

Ofgem
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28 July 2021

Interconnector policy review: Working Paper 4 – Multiple-purpose Interconnectors

Dear IC Policy Review Team,

Thank you for giving us the opportunity to provide comments on the WS4 consultation.

Etchea Energy Partners is an independent firm providing management and consulting services to clients operating in the energy sector including interconnector projects.

Question 1: Do you agree with the approach we have taken to workstream 4?

We broadly agree with the approach adopted by Ofgem to WS4.

Question 2: Do you think we have missed any important benefit that MPIs could deliver?

We expect Ofgem to appraise MPIs with a detailed cost benefit analysis to assess consumer benefit and we agree with Ofgem's comments "*At a high level, this means we see value in potential future needs case assessments drawing on both socio-economic modelling and assessment of wider impacts*". This approach is supported through an MPI's contribution to Government's decarbonisation objectives emphasised in its recent policy papers and consultation:

- i. *Ten Point Plan for a Green Industrial Revolution (November 2020)*. The Government's plan identifies objectives to achieve a net zero economy by 2050. Points 1 and 10

identify areas where MPIs can contribute directly or enhance the benefits of connected projects:

- Point I: Advancing Offshore Wind to “transform our energy system, building more network infrastructure and utilising smart technologies like energy storage”.
 - Point 10: Green Finance and Innovation details the commitment to innovation funding of "energy storage and flexibility".
- ii. *The Impact of Interconnectors on Decarbonisation (December 2020)*. BEIS published a report on the impact of interconnectors on decarbonisation alongside the White Paper, which states that a higher level of interconnector capacity could decrease cumulative emissions in Great Britain by up to 199 MtCO₂ by 2050, as well as reducing total system costs.
- iii. *Enabling a high renewable, net zero electricity system: Call for evidence (December 2020)*: BEIS’ consultation addressed the deployment of new low carbon generating infrastructure on the Government’s target of net zero greenhouse gas emissions by 2050. The focus on the consultation was primarily on CfDs as an alternative support mechanism. Questions 18 and 19 considered the role that international renewable projects could play and whether there are benefits to supporting these projects with Government schemes “given projects overseas could have different patterns of intermittency or different availability of baseload or dispatchable renewable resource.”

Question 3: Do you agree with our views on the conclusions of the ITPR?

We agree with Ofgem’s view that “to get new asset types off the ground developers and their investors require regulatory clarity and certainty”. However, we have further questions on Ofgem’s proposal “to shift towards a more system-wide and coordinated approach to identifying new MPI projects”. This would mark a large shift in policy away from the developer-led approach to date. Stakeholders would need to see a detailed scope of the ESO’s role going forward to fully understand that the role is commensurate with its resources. The ESO appears well placed to assist in the coordination of assets once built but may be less adept at identifying cross border projects.

We have the following reservations/comments regarding a centralised decision-making process.

- The ESO’s input may be better achieved through its proactive participation in Ofgem’s project consultation process. The decision to invest in ITPR requires input from a large group of stakeholders with a broad skill set including cross border expertise and raising capital to finance projects.
- NGESO’s and Ofgem’s perspective for the need for additional interconnection/MPIs is necessarily seen through a GB lens, however, this is only half the story. Developers are often better placed to assess the need for a specific project after analysing a broad set of project criteria and following detailed discussions with stakeholders in the connecting countries.

- Interconnection is one of National Grid's unregulated businesses. While NGENSO is separate from National Grid Ventures, it retains a common shareholder and geographical location. Until there is full legal separation, developers and consumers will be naturally cautious of potential conflicts that could arise between NGENSO and National Grid Ventures.

Question 4: Do you agree with our proposal to further explore the applicability of the cap and floor regime for the MPI projects currently under consideration? Please provide supporting information if available.

We broadly agree with the approach adopted by Ofgem to explore the applicability of C&F for MPI projects.

Question 5: Do you agree with our proposal to also consider alternative regulatory models for MPI projects in the long term? What models should we consider? Please provide supporting information if available.

Ofgem's discussion in section 3 of the consultation document highlights the complexity of finding a single model for MPI Projects despite the potential benefits such projects bring.

We believe Ofgem should maintain a flexible approach and consider a range of regulatory models in addition to C&F. ITPR dates back to 2012 but has seen few projects emerge given the difficulties of creating a favourable regulatory backdrop. Ofgem could consider project assessment on a case-by-case basis including a request from project sponsors to propose a regulatory model that would allow the projects to advance.

For example, Integrated generation/transmission projects ("Integrated Projects") could consider obtaining a CfD as a single support mechanism assuming BEIS would regulate the whole project. A single support mechanism would require a single authority to review all aspects of the project and take a consolidated review of the project risks. A single support mechanism avoids potential friction between two regulatory regimes and may be adjusted for a more tailored solution to address specific project challenges and ensure the project gets financed and built.

The regulation of an MPI should contain sufficient flexibility to incentivise project lenders to permit further development of a project where it is in the interest of consumers and Government. For example, the split of a point-to-point Integrated Project to a multipoint interconnector and generation project may require the alteration of financing arrangements. Project lenders will require protection that existing loans will continue to benefit from the same quality of operating cashflows.

As an alternative, a hybrid regulatory model could be developed with a CfD for the generation assets and C&F for the interconnector system. The cumulative support and management of the two schemes should be adequate to attract financing while maintaining the regulatory separation between transmission and generation. Such a model could prove to be cumbersome for developers and regulators alike unless the administration of the CfD and C&F is undertaken by the same authority. However, this may enable the more rapid

development of generation under the CfD mechanism, with C&F agreements being agreed at a later date.

Question 6: What other wider policy issues or aspects related to MPIs should we be aware of?

The focus of the WS4 consultation is generally on local MPIs integrating nearby renewable energy resources. We provide some comments on the emergence of several integrated projects with cable lengths of over 1,000km which seek to integrate significant wind and solar resources with regions of high demand (“Integrated Projects”). Examples include Sun Cable (Australia-Singapore¹), Gulf Interconnector (India-Gulf States²) and Xlinks (GB-Morocco³). These projects skirt the length of entire continents. This creates significant optionality for future developments, including connections with floating offshore wind farms and lateral connections to power transmission systems along its route.

These projects are likely to impact wider policy issues including:

- *Unbundling requirements:*

Some Integrated Projects are being developed on a point-to-point basis with limited capacity for third parties’ users over and above the project’s integrated generation capacity or where there are limited entry points into the HVDC system. In these cases, the requirement for unbundling is expected to stifle the development of the overall project or the costs of unbundling render the project uneconomic. A case-by-case approach to unbundling may be required to ensure the delivery of projects.

- *Regulated revenues:*

Regulated revenues streams form the basis of project lending. Lenders to large Integrated Projects will want to ensure that the revenues on which loan documentation is based cannot be diluted in quantum, tenor, and credit quality. Project lenders will not advocate creating an environment that allows the interaction between different regulated revenue streams that would reduce credit quality.

- *Anticipatory investments (AI):*

Most Integrated Projects primary objective is to get the end-to-end system built. AI will be considered for a future period and will need to be structured so that there is adequate incentive for project promoters to consider further development of the system for the benefit of consumers and Governments’ objectives as well as protecting existing capital providers.

Question 7: Do you agree with our initial conclusions? If not, please concisely explain why and provide supporting information if available.

We broadly agree with the Ofgem’s initial conclusions caveated by our response to Question 3 above.

¹ <https://suncable.sg/>

² <https://www.sterlitepower.com/blog/achieving-power-all-intercontinental-power-grids>

³ <https://xlinks.co/>

Question 8: Do you agree with our initial proposals? If not, please concisely explain why and provide supporting information if available.

We broadly agree with the Ofgem's initial proposals.

We are available to discuss any of the responses in this letter.

Sincerely

Simon Ludlam