

## National Grid ESO

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14<sup>th</sup> August 2020

### Phase 2 consultation – Early Competition Plan

On behalf of National Grid Electricity Transmission (NGET), we welcome the opportunity to respond to National Grid Electricity System Operator's (NGESO) Phase 2 consultation and be part of the stakeholder events that have been undertaken over the last few months to support the work on the Early Competition Plan (ECP). We continue to support the development of early competition in onshore transmission and think significant benefits can be realised for consumers from it.

We agree with the areas identified by NGESO to review and develop the ECP with support and insight from stakeholders from a variety of backgrounds. We are pleased to see the introduction of new concepts to help facilitate interest from a wider pool of bidders, identifying ways to reduce risks to consumers and bidders through the process. We are however concerned with some items which we think will have an impact upon the final product and ultimately the process that will be implemented:

1. *Timeline for ECP development:* the scope of work and areas covered by NGESO make it difficult to work with the challenging timeline set to populate a detailed and robust ECP. The Phase 2 consultation highlights the considerable work still needing to be undertaken. Failing to give sufficient time and effort means an impact on consumers and potential bidders due to the implementation of a sub-optimal process. This will have a long-term impact upon the types of projects likely to be tendered for, bidder appetite, increased cost and risks to consumers and the uncoordinated development of the future transmission network thus detrimentally impacting upon our Net-Zero targets.
2. *Clarity:* we need more clarity on the support actions for early competition required from incumbent Transmission Operators (ITO) so we are prepared, and we can meet the ring-fencing requirements which will allow us to participate in the competition process.

We continue to support the development of the ECP and are available to provide additional details where necessary on our response below, to ensure a robust and quality process is implemented in the future for the benefit of consumers and the network. If you have any questions on this response, please contact Sultana Begum on 0750 003 1237.

Yours sincerely,

Chris Bennett (Director, UK Regulation, National Grid)

**1. Do you agree with the types of drivers of network needs that should be within the scope of the ECP? \***

We agree with the scope of the Early Competition Plan (ECP) consultation relating to High-Voltage and Customer Connections. It is worth noting, Customer Connections which are competed, need to ensure the contractual obligations are clear so the TO can still maintain the connection date which has been agreed with the customer when they do not have accountability for delivering all work elements. Consideration also needs to be given to how customer connection dates factor in the potential for competition in the first instance.

We do not agree with the inclusion of Asset Replacement as a driver for Early Competition (EC). The proposal to include it also contradicts later statements about the limited value of competition for asset replacement. These assets are linked to the reliability of the network and we are unclear how this would be considered if it was to be included as a driver for EC.

In addition, Asset Replacement timescales seldom factor in time for consenting and major stakeholder engagement in the way that a new and high value Network Option Assessment (NOA) driven project would do. Meaning there is insufficient time to fit a two-year competition process without causing consumer detriment in the delivery programme.

It is also worth noting the uncertainty element of asset replacement projects, we reassess the health of our assets every year, new information means timing of interventions may advance or be delayed, therefore making it difficult to know what projects could be competed and aligned to the EC process. The risk could lead to assets that do not need to be replaced, to be replaced, to help facilitate competition.

The consultation also proposes to consider whether projects which are focused on improving visual impact (referred to as VIP projects) could be part of EC. We would have concerns about any approach which results in one single circuit having multiple owners (with a third party owning a short section of a longer circuit). This point also contradicts later statements in the consultation that there needs to be clear delineation between assets and clarity of accountabilities and ownership. Therefore, at this stage we do not agree that VIP projects should be within scope of the ECP.

We also seek to understand more about how a competition will be run so solutions can be optimised to meet multiple drivers where this is in the interest of consumers.

**2. Do you think a tender launched 'early' (i.e. after an indicative solution has been identified) but informed by market engagement that begins 'very early' is a suitable process? \***

We agree with the principles of launching a tender at an 'Early' stage while undertaking engagement activities at 'a Very Early' stage. We do, however, also see limitations in doing this. We have several questions which we would appreciate if Electricity System Operator (ESO) could answer before any conclusions can be made on when to launch the tender process:

**1. Indicative Solution Development**

- During the market engagement process, it is unclear how this process would deliver the optimum solution as market participants may be unwilling to share their intellectual property (IP) and thus the solution designed maybe sub-optimal. How does the ESO propose to mitigate against this challenge?

- In addition to the point above, how does the ESO propose to incentivise the incumbent Transmission Operators (ITO) or any third parties to put forward optimised solutions which may then be used by other market participants who they will compete against. If no incentives are provided, it is likely there will be limited input and thus less optimal solutions developed for tender.
- As the early market engagement will not be part of the formal tender process, how and what safeguards are proposed to be put in place to ensure credible inputs are made?
- Clarity is also sought on how an indicative solution is developed and proposed in the NOA process. Is it that the ESO envisages undertaking this role in the future or does it expect ITOs and third parties to provide these options in the way TOs do today (or a combination)?

## 2. *Network Options Assessment*

- We support the development of EC, however, the risk that the project does not go ahead is also very relevant. One of our main concern is around the uncertainty of the annual NOA process. In its current form it would detract potential participants from competing or even committing to projects when a year from now the project may not proceed. Even if participants do engage and submit a bid, this would likely be at a premium and at the detriment to consumers. In its current format the NOA process is not granular enough. Therefore, a real time process that considers works triggered by Connections & Boundary capabilities rather than bulk process would be required to facilitate the EC process.
- Currently the NOA process results in a recommendation to the ITOs who have a duty to 'develop and maintain an efficient, coordinated and economical system of electricity transmission'. The proposals place greater importance on the NOA for decisions to make commitments to developments and clarity on this is essential to all stakeholders, specifically the ITOs.
- The consultation proposes that the tender will contain information about the MW and any voltage/stability requirements. Currently the NOA process does not consider stability in detail, we therefore, welcome clarification as to how this would be made part of the existing process.
- The NOA timescales are already very constrained and it is challenging to understand how these additional steps would sit within the current process. An additional area important for consideration is that the NOA process gives a 'Proceed' recommendation at the latest point at which development of a project can begin (by using an 'Earliest In-Service Date' approach). There may be merit in a different approach to ensure that there is sufficient time for any cost-benefit analysis or tender work to be undertaken ahead of the project needing to commence. This helps to ensure there is no consumer impact of the competitive process delaying project delivery beyond the point of system need. In addition, NOA is a least worst regrets options process, consideration needs to be given to the long-term effects of terminating works as priorities and needs change, both on the contracted party and confidence around future bidders.
- Currently, options in NOA are often optimised to consider other drivers; this needs to continue and be considered when deciding if/how a project should be tendered or not.

**3. Have we identified the appropriate criteria to determine whether to compete a project? \***

We agree with assessing market appetite and undertaking a cost vs benefit analysis to determine whether a project should be competed or not. It would be helpful to understand how the potential benefits of competition would be quantified as part of the cost vs benefit process.

We do however have concerns with the following areas when considering the criteria to compete a project:

1. The removal of the minimum threshold has a significant impact:
  - on the overall financing of the ITO business as it does not have an orderbook of projects to develop and work on. This limits our ability to negotiate effective frameworks with our suppliers given the uncertainty in future requirements and may result in increased asset costs.
  - in its current proposed form, this means every project is potentially subject to competition, which will have a detrimental impact upon consumers as we have no or limited opportunity to plan, which we presume ESO will coordinate.
  - on the effectiveness and efficiencies available in assessing all projects regardless of size, consumers as a result maybe disadvantaged by competitions where the transaction costs exceed the potential benefit from competition.
2. The Certainty of Need principle should be utilised, as it can dictate the level of interest from the market. It might be; however, a subjective criterion and it is not clear how it could be used in the assessment. This can be interpreted in different ways by different people. For a criterion to be effectively used, it should be clear and objective.
3. Ofgem needs to give due consideration to the ITOs funding of pre-competition works as a result of EC. It is implied ITOs would be expected to continue to progress projects which have low certainty or where there is little interest from market participants who clearly do not see a commercial business case to deliver the project.
4. We agree with the statement: "...frequent tenders of small projects (arising from a low project value threshold) could potentially introduce many small transmission owners. We need to consider what implications this may have for the operation of the network and the ability to effectively plan the development of the transmission system." This is especially true for replacement works of existing assets. In relation to this point, one area we would highlight for consideration is how networks are coordinated during an emergency or black-start scenario, where clarity and timeliness of communications and a coordinated response are critical to the successful operation and/or restoration of the network. This becomes more challenging when the network is owned by multiple small parties.

**4. Do you agree with the approach where the ESO makes recommendations to Ofgem on the projects/needs which are suitable for competition? \***

We agree Ofgem should be the party making the final decision on whether a project should be competed or not. How Ofgem inform their decision is a matter for Ofgem, where they can call upon any number of parties to recommend, including the ESO, ITOs or any other stakeholders. Ofgem should be accountable to end consumers for making that decision and should consult with stakeholders on that decision. However, any process should be timely to ensure project delivery is not adversely impacted unnecessarily.

**5. Do you agree that the incumbent TO's should participate in competitions through the same process as other bidders, and what mitigations may be needed to allow this?**

1. We agree ITO should be able to bid into the competition process as any other market participant to ensure effective competition from potentially value adding participants. ITOs have a great amount of skills and experiences to be able to offer solutions that will bring value for consumers and we would have significant concerns if there was any attempt to prevent any ITO from participating in a competitive tender. ITOs must receive their revenues in the same way as any other participants to enable them to make an equivalent bid. Unfortunately, this has not been the case on Pathfinders and has meant the ITO is disadvantaged in that process. An example being the Mersey Reactive Power Pathfinder project:
  - a. Other participants were asked to bid in a service price for the 9-year contract period. This meant they could make commercial risk-based decisions which allow them to consider how they bid in the competition e.g. do they want to recover their costs in the 9-year term or assume a residual value/requirement beyond 9 years etc. They could also use their assets to provide other services and therefore receive multiple revenue streams for the asset.
  - b. NGET had to provide the costs for their asset as Pathfinder sets out that ITOs will be funded through the normal regulatory mechanism and paid over 45-years...but the Cost Benefit Analysis (CBA) assumed no requirement after 9 years, therefore, assumed only 9 years of benefit even though our full cost had to be included.

The ITO must also have the option not to compete if it does not wish to do so. We do not agree that the ITO should be the 'TO of last resort' for projects which are not appealing to the market. This should not be necessary if the ESO has undertaken effective market engagement prior to the competition being launched or even during it and providing a robust process is run.

2. We appreciate the concerns that market participants may potentially have of ITO involvement in the process. As such, the ESO should work with ITOs to be clear on ITO roles that support the competition process so that these can be ring-fenced from bidding activities and allow ITOs to take part in the EC process.

The areas where ITOs may be required to support the competition process are:

- a. *Initial needs identification:* The ITO will know from activities it undertakes as part of assessing the works required for customer connections and network asset health condition, whether there are multiple needs being addressed (or that could be addressed) by one solution. This ensures consumers are protected from the potential 'over-reinforcement' which could result if there is no optimisation of solutions to meet a range of drivers.
- b. *Interface definition between the competitive bid and the existing system and costing:* As per the approach with Pathfinder, the ITO will need to provide information regarding the works required to accommodate the proposed solution, the cost of those works, the timeline of those works and any other relevant impacts. The ITO may also be asked to provide information regarding availability of land or other known issues that may be appropriate for the ITO to share e.g. interacting projects at that site.

- c. *Compliance*: ITOs need to ensure that the solutions proposed do not result in any consequential safety or SQSS non-compliance and, where it does, conditions are put in place to mitigate this e.g. a connection could result in power quality issues, such as Negative Phase Sequence levels, which would breach SQSS limits.
  - d. It is also worth highlighting, the ITO will provide information to the ESO. The ESO will utilise the information as it sees fit for the competition process. The ITO does not have any influence on how this information is disseminated or used by the ESO.
3. Other points to be considered:
- a. *Draft Determination (DD)*: The recent DD for RIIO-2 implies resources for ITO activities may be subject to additional case by case re-openers and assessment by Ofgem. As well as direct timing impacts, this would also limit the scope for parallel tracking of interface design work by ITOs and other parts of the competition preparation process. This will have impacts on the lead-times for customer and net-zero projects. We welcome feedback and clarity on this point from ESO on how this will be factored and mitigated in the ECP.
  - b. *Ring-fencing of TO bidding teams from competition support activities*: Clarity on the support activities will minimise the costs and risks associated with ensuring acceptable separation.
  - c. *Use of a business separated TO affiliate company*: should remain an option for the EC process if stakeholders consider ITO activity ring-fencing to be inadequate. However, of the three ITOs only NGET can form affiliates which meet current unbundling requirements for transmission licensees. The options for meeting business separation requirements without forming a new ITO affiliate should be further considered.
  - d. *TOs licence restrictions*: each ITO is only able to operate within their licenced jurisdiction and therefore can only bid for work within their licenced area. To enhance competition, this restriction should be relaxed.

## 6. Which parties do you think would be best placed to fulfil each new role identified in the early competition model and why?

We agree with the roles identified:

1. **Procurement body**: NGESO in its system operation role (and following its separation from NGET), is best placed to undertake this activity. Ofgem's role should be to approve the projects recommended for competition by the ESO (see question 4). Regarding a third party running the process, it would need to identify and build up its capabilities if it doesn't already have it, before commencing the tender process, which could delay EC implementation.
2. **Licence provider**: This can only be awarded by Ofgem, along with making any consequential amendments to ITO licences if needed. We do however have some concerns about which party is best placed to determine if the licence is actually required or not – this has been an area of disagreement on Pathfinders as to who can advise if a licence is required as transmission assets seem to be able to connect to the transmission system and so form part of it without a licence. It is unclear at what point the owner and operator of the relevant asset becomes a TO?

3. **Approver:** As per the approval/review of projects to be competed, Ofgem should provide scrutiny and final approvals to recommendations made by the ESO. Ofgem should be accountable to end consumers for making that decision and should consult with stakeholders on its decision. This will ensure consistency across the process and accountability given to the relevant parties.
4. **Counterparties** – We agree with the proposal of Ofgem continuing with the licence provider role and the ESO for the Contracts and Payments counterparty. These roles are already well-established and do not require the introduction of a new party to undertake them. The ESO is responsible for ensuring that third parties deliver (as per their contractual obligations for non-network solutions).

**7. Do you agree with a TRS type revenue model as the default model? \* In what circumstances (if any) do you think a regulated model may be more appropriate?**

We agree that a TRS type revenue model should be the default and create an additional revenue allowance and output obligation for ITOs. Only where there are strong interactions with existing price control outputs should the bid parameters be translated to revised price control parameters.

**8. Do you think that revenue during the preliminary works period would help encourage participation in early competition? \* If so, what mechanism would be most appropriate?**

We do not think the market will accept anything other than payments being made during preliminary works.

If parties are not paid as they incur costs and take on the risks, a premium would naturally be applied if the risk is borne by the winning bidder during preliminary works (which can be both risky and costly). We do not think it is in the best interest of consumers to pay a premium and make the project more costly. It is therefore in the interest of both the winning bidder and consumers to make a payment at this stage of the process.

A fixed upfront payment with staged milestone payments is one recommendation. This ensures successful bidders know what they will receive upfront and what they can receive if they meet the required outputs at defined timings during the preliminary works as set out in their terms and conditions.

An alternative approach that is proposed by Ofgem for the Large Onshore Transmission Investments (LOTI) mechanism under RIIO-2 is the provision of pre-construction cost payments being made upfront (which could be submitted as part of the bid) and then trued-up after a defined period/milestone is achieved.

**9. Do you agree with the current preferred option of setting the duration of the revenue period to the length of the network need? \***



Fixing revenues to the duration of the need appears to be an appropriate approach. However, we do not believe the annual fluctuations between Future Energy Scenarios (FES) cycles that we have seen in recent years gives confidence in the ability of any party to accurately forecast the length of need for a project in the longer term. We would need to see that further detailed analysis has been carried out on how this would be established to determine if this is the most appropriate approach. Without this it is difficult to provide a view on whether this approach is a good one.

**10. Do you agree that the maximum length of the revenue period should be capped? \* If so, at what length?**

Design life of assets is typically based upon 45 years. There is an opportunity to align a potential cap to the asset design life. However, Transmission assets tend to be utilised longer than their design lives (as is evident in some of the assets currently operating on our network). The arrangements should not restrict the option of using an asset for longer than its original design life if that is valuable to consumers.

We would request some analysis to be undertaken to understand the rationale for capping the duration (similar to question 9 and limiting it to just the Need) as there will be a number of factors that will determine the appropriate duration which is in the interest of consumers. As potentially identified by ESO in the consultation when it refers to 'other precedents' but does not specify what these are.

**11. Do you agree with the current preferred option of including a mechanism for extending the revenue period? \* How should such a mechanism work?**

We question the need to assume a position for assets once the regime duration ends. The precedence set within Offshore Transmission Operators (OFTO) and Interconnector regimes is not to make decisions for assets/regimes now. Due to the uncertainties, it is left for when the regime ends, where more information is available. It may be the case that there are alternative regimes available in the future, the Need may have changed, more adverse/positive market conditions are prevalent, change in energy landscape are a few examples that could impact any decisions taken now.

It is also unclear what the Ownership provisions will be post the duration end date. This will likely dictate how the revenue period post the duration end date should be treated.

The future uncertainties make it difficult to be able to agree with the recommendations put forward and the precedence set by OFTOs and Interconnectors.

**12. What is the most appropriate cost assessment mechanism for fixing underlying costs after preliminary works are completed?**

The most appropriate and true form of competition is to lock the prices in where there is competitive tension. The proposed option partially does this however there will naturally be some "single source" effect by introducing a cost assessment at a later stage (i.e. Financial Close (FC)). This may lead to inappropriate benchmarks and assumptions being taken from the initial competition event which is later adjusted.



It is however important that the participant is not asked to commit to anything which undermines any consenting process as they need to be able to undertake meaningful consultation and adjust their design as a result. Fixing costs at the bidder stage would seem to be at odds with this requirement.

Consideration therefore need to be given to the following during cost assessments:

- Robust checks need to be in place to prevent a bidder from submitting an unrealistically low bid for the overheads/margins and then to recover the difference in the underlying costs prior to FC.
- New entrants or parties not familiar with developing projects of a certain type or at a location may not understand the likely costs or challenges in developing the proposed solution.
- There needs to be an appropriate level of assurance undertaken otherwise consumers will be negatively impacted where a cheaper solution was available.
- It seems risky if some decisions need making at final bid stage based on indicative costs. It is unclear how the processes ensure later adjustment to costs can be considered.

### **13. Will there be enough lender interest in a debt competition to drive competitive pricing? What other debt structuring options do you think would be appropriate?**

There is usually reasonable appetite from lenders to fund good projects, but this appetite adjusts to the prevailing economic conditions of the market at the point financing is sought, which are very difficult to predict.

We think it is important to clearly define under what terms that debt competition will be run, and what it will entail for bidders. If the intention is to remove the input of financing cost into the bidding process – as financing would be sought upon award; then a debt competition may present some challenges.

Firstly, it normally comprises a longer and more complex procurement process, as financing is sought after the project has been awarded, not in parallel with the bidding process. Secondly, as bidders don't need to underwrite financing as part of the bid presented, the process carries some degree of uncertainty on successful bidder's actual capacity to raise finance at a stage in which the project has been assigned. Finally, for the same reason, it reduces incentives for bidders to explore ways to minimise financing costs, as these may not be part of the bid - as they would be in a traditional procurement process.

An alternative would be to follow a traditional procurement process whereby each bidder will normally discuss their own financing options with their relationship portfolio and other financial advisors and will include those assumptions into the bid. In this process, optimal financing terms for each bidder will differ depending on their own economic and financial credibility.

Strong participants with solid investment propositions, good credit ratings and proven business expertise should have access to a big pool of lenders and a wide spectrum of financing options to choose from (i.e. bank loans, private and public bonds, other forms of financing) which should result in competitive financing terms. In this case, competition occurs, but at each bidder's balance sheet level.

Project Finance may be a further option. However, given the specific nature of the asset and the complexity of this form of financing, attractive terms may be difficult to achieve. Lenders may be reluctant to accept full non-recourse terms given the potentially limited secondary value of the asset and any licence restrictions regarding the use of the asset as a security for lenders.

It is also important to draw attention to the gearing levels prescribed to ITOs in the recent DDs, which may restrict financial viability and/or limit the optionality of financial instruments offered by ITOs. This would adversely impact upon incumbents and prevent the ability to offer compelling solutions which leverage their capabilities and asset management expertise. We would request this is reflected in any assessment of financing options so as not to unduly exclude or disadvantage incumbents.

Overall, it is not clear that a debt competition will be a more effective process for efficient debt pricing than the traditional procurement process described above.

**14. How should the indicative debt costs and level of gearing used in final bids be determined? How should the risk of the actual amounts be allocated?**

In a traditional procurement process, bidders will typically discuss with relationship banks and financial advisors about financing options available for the project and the tentative pricing they could achieve. This information is then used to formulate a bid. A reasonable estimation can be obtained from prevailing market data and future projections, which in normal circumstances should be a fair estimation of actual numbers that could be achieved later at FC.

Each bidder will have a different optimal gearing level at which they could minimise financing costs. However, leaving the gearing entirely at bidder discretion may result in bids that include high levels of debt funding and gearing compared to the levels in existing onshore TO businesses. This would result in higher financial risk, which could affect the deliverability or sustainability of the project in certain circumstances. For this reason, prescribing a gearing level to be used by all bidders could be appropriate to ensure that financial risk levels are not excessive.

In terms of the risk allocation mechanism to address pricing differentials between the bid stage and FC, there are several options. These include pricing deviation assumed by the bidder only or by a pre-agreed share of pain/gain with the procurement body (.i.e. consumers). A mechanism in which the bidder takes the full impact of any pricing deviation is likely one that maximises efforts for accuracy at the bidding process, as it removes any incentive to underestimate financing costs. In addition, locking in a fixed cost of capital at early stage gives bidders additional incentives to reduce financing costs at FC, as any positive differential benefit would be fully captured by them. This mechanism is, however, unlikely to deliver the lowest overall cost to consumers if interest rates remain flat or decrease in the time between bid and close.

**15. Are there any other key risk that should be addressed at this stage?**

We agree risks should sit with the party that is best placed to manage it. Below is our feedback on the risks that have been identified by the ESO and the associated party identified to manage it:

- *Change of Law to sit with the consumers*: this is outside the control of the bidder if not reasonably foreseen by the winning bidder. There is precedence in decommissioning costs on OFTOs and Interconnectors whereby higher costs due to a Change in Law is treated as a pass-through cost (where it has not been reasonably foreseen).
- *Network charged bad debt*: this risk is not relevant to competition and should be managed through the normal activities of the ESO. We are, however, unclear on whether cashflow risk (which is proposed to be moved to ITOs in RIIO-2) get shared amongst the CATOs. We would welcome clarity on this.
- *Interface risks*: we would expect ITO interface risks to be included into this list of risks, considering the number of potential competitive projects needing to be interfacing with the ITOs.
- *Change of Need*: if this sits with consumers there need to be appropriate checks and reviews undertaken on costs incurred and the efficient management of those costs before the party is held whole for all costs incurred. Should this not happen consumers may be exposed to unnecessary costs (just as ITOs must put in a claim to Ofgem and justify efficient expenditure).
- A 10% re-opener threshold on a £1bn project is significant risk to bare (£100m prior to being able to seek recourse from Ofgem). This may lead to inappropriate outcomes in bid prices.

**16. Do you consider the overall risk allocation between bidders and consumers appropriate? What are your views on risk allocation?**

See response to question 15 above.

**17. Do you have any views on the list of potential activities that could be undertaken to support bidders, the information that would be required and the potential value to consumers they could drive?**

All proposed activities identified are reasonable however the ESO need to consider the balance of additional pre-tender activities and the associated time/cost with the impact of further delay to the commencement of the project.

Addition NGET activities could be to:

- Facilitate pre-tender site visits or access to NGET owned land – we would need to consider risk assessments and who is effectively setting the parties to work and therefore potential accountability for any safety incidents.
- Network mapping information should it be needed especially for those parties that may not have the internal capabilities.

**18. What are your views on the challenge of flexing the procurement process to varying needs but maintaining standardisation?**

The desire to be flexible is correct however, more information on how this might work in practice needs to be shared in order to be able to provide an informed opinion. It is important that the procurement process is appropriate for the need identified and therefore the range of potential solutions.

**19. Do you agree that the proposed list of primary information relating to network information is adequate to identify and cost potential solutions for both network and non-network solutions? \***

The list of information that will be made available seem appropriate for the purposes of identifying and costing potential solutions. We do have comments relating to some of the items listed.

1. Land information provided by the ITO:
  - a. In instances where the ITO does have information on land, it should make available, however, there may be occasions where it is a new project or very early, whereby minimal or no information can be shared. It would be appropriate to look at other ways to retrieve this information if not available from the ITO.
  - b. There may also be instances where the ITO may be in confidential negotiations or discussions with third parties to make use of NGET land and this cannot be shared with a third-party bidder even if it has the potential to significantly impact the viability of their bid.
  - c. We do agree that land information provided by the ITO may be inaccurate or need to be maintained during the tender process. We would therefore, welcome further thoughts on how this would be practically managed.
  - d. In relation to point c, we would highlight, that the ITO should not be liable for that information and how it is used. The onus should be on the bidder to undertake necessary due diligence. We welcome clarity on what liabilities the ESO/ Ofgem would place on the ITO on handing over such information.
2. Non-licenced entities should be subject to appropriate sanctions for breach in the same way a licenced party would be. This is to allow a level playing field for both licenced and unlicensed parties in the same competition.

**20. What are your views on our current thinking for the elements that potential bidders should demonstrate at PQ?**

We agree with the elements that have been listed. We would include an addition to this list, which is the licence for network solutions.

During the PQ stage, there should be some requirement or provision in place to pre-qualify on the basis that bidders can be awarded licences should they win the bid. The early assurance (Ofgem will need to determine how they provide this), ensures the bidders are appropriately ownership unbundled and able to meet additional certification requirements should they be successful in the competition

process. This also ensures no delays in contract award and commencement of project development and delivery.

**21. Do you think that the range of criteria we are considering at ITT (stage 1) is appropriate and will drive value for consumers? \***

Several criteria have been rightly considered; however, we think there are more that need to be taken into consideration for this stage:

- *Bonds*: If requiring a Bid bond this is where it is likely to be requested (if not required at PQ stage).
- *Financial model or a TRS revenue model*: Cost assessments are expected to be undertaken at various stages of the process, providing a financial model template to bidders ensures consistency of costs submitted, assessment and input into the TRS.
- *Risks*: We think it is appropriate to consider the potential risk to network reliability, we believe consequential impacts on ITO assets (or other third-party assets) could impact the benefit of the proposed solution.
- *Incentives*: We would welcome a requirement on participants to align to environmental incentives that are placed on ITOs through the RIIO regulatory frameworks.
- *Assessment*: We believe there should be greater weighting on cost and program viability for low-value/short duration solutions which are less complex and where there can be more certainty on the viability of a much shorter program and the availability of technology to meet that need.
- *Consultation criteria*: In point (a) of the criteria section, it should read as '(a) **How well** does the proposed solution meet the specified network requirements?'. This can be beneficial to allow flexibility in solution proposals that may be short or beyond ESO requirements but with significant cost efficiencies.
- *Clarity requests*:
  - o We would welcome further information on how technology readiness would be assured by ESO as part of the tender evaluation process.
  - o How will the 'plausibility' of construction proposals be assessed by ESO given they do not have experience of delivering construction projects?

**22. Do you agree with our approach for evaluating bids at ITT (stage 2)? \***

To some extent we agree with the approach proposed but have some additional points that should be taken into consideration for this stage.

- *Replacement costs*: (the consultation states whole-life costs will be assessed, but there is no mention of replacement costs, especially if the duration is long, there would be an expectation of replacement costs to be incurred on projects. Should that be the case, it should also be captured) - power electronic/control system equipment that need replacing which may have a longer life than the primary asset, for example.
- *Interface costs*: Bidders should include any interface costs (including the cost of acquiring land from the ITO) in their bids and pay such costs should they win the competition. As well as

funding any interface works with the ITO. This ensures that the ITOs meet and discharge licence obligations to operate the network, dispose of assets and land on normal commercial terms.

- *EPC and O&M contracts*: the consultation states these contracts should be in place, however, we are unsure why this would be required at the ITT stage, particularly on long lead time projects.

### 23. Do you agree with the criteria/features we have proposed to be within the evaluation? \*

The high-level concepts seem reasonable to us, but we need real clarity and detail on how this will work in practice. For instance, indicative timeline for process? How long between ITT stages where much more detailed costs are expected?

It seems benefit of solutions is not considered a criterion at this stage. How will the ESO's process facilitate fair comparison of solutions if they provide different levels of benefit (e.g. capacity) with different costs profiles.

### 24. What are your views on our current thinking for the PB stage?

A licence heads of term would not be sufficient at the PB stage. More detail on the project, delivery risks, financial model, incentives will need to be provided, so all parties are clear on what they are licensed and contractually obligated to deliver. These being a few examples of what will be needed at the PB stage. Further clarity is sought on the following:

- How and when is it decided if the solution needs a licence?
- How would the development of the licence in parallel with the tender process work if solutions look different from different bidders?
  - o Would it potentially change the licence drafting?
  - o Is the ESO proposing Ofgem may have to progress this for ITOs/Competitively Appointed Transmission Operators (CATOs) in parallel while a decision is made?
  - o What are the envisaged timelines for this?
  - o Does it have the potential to delay contract award beyond the timescales proposed by the ESO in the consultation?

As per our experience in licence activities, drafting and agreeing licence terms is a time-consuming process and hence need to be considered early on.

### 25. What is your view on the need for a bid bond and what do you think would be an appropriate value and time period?

We are unsure whether a 'bid-bond' is the correct instrument if the ESO is expecting the bond to be placed post contract award. It is normal practice for a 'performance-bond' to be issued once a contract has been awarded and work commenced. We request the ESO review when it expects a bond to be placed - during the tender process or post-contract award. Depending on when it might be, will have

an impact upon who bids, how the contract is structured and the structure of the bond.

Moving the delivery of transmission projects from ITOs to a competitive process introduces additional risks to consumers (i.e. quality of delivery, actual delivery etc.). Even meeting the minimum financial threshold does not guarantee the bidder will not face issues later as the project progresses. Having a performance bond in place provides protection to consumers that the winning bidder will comply and deliver the project in accordance to the contract awarded. And if they cannot, the consumer is protected from non-delivery via the performance bond.

In such instances where the successful bidder is not able to deliver, we would like clarity on the ESOs expectation of what would happen to the project?

In respect to the percentage the bond should be set at. OFTOs appear to be a reasonable example and is based upon the requirements of the STC, which the successful bidder would accede to once a licence is awarded. However, it is worth noting the 20% of the capital value of construction as stated in the STC, may fall short of the true value of EC projects. The ESO need to appreciate the structures and delivery models of OFTOs, whereby the whole project is not delivered by one party (in contrast to EC, one party would develop, construct and operate the asset). We are therefore apprehensive the 20% will be sufficient for EC projects (though a higher value may deter bidders or even be reflected in the overall contract price). Under a bid bond however, the typical bond issued is between 5-10%.

We support the intention to protect consumers but would request a thorough review of placing a bond, at what stage they are appropriate to be applied and at what value.

**26. Do you agree the tender revenue stream should not commence until successful commissioning and that no payments should be made to the successful bidder prior to this point, except potentially for preliminary works and/or where there is a particularly long solution delivery works programme? \***

The TRS commencing post-commissioning is standard practice for both OFTOs and Interconnectors and aligns to project finance assessments.

Due to the nature of EC and the potential for a varying set of bidders, it would not be good practice not to pay for preliminary works. Preliminary works is where risks and costs are highly likely (due to the potential changes in design following stakeholder consultations). This may leave some bidders at greater risk of financial distress due to non-payment of work till post-commissioning. Such an impact could put the project at risk and thus consumers due to non-delivery or even delays to the program. We are not confident the market would accept not being paid during this period either.

As mentioned in question 8, an approach proposed by Ofgem for the LOTI mechanism in RIIO -2 is the provision of pre-constructions payments being made upfront (which could be submitted as part of the bid), this would then be trued-up after a defined period or when a milestone is achieved.

**27. Do you have any views on incentives or penalties in relation to preliminary works and solution delivery, including the impact of commissioning delays on the tender revenue stream / revenue period?**



Any penalties and incentives that are set should ensure the minimal disruptions to consumers and be aligned where possible to existing incentives.

We are not confident the incentives and current processes work as effectively as implied in the consultation document where there are competing priorities between ITOs/Distribution Network Operators (DNO)/OFTOs and CATOs. We are also unsure on how consequential works on ITO assets are considered and paid for. For instance, if the ITO has a Transmission Operator Connections Agreement (TOCA) in place with the ESO, and the ESO has a connection agreement in place with the customer, how are any impacts on customer connections managed with ITOs who are reliant on a third party they have no control over?

In the RIIO-T2 Draft Determinations Ofgem proposed a Large Project Delivery incentive, we would expect project delivery, and any impacts of late delivery, to be managed in a similar way as far as possible.

Further clarity is sort on the following areas from the ESO:

- What happens if late delivery results in network non-compliance?
- Who is accountable and how will this be managed, and any derogations/costs incurred as a result?
- How will out-performance be managed?

**28. Do you agree that the existing industry arrangements in respect of commissioning will be appropriate for early competition with minor adaptations? \* What adaptations do you think would be required?**

Industry arrangements should be followed as they are set for the purposes of commissioning transmission assets. We are unclear why commissioning would be different whether it's a late or an early competition project that requires a licence. The only exception where adaptations maybe required is if it's a non-network solution that is being commissioned.

**29. Do you agree with the proposed potential operational incentive regime for early competition? \* Are there any topics omitted which you feel should be Incentivised and why? \***

We do not feel adequate analysis has been undertaken on the best incentive regime to take forward. Both the Availability examples given are for offshore projects. It would be appropriate to undertake some quantitative analysis to determine the best value incentive for consumers. This is of greater importance following the comment that an asymmetrical incentive will be needed, because there are likely to be more downside risks associated with it (no analysis has been provided on this point). We therefore question why this is the preferred position if there are likely to be more downside risks and why consumers should take that risk on?

ITOs should not be penalised under 'Energy Not Served' if the failure of a CATO asset results in the loss of supply (similar to how NGET is not penalised if a DNO asset failure results in loss of supply).

**30. Do you agree that with minor adaptations the existing industry codes/processes they can incorporate both network solutions and non-network solutions arising from early competition? \* Are there any fundamental gaps or issues you foresee in relation to early competition?**

We would have expected the ESO to have undertaken the gap analysis as the developer and owner of the industry codes upon which these EC projects will have to operate. We are therefore not able to make a judgement on the question posed. We have however, set out reflections on things to be considered by the ESO to facilitate EC:

- ESO will need to ensure that ITOs and CATOs are incentivised to work together as part of the customer connection process. For instance, how would it work if a customer connects to the incumbent network or the new asset that has been delivered by the CATO? How does the ESO interact with ITOs to get the required inputs to make a customer offer?
- The NOA process needs significant changes to support EC, in its current format it is not fit for purpose.
- There will be issues when reviewing overall accountabilities for network development, whole system risk/security etc. It is paramount to make sure processes have clear lines of accountability if EC is to be successful.

**31. Do you agree that decommissioning costs should be considered as part of the tender evaluation and that there should be an obligation on the successful bidder to develop a proportionate decommissioning plan and place a form of decommissioning security at an appropriate time? \***

We agree decommissioning costs should be considered in the tender evaluation and the whole life cost of the asset. In both OFTOs and Interconnectors, costs are allocated to decommission projects at the end of its life. Any additional costs incurred above the approved allowance (prior to commissioning), the developer will need to fund. The only exception is if there is a Change in Law which requires the decommissioning to incur additional costs other than what was originally planned, is allowable as a pass-through cost. We expect the same policy to apply here too.

There have been no provisions in these two regimes for securities to be placed, we are therefore unclear as to why it would be requested for EC or a legal obligation to do so. Should a security be needed, bidders will likely price this into the contract and therefore increase the cost to consumers.