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National Grid ESO response to early competition in onshore electricity transmission networks consultation

Dear Thomas,

We welcome the opportunity to respond to your consultation on early competition in onshore electricity transmission networks.

We have developed an Early Competition Plan ("ECP"), completed in April this year, that sets out our recommendations on introducing an early competition model. This was requested by Ofgem through the RIIO-2 Sector Specific Methodology Decision. The ECP is built on the basis of invaluable feedback from a wide range of industry stakeholders and the independent challenges from the ESO Networks Stakeholder Group ("ENSG").

We are supportive of and excited about Ofgem's consultation on the development of Early Competition. We agree with the aims and believe competition can unlock consumer benefits and facilitate the achievement of net zero ambitions through enabling new, economic and innovative approaches to network development. This aligns with one of our RIIO-2 ambitions to support competition everywhere.

Our responses to the consultation questions are included in the appendix below. We have provided extensive views on early competition development in the ECP and have commented below only to provide additional thoughts, albeit still in line with our ECP positions.

Should you require further information or clarity on any of the points outlined then please contact Hannah Kirk-Wilson in the first instance at hannah.kirk-wilson@nationalgrideso.com.

Our response is not confidential.

Yours sincerely,

Matthew Wright

Head of Strategy and Regulation, National Grid ESO

Appendix - National Grid ESO response to Ofgem Early Competition consultation questions

ESO's Early Competition Plan

Q1: Do you agree that the continued development of the arrangements to allow early competition in electricity transmission represents good value for money for consumers?

We welcome Ofgem's consultation on early competition in onshore transmission networks and the positive commentary given to the early competition model we proposed in April 2021. We agree with Ofgem, that the continued development of the arrangements to allow early competition represents good value for money for consumers. Significant investment is required into the UK transmission network over the next 30 years to achieve net zero by 2050. We expect that having a range of options and methods available to ensure network capability is delivered economically represents value for consumers.

Identifying which projects are suitable for Early Competition

Q1: Do stakeholders have any views on how a very early competition could be accommodated within the network planning process without having a detrimental impact on the planning of the rest of the network, or whether there are any specific network situations where a very early competition could be run for a solution without it having a detrimental impact on the planning of the wider network?

As set out in the ECP, we believe that launching a competition early is likely to be the most practical approach. We agree that we should continue to explore the potential to compete at a very early stage if such opportunities arise. Competing very early will maximise the potential for a variety of solutions to be considered. However, there are significant challenges to running a tender process when the outcome desired is not tightly defined. There will be significantly more variability between solutions which need to be fairly assessed and accounted for. This would need to include calculating the cost of consequential investment in the wider network, as different solution types will provide different capabilities. Bidders may also struggle to tailor their bids as they will not know what is most valued.

The ESO will explore whether any of the changes to network planning being considered as part of Ofgem's Network Planning Review, such as strategic future planning, provide an opportunity for very early competitions. Further thought is needed, however, to consider whether this would be appropriate as many of the challenges of very early competition are likely to remain.

Q2: Do you agree with our assessment of the ESO's proposed process for defining the technical scope of a tender under an early competition?

We agree with Ofgem's views. In particular, we agree it is important to consider the application of competition to projects that do not flow through the Network Options Assessment (NOA) process. We are currently developing processes for how both connections enabling works and asset replacement works might be identified for competition and what additional factors might need to be considered. For example, for connection enabling works, it is important not to delay customers' connections.

We also agree that we need to continue to develop our planning process as the industry evolves, in order to ensure all types of solutions can be incorporated wherever appropriate.

Q3: Do you agree with our assessment of the ESO's proposed criteria for early competition? Specifically, do you have any views on whether:

- **there is a need for a 'high value' criterion?**

Competition experience in the US suggests there could be potential benefit gained through competing lower value projects. Also, our NOA pathfinders undertake a form of early competition, including tenders for low value projects (e.g.~£20m). The pathfinders suggest that there could be benefit from tendering low value projects. However, it is important that the procurement process used is appropriate to the scale of the project so that the costs of competing do not outweigh the benefits that can be gained.

In the ECP, we propose that an individual project Cost-Benefit Analysis (CBA) process could be used to assess whether the benefit gained from competing is likely to outweigh the costs. This CBA approach could ultimately reveal a natural value threshold at which benefit is unlikely to be gained for particular types of projects. This CBA approach also enables other factors, such as the potentially significant impact of constraint costs if delivery is delayed, to also be considered in deciding whether to compete.

- **'new' and 'separable' are necessary or appropriate as specific criteria for identifying projects for early competition?**

In regard to the 'new' criteria, we believe that the same arguments that were considered for late competition also apply for early competition. We therefore believe these criteria should be applied consistently across both early and late competition. Similarly, we believe that the same thinking as for late competition also applies to the need for 'separability' in terms of clear delineation of ownership and accountability.

We also consider it is important to consider whether separable transmission asset solutions are plausible as part of considering suitability for competition as this will affect whether value can be gained.

We agree, however, that for early competition, this should consider whether alternative separable solutions are plausible, rather than whether the indicative solution is separable. In particular, non-network solutions may offer separable options. However, it will be important to consider in each case whether such solutions provide for a sufficiently competitive market. We are currently developing thinking on how the criteria could be applied in practice and will work with Ofgem to consider how best separability might be reflected, including whether the impact on the competitiveness of the market could be factored into the CBA.

Roles and Responsibilities within Early Competition

Q1: Do you have any material concerns about the ESO's expertise, incentives, or independence, should they be appointed to carry-out the Procurement Body role for early competitions?

In the ECP we have explored the role of the Procurement Body and the risks and obligations associated with this role. We believe that the delivery of the unique and untested model of early competition, and the resulting benefits to the end consumer, presents inherent risks to whichever entity takes on these activities.

We believe that we are best suited to take up the role of the Procurement Body due to the efficiencies with aligning it with other ESO roles in the tender process and our strategic ambitions of facilitating competition in the interest of consumers. Further thinking and development is required to fully understand how to address the risks and challenges created by this role.

The legal separation of the ESO from National Grid Group, has successfully delivered a framework that recognises the uniqueness of the ESO as an asset-light, service focused business, and has enabled the

organisation to prioritise wider system and consumer interests in its decision making. However, as our roles in the industry evolve and expand, through the future system operator review, we recognise that it is the right time to consider a further change to our ownership model. We understand the need to create an increased level of independence from other energy interests, and to prevent perceived or potential conflicts of interest from these new roles.

Q2: Do you agree with Ofgem's proposed roles?

We agree with Ofgem's proposed roles. We believe Ofgem is the most suitable party to take on the approver role and approve the outcome of competitions resulting in either network or non-network solutions. They are also the only body capable of issuing transmission licences. Our stakeholders, through our early competition stakeholder engagement, agreed with Ofgem being the most appropriate party to take on the approver role and that they should approve the procurement outcome. Further thought is required on how Ofgem's roles, and the detail of tender decision-making, impact on the Procurement Body's liabilities. Should the ESO be appointed as Procurement Body this would then need consideration in the context of amending the risk profile of the ESO, which will play a key part in implementing early competition effectively.

Q3: Who should undertake the network planning body role? What role should TOs play in network planning?

We see this consultation as a unique opportunity to step back and consider how energy system planning and governance needs to change to meet the enormous challenge of decarbonisation we are facing as a society.

We believe we have an important role to play in network planning. This includes ensuring that all different types of solutions and options are considered in the network planning process. As network owners, the incumbent Transmission Owners (TOs) are integral stakeholders in network planning. As a minimum, we should have a role to scrutinise and challenge the options put forward, alongside considering alternative options. Ofgem's Network Planning Review and the Ofgem and BEIS Future System Operator review consultation also consider network planning roles and responsibilities. This should include consideration of whether there is a need for broader changes to network planning roles and responsibilities, including potentially a stronger role for the ESO in developing a strategic plan.

Q4: What are your views on the proposed conflict mitigation arrangements for TO roles? What might be an appropriate level of challenge from the ESO on solutions put forward by TOs as part of their network planning role?

If TOs are to be involved in providing solutions for competitions, we believe that appropriate conflict mitigation arrangements for TOs are required in order to provide bidders with sufficient confidence that the tender process will be fair. We believe there should be alignment to late model competition arrangements wherever possible and consider the conflict mitigation arrangements developed for late competition, following industry consultation, should be broadly appropriate for early competition.

We believe the ESO should challenge TOs on the costs and timeframes of their solutions. We should also be able to propose alternative build and non-network solutions, incorporating third party options where appropriate.

Q5: Do you agree with our views on the TO counterfactual approach?

We agree. We believe that the most fair, transparent, and efficient way to compare bids and maximise competitive tension is by allowing TOs to participate through the same process as other bidders.

Tender process and commercial model

Q1: Do you have any material concerns with the commercial model proposed by the ESO?

We do not have material concerns with the commercial model or tender process we have proposed in our ECP. We acknowledge that there are still risks and challenges to be worked through on these proposals. If implemented, we would continue to refine and develop our thinking further in collaboration with stakeholders to address any of these challenges.

Q2: Do you have any material concerns with the tender process proposed by the ESO?

See above.