

Email to:

[oftobuild@ofgem.gov.uk](mailto:oftobuild@ofgem.gov.uk)

4 May 2024

Dear OFTO Build Tender Development team,

**Response to initial proposals for an OFTO build model to deliver non-radial offshore transmission assets consultation**

Scottish Renewables is the voice of Scotland's renewable energy industry. The sectors we represent deliver investment, jobs and social benefits and reduce the carbon emissions which cause climate change. Our 360-plus members work across all renewable energy technologies, in Scotland, the UK, Europe and around the world. In representing them, we aim to lead and inform the debate on how the growth of renewable energy can help sustainably heat and power Scotland's homes and businesses.

Scottish Renewables welcomes the opportunity to respond to Ofgem's consultation on its initial proposals for an Offshore Transmission Owner (OFTO) build model to deliver non-radial offshore transmission assets. The Electricity System Operator's (ESO) 'Beyond 2030'<sup>1</sup> plan sets out a sophisticated web of transmission architecture required to meet the UK's ambitious net-zero by 2050 target, including 50GW of offshore wind by 2030. A fundamental design element, which marks a noticeable departure from the previous Holistic Network Design (HND) plans, is the clustering of offshore wind farms via shared infrastructure. Offshore 'hubs' efficiently replace the need for singular, radial connections to shore, thus reducing coastal disruption, as well as financial, time and material costs.

While the OFTO regime is responsible for radial offshore connections, developing a methodology to ensure timely connections for multiple developers via a single OFTO is a highly complex task. Our response<sup>2</sup> to DESNZ's call for evidence<sup>3</sup> around the OFTO regime early this year highlighted the issues our members are encountering with the existing profile of OFTOs in the UK, which is predominantly thinly capitalised and resourced Special Purpose Vehicles (SPVs). Ofgem's proposition of an OFTO build model might see significantly increased responsibility placed onto the UK's already shallow pool of OFTO owners to construct novel assets without prior construction experience.

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<sup>1</sup> [Beyond 2030 | ESO \(nationalgrideso.com\)](https://www.nationalgrideso.com/beyond-2030)

<sup>2</sup> [SR Response: Offshore Transmission Owner \(OFTO\) regime call for evidence \(scottishrenewables.com\)](https://www.scottishrenewables.com/sr-response-offshore-transmission-owner-ofto-regime-call-for-evidence)

<sup>3</sup> [Offshore Transmission Owner \(OFTO\) regime - GOV.UK \(www.gov.uk\)](https://www.gov.uk/offshore-transmission-owner-ofto-regime)

While our aforementioned response recognised the possibility of an OFTO or incumbent Transmission Owner (TO) undertaking non-radial asset buildout, we believe that the presented model needs to rebalance risk allocation to ensure assets are delivered on time and cost-effectively for consumers. Guaranteeing meaningful compensation for developers in the event of delayed delivery that also effectively incentivises OFTOs to build at pace requires more innovative, reinforced methods.

Venturing into a complex and, as yet, unknown infrastructural world, inevitably increases risk for all parties involved. Risk must be strategically managed to prevent delays caused by commercial negotiations or bankruptcy which could lead to increased costs and put net-zero goals at risk. It is also important to avoid excessive premiums that could overburden consumers.

Recognising the national importance of these works, we also expect the tendering process to include a pre-qualification stage that would ensure only the most experienced companies, which have an extensive history of delivering infrastructure (on-time and on-budget) including in other markets, are shortlisted to be considered for the role of OFTO builder. This shortlist should not preclude incumbent onshore TOs if they choose to bid, nor capable, third party, construction specialists from entering the transmission space. Finalising the conditions of a model that can attract capable bodies to bid while balancing risk fairly will determine the success of the shared asset buildout.

In an early competition model for OFTO builders, experience with development will be most relevant, while participation in a later competition model would rely additionally and more heavily on capabilities in construction and delivery. Within the tendering process, the specific skillsets relevant to the decided upon stages of the asset for which the OFTO builders will be responsible should be appropriately weighted.

Additionally, Ofgem should assess all opportunities to accelerate the process of delivering a coordinated, offshore network and achieving promised consumer value, including via the tendering process. Considering an Accelerated Strategic Transmission Investment (ASTI)-style approach for the required offshore transmission infrastructure could help mitigate financing and procurement issues by packaging and investing in strategic works.

Recognising the scale of transmission works commissioned nationwide and the immense workload of existing TOs, OFTO builders and developers need to be adequately supported in their collaborative undertaking of these works. Additional monitoring of project performance while delivering novel infrastructure could be introduced initially, by Ofgem, as an interim

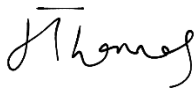
measure as the stable of competent OFTO builders gain market recognition and relevant expertise.

In addition, the inclusion or updating of clear asset classification terms and definitions for radial and non-radial assets in the context of the 'Beyond 2030' plan would aid clearer collaboration on this piece going forward. Scottish Renewables is urging Ofgem to reconsider aspects of its design to ensure a robust scheme is in place for the timely delivery of vital offshore wind generation to meet climate targets.

Ofgem must think critically through the lens of the current macro-economic landscape and the capacity of the existing UK TOs to design a regulatory regime that is realistic and safeguards the UK's ambitions on climate targets.

Please find our response to the questions posed in the consultation below, where we have provided more detail on the highlighted issues. Scottish Renewables would be keen to engage further with this agenda and would be happy to discuss our response in more detail.

Yours sincerely,



Holly Thomas

**Grid & Systems Policy Manager**  
**Scottish Renewables**

## **1. Which party should be responsible for procurement in the late competition OFTO build model and why?**

As is the case with various elements of the late competition OFTO build model, there are high levels of uncertainty associated with procurement for either party. Regardless of which is eventually selected, procurement will have to be undertaken before confirmation of a firm route to market and thus, at risk. However, among Scottish Renewables' members, there is consensus with Ofgem's minded-to position that the developer, via Option 2, is the most viable party to engage with the supply chain and procure the necessary parts.

Similarly to the constraints faced by Competitively Appointed Transmission Owner (CATOs) via onshore competition models, OFTO build organisations simply do not possess a sufficient pipeline of projects to secure materials for assets in the current market at a competitive rate or in necessary timescales. Due to the severely constrained supply chain for High-Voltage Direct Current (HVDC) cables globally, suppliers can and will 'cherry-pick' larger, standardised orders for cost and design efficiency reasons.

The limiting nature of the model, predicated on building circuits on a case-by-case basis, prohibits OFTO build organisations from achieving the volume required to secure competitive contracts. Only via large scale tendering of multiple contracts over a multi-year period could OFTO build organisations amass sufficient volumes to undertake procurement more realistically. Such a package approach could also help curb current time lags on HVDC cables, which are currently 7-10 years from point of contact to asset transmission. Thus, within the proposed model, maintaining consistency, certainty and scale in procurement by involving the developer in a comprehensive package of works in the short term avoids a more costly, delayed and 'piecemeal' approach until organisations have transitioned to be OFTO builders and are potentially able to assume greater overall ownership in the longer term.

However, there are complex liabilities associated with procurement for the developer and the risks incurred need greater consideration by Ofgem. The allocation of risk during the developer phase of pre-construction and procurement, and the question of anticipatory investment on behalf of 'late users' (those developers connecting to shared offshore infrastructure at a later stage), needs more detail for developer security.

Similarly, there should be some standardised guidance for ensuring the successful transfer of procurement contracts to maintain clear and strong relationships with the suppliers. For example, the current lengthy lead times for securing HVDC cables could bring about the possibility of renegotiation with Original Equipment Manufacturer (OEM) suppliers at the time of contract transfer between the developer and new OFTO build organisation. Ensuring that

suppliers are not deterred via the unconventional change of hands will be vital to avoid weakening the UK's attractiveness for suppliers. In light of the complex challenges being faced within the supply chain market at present, Ofgem needs to ensure it is thoroughly informed of the various issues, e.g., via benchmarking, to suggest policies that ensure efficiency and effectiveness.

To mitigate risk to the developer and uncertainty to the supplier at this stage, it would be beneficial to explore including the OFTO build organisation in the procurement discussion as soon as feasibly possible once appointed. If there is the possibility for the OFTO build organisation to join final stage negotiations, such as agreeing to the draft contract that the developer has arranged, the OFTO build organisation could engage directly with the supplier before contract finalisation.

In addition, including the OFTO build organisation at this juncture would allow them to be held more accountable during construction as they would hold shared responsibility for the procurement. If the timings of such an arrangement are not afforded via the proposed model, there should be a formal acceptance by the OFTO build organisation of the procurement contract and any associated risks. This would prevent the OFTO build organisation from demanding contingencies from the developer, which would place undue commercial risk onto and de-incentivise the developer from undertaking procurement, particularly in a shared-asset environment.

## **2. At what point should the OFTO tender process commence? Does option 1 or option 2 present the best approach?**

As acknowledged by Ofgem in the consultation, Scottish Renewables believes that carrying out the OFTO build tender process before consent grants would pose an unsurmountable level of risk and thus, we believe Option 1 is the only viable route.

Only with consent granted would potential OFTO build bidders be able to secure final investment decisions (FIDs). In addition, pre-FID capital expenditure is also kept to a minimum for potential bidders via Option 1. Option 2 could otherwise increase upfront costs associated with assessing a project's viability. Option 1 facilitates existing, capital-low bidders to engage in the bidding process more easily, whilst also attracting more experienced OFTO builders through providing more project certainty.

Bidders are inherently reliant on an indication of price to be able to submit an informed project bid. If the developer is undertaking the procurement, they will require information from tender returns to sufficiently inform the OFTO invitation to tender (ITT). Designs need to be

sufficiently detailed for suppliers to estimate costs accurately and early engagement with the supply chain allows suppliers to plan for activity in terms of facility capacity, which could include facility investment. Under Option 2, the developer's design is all that is available to inform its ITT. Without a consent, developers would be unable to solicit accurate bids, leading inevitably to a delayed and ineffective tender process.

In addition, during the consenting process itself, constraints and conditions may arise and lead to significant delays or even render a project non-viable if solutions are too costly. For example, underestimated challenge from local stakeholders. If the tender process were to run concurrently with consenting, the former could receive knock-on delays from complications resulting from the latter, leading to a drawn-out process that could eventually be futile if a project did not ultimately go ahead.

Relating to the tendering process more generally, Ofgem needs to remain cognisant of the shrinking timelines to deliver the offshore transmission network and, as such, should seek all opportunities to accelerate the tender process while maintaining a rigorous review.

- 3. Do you agree with the view that, providing stakeholder engagement is properly conducted ahead of consent submission, developers should have a reasonably clear view, at the time of consent submission, as to whether the consent is likely to be granted in the form requested, and that an OFTO would be comfortable to submit tender bids on this basis?**
  
- 4. As compared with commercial liquidated damages, how effective are options 1 and 2 in incentivising timely delivery and managing the risk of delay? Could these options make OFTO build a meaningful option for the developers?**

The lack of appropriate risk mitigation for developers is a key issue that has deterred the use of the OFTO build model for radial connections. Ofgem needs to identify innovative, pragmatic approaches to fit the typical OFTO builder profile that go beyond existing models if this model is to have any chance of success.

Due to the current OFTOs' limited capital, Option 1 which employs a standardised delay charge mechanism to compensate developers would most likely render OFTO build too high-risk and deter potential bidders. Within Option 1, Scenario B would offer the most effective compensation for developers through the portion supplemented by consumers; however, Scottish Renewables does not consider Option 1 a viable route for developer compensation.

Under Option 2 whereby the revised existing Tender Revenue Stream (TRS) availability incentive would be subject to an annual cap, the compensation to developers risks becoming insufficient. The strength of the incentive for the OFTO builder to deliver on schedule may also be weakened due to the time delay in application of the penalty (with compensation being paid out years later). Ofgem should strengthen this model to provide a more meaningful signal than the availability incentive sends at present. To appropriately compensate developers, the incentive should mitigate delays that erode Contracts for Difference (CfD) commissioning windows and connection dates with the ESO.

Alternatively, Ofgem could consider including a series of stage gates within the OFTO build project to monitor and incentivise performance in line with the developer project build, which could employ more immediate ramifications for delivery delay, e.g., withholding of payments. Issues outside of the OFTO build organisations' control could be accounted for within contract contingencies to avoid unfair penalties through this model.

Once OFTO build organisations are more established with delivering shared, offshore transmission infrastructure, like the incumbent onshore TOs, levels of monitoring introduced in the interim could be subsequently reduced. However, considering fairness in the model, there would also need to be measures in place to protect OFTO development in the event of developer delays.

Developers / the ESO should also be encouraged to de-risk their designs as much as possible to mitigate risks within their control. OFTOs currently have incentives to maintain 98% export availability, so a similar policy should be applied to this model. For example, designing a multi-circuit OFTO build could enable staged circuit energisation through non-firm connection should the build encounter delays with the full delivery package, thereby allowing the developer to export a portion of its project capacity. This would attract lower TNUoS charges until final, full project energisation and allow the developer to attract merchant benefits of pre-CfD market prices. Balancing the final cost to consumers of such designs, especially in light of the constrained HVDC market, versus the risk of delayed output will be important for encouraging innovative designs that benefit all parties.

Scottish Renewables recognises that Ofgem must balance performance incentives with attracting sufficient market investment; however, the models proposed at present place undue risk on the developer in both scenarios.

**5. How can the OFTO delay charge and consumer underwriting in option 1, as well as the TRS reduction in option 2, be appropriately set and executed?**

**6. Which of the four proposals offers the most suitable option for the treatment of cost increases during construction?**

Among our members, there is little preference between the four proposals outlined but rather a desire to see OFTO build organisations carry a larger portion of the risk appropriate to their ability to control it, as the party responsible for construction. While Options 1 and 2 are less contingent on the level of capital, there is the potential that within Option 2, OFTO build organisations would include a risk premium into their bid offer up to the threshold value and so the benefit of this approach is unclear.

If cost increases are outside of the OFTO build organisation's control, i.e., due to the macro-economic environment, Ofgem could explore options similar to those within the developer-build model such as a RIIO re-opener mechanism with a threshold. A clear definition of events outside of the OFTO builder's control should be developed by Ofgem, including any conditions whereby additional costs would be shared between the OFTO builder and the developer.

**7. What, in your view, is an appropriate calibration for the pain-gain share mechanism outlined in options 3 and 4?**

The 'pain-gain' share calibration should proportionately reflect the control each respective party has over the construction process, of which the transmission construction organisation has the majority. In the event of cost increases during construction, developers may likely already be disadvantaged by a potential delay and thus, penalising them further when they have little to no control seems illogical.

As it stands, the mechanism seeks to protect OFTO build organisations to attract more competition to the market and over-penalises developers. While developers will benefit from the shared asset, Ofgem should reweight the share to better shield developers and recognise the responsibility of the constructing party to manage the risk in this model more effectively.

More generally, within Ofgem's remit of protecting consumers, it should consider mechanisms that reduce unnecessary, inflated risk premiums from being incorporated into CfD and TRS bids that are ultimately recovered from the consumer. Simple delivery models with residual risk shared ex-ante across consumers, as opposed to the OFTO build organisation or developer estimating premiums based on uncertain cost assumptions, could reduce total cost to consumers. Managing risk premiums while maintaining sufficient



incentive to affect behaviour and encourage successful delivery will be key to timely, cost-efficient delivery.

- 8. Should we expand the refinancing gain share mechanism to cover the conversion of equity to debt or the sale of equity? How could the mechanism work in principle?**
- 9. What do you think is the best way to deal with a failure scenario during construction?**
- 10. In the event that the appointed OFTO cannot continue with the project, which party is best placed to take the build to completion? How should the transfer value for a partially completed project be set?**

In the event of failure during construction where the risk is shared between OFTO build organisation and the developer, we believe that the developer would be best positioned to respond via step-in rights due to having the most experience and knowledge of the project to resume the asset efficiently. The option of an incumbent TO or CATO taking over as an OFTO builder of last resort is also possible if sufficient contingency is included but this approach could result in additional delay, not least through the need for a re-tendering process. However, this approach would be likely necessary in the specific event of failure post construction as, if an asset was already operational, a transmission license would be required to take over the asset. To avoid continued difficulties in inheriting the project, Ofgem would need to investigate the causes of the failure and assess these criteria closely against those taking over the project.

However, if the developer were to assume the failed build, it would require significant assistance, financially and otherwise, to be able to complete the construction of the asset. Failures would likely need to be assessed on a case-by-case basis whereby the financial credentials and capabilities of the project developer would be considered. Ensuring that such a risk is not priced into developer CfD bids is also important for keeping costs down. In addition, the contractual complexity of and risk undertaken in resuming a half-stranded asset would require assistance and potentially benefit from some standardised guidance where possible.