th February 2008
- ◆ For more information please contact the offshore team at National Grid

gbsso.offshore@uk.ngrid.com

- ◆ Responses will be used to formulate National Grid's report to Ofgem and BERR on offshore Access and Compensation

Conclusions / next steps

Duarte Figueira, BERR

Robert Hull, Ofgem

Conclusions / next steps

- There is still significant work to be done as set out in Ofgem's document
- Key that stakeholders continue to engage in the process
- Significant work for Government and Ofgem to deliver Energy Bill powers to enable the regime to function as planned
- Commencement of regime and timetable tied to delivery of Energy Bill powers

High-level timetable

- **January 2008** - Publication of Government Response and Ofgem's Consultation Document
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- **December 2009** - 'Go-Live' commencement of ss. 89 & 180 of the Energy Act.

Points of contact - Ofgem

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