

## **Renewables Obligation – Announcement of a review into the support for offshore wind**

Following the announcement in the Budget on 22 April that we are reviewing the support for offshore wind under the Renewables Obligation, this sets out more detail about this process and the proposals which we have suggested we would bring in if the review and consultation process supports our current analysis.

We are aware that the economics of offshore wind projects have been particularly hard hit by a combination of the credit crunch coming at a time when their supply chain costs were already rising. We have commissioned a study by Ernst and Young into the costs being faced by projects which are looking to achieve financial close in the next year. The results set out in their report appear to demonstrate clearly how a combination of factors has led to significant increases in costs over a relatively short period. These factors include: increased costs due to the immature supply chain; increased foreign exchange costs where the majority of the capital costs are priced in Euros or Danish Kroner; and increased cost of risk in the current financial climate. Given that this report is based on evidence provided to us by developers and on Ernst and Young's own information, we believe that this is a robust piece of work. This report has been published<sup>1</sup>.

The Secretary of State has decided that these changes to the costs of generation meet the criteria for announcing an early review of the offshore wind banding provisions set out in the Renewables Obligation Order 2009. Therefore, as part of the Budget, we have announced a review of the support for offshore wind under the Renewables Obligation (RO).

We intend to complete this review over the next few weeks and would be grateful for any additional evidence on the costs which you can provide to us. In particular comments on the assumptions and analysis contained within the Ernst and Young report would be most welcome. We will also be asking the Renewables Advisory Board to peer review the evidence and analysis provided in that report.

If the review confirms the information we have received to date, we would consult on amending the Renewables Obligation Order with effect from 1 April 2010 so that offshore wind projects qualified for 2 ROC/MWh subject to a number of conditions. These conditions would be designed to ensure that any additional support is targeted at projects which are most affected by the current high costs caused by the supply chain issues and current financial climate; these are the projects which we believe would otherwise not proceed. However we expect that several of the factors which have led to the increases in cost will be resolved over the next one or two years as the supply chain matures and the financial position stabilises. Our current view therefore is that only projects which reach financial close over a limited period will be eligible for any additional support.

Any proposal to change the bands will, of course, be subject to state aid clearance.

Before making any change to banding for offshore wind the Secretary of State will have regard to the matters set out in section 32D(4) of the Electricity Act 1989 (as

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<sup>1</sup> <http://www.berr.gov.uk/energy/sources/renewables/policy/renewables-obligation/page15630.html>

amended). Based on the evidence we have to date, however, and subject to the outcome of the statutory consultation we anticipate amending the banding of offshore wind along the following lines.

Any increased support will be limited to the capacity of a generating station which meets defined criteria as outlined below. We refer to this in the text that follows as the 'specified generating capacity'.

Electricity generated using a specified generating capacity of an offshore wind generating station (or a part of a generating station) of defined site which meets the following criteria should be eligible for 2 ROC/MWh:

- Nobody has entered into a firm contract for the delivery of wind turbines generators relating to the specified generating capacity before 22 April 2009.
- The firm contract is made for the delivery of wind turbines generators for the specified generating capacity no later than 31 March 2010.
- A copy of that contract is sent to Ofgem, or otherwise made available for audit (we will aim where possible to make use of the information which is already being reported to Ofgem for the OFTO process).
- At least one foundation for the installation of one of the turbines subject to the qualifying order in that generating station (or the specified part of a generating station) is completed to above the surface of the sea no later than the 31 December 2011.

Electricity generated using a specified generating capacity of offshore wind generating station (or a specified part of a generating station) of defined site and capacity which meets the following criteria should be eligible for 1.75 ROC/MWh:

- Nobody has entered into a firm contract for the delivery of wind turbines generators relating to the specified generating capacity before 1 April 2010.
- The firm contract is made for the delivery of wind turbines generators for the specified generating capacity of that generating station (or the specified part of a generating station) no later than 31 March 2011.
- A copy of that contract is sent to Ofgem, or otherwise made available for audit.
- At least one foundation for the installation of one of the turbines subject to the qualifying order in that generating station (or the specified part of a generating station) is completed to above the surface of the sea no later than 31 December 2012.

We believe that 'firm contracts' will typically involve specified delivery schedules for an identified number of turbines and schedules of payments which cannot be broken by the developer of the project without material penalty clauses. We do not believe that framework contracts or options for possible future delivery should qualify as firm contracts for the purposes set out above. There is a possibility that a contract will be unfulfilled because the turbine supplier fails. While we regard this as a low risk in the

offshore sector we will consider whether this circumstance requires specific provisions, and if so what these should be.

In order to qualify for the criteria above, we intend that turbine foundations will have to be of the type and location for which consent has been granted under s63 of the Act (or other planning consents if appropriate).

Assuming that the projects meet these eligibility criteria we intend that grandfathering principles will apply to protect investment decisions made on the information available at the time and that any reduction of support will only apply to future projects. Further details of how grandfathering will apply in an RO which is extended to at least 2037 will be set out in the statutory consultation which we expect to publish before the summer recess.

**1 May 2009**