

FAO: Susanna Onyemauwa

By email: Cap.Floor@ofgem.gov.uk

31 March 2023

Dear Susanna,

Project delivery delays as part of the timelines and incentives framework applied to the Third Window

Transmission Investment (TI), as one of the UK's leading independent transmission companies, manages one of the largest offshore electricity transmission portfolios. We have successfully participated in the NG ESO Pathfinder programme, securing contracts to provide stability services at four sites in the two recent stability tenders.

TI is developing two GB interconnector projects: one from the First Window where the mechanisms for relief from delays is limited to pre-Operational Force Majeure following implementation of the Special Licence Conditions; and one in the Third Window which would benefit from the proposed additional Reasonable Delay Event mechanism, which allows for a broad range of delays to be considered, not limited by requirement such as being outside of reasonable control of the project.

We support Ofgem's policy of seeking to better protect projects from delays which are outside of their reasonable control, recognising that in previous Windows the mechanisms for seeking relief from delay were more limited to how they could be applied. We would encourage Ofgem to apply these proposed conditions, or reflect the intent, to all interconnectors that are yet to reach the Final Project Assessment stage (regardless of Window), levelling the playing field across all current competing projects - noting Ofgem's previous reassurances to the industry that the events listed in the text of the Force Majeure clause was not intended to be prescriptive¹.

We are supportive of the proposed additional delay mechanisms, subject to: clarification of how Ofgem intends the mechanisms to be used; how accumulation of approved delays will be treated; and confirming there will be consistency of the consequences for a project irrespective of the delay mechanism used.

We support the change in the incentive approach which preserves the full 25-year duration of the regime to support the long-term, low-cost financing of these projects. However, to comment fully, more detail is required on the Post Regime arrangements, including how flexible these can be against scenarios where the Floor could be too low to support operations and how the payback mechanism aligns with the Retained Electricity Regulations use of revenue provisions.

¹ "We would also reiterate that whilst the proposed definition contains a suite of events that could constitute a force majeure, the events listed are not exhaustive and the proposed definition of Pre-operational Force Majeure can also accommodate other events that are not expressly included – so long as such events can be demonstrated by the licensee to have been beyond its reasonable control." Ofgem: Decision on pre-operational force majeure arrangements, 08 June 2021, Appendix 5

We do not support the policy where projects carry the impact of unapproved delays for the duration of the regime. We believe the policy should include opportunities for projects to reduce the length of the Exposure Period where they deliver additional or accelerated benefits to consumers, for example, providing early rebates of revenues above the Cap, or increased capacity availability.

With the consultation lacking detail in how the Reasonable Delay Event mechanism, the Payback Mechanism and Post Regime period will work, this may be Ofgem's intent. This would leave the details to be agreed on a case-by-case basis, either at the point of assessment of the delay (noting this is some 25 years ahead of the Exposure, Payback and Post Regime) or allowing some details to be determined closer to the end of the regime, i.e. if a payback is actually required.

We expand on the above main points in our response to the specific questions in the attachment to this letter. We have also appended our response to the Statutory Consultation on the licence amendments, which should be read in conjunction with this response.

We hope the contents are helpful and we would be pleased to discuss any of the points raised.

Yours faithfully,

A handwritten signature in blue ink, appearing to read 'Mark', with a long, sweeping horizontal line extending to the right.

Mark Fitch
Corporate Development and Regulation Manager

ATTACHMENT – SPECIFIC QUESTIONS

Chapter 2: Minded-to Decision on our Timelines and Incentives Changes, including the Payback Mechanism for Delays (Third Window)

Q1: Do you agree with the proposals of the modified Regime Start Date and modified Backstop Date concepts as part of the Timelines and Incentives changes to the Third Cap and Floor Window for Interconnectors?

Yes.

Q2: Do you believe that there are any improvements that could be made to the development of the modified Regime Start Date and modified Backstop Date concepts?

No.

Q3: Do you agree with the proposal to implement a Payback Mechanism for Delays as a proportionate incentive to encourage developers to deliver projects on time and protect consumers from the impacts of delays?

Yes, we recognise that the Payback Mechanism for delays provides an incentive for projects to deliver on time for events within their control. The payback mechanism is a preferable arrangement compared to shortening the duration of the Cap and Floor regime.

Q4: Do you believe that there are any improvements that could be made to the development of the Payback Mechanism for Delays?

There is currently a lack of detail (in this consultation and the associated Statutory Licence consultation) to provide a comprehensive view of the impact of the Payback Mechanism. We outline below some features of the policy where further detail is needed to be able to provide a more comprehensive response.

As part of the regime Ofgem has outlined within the incentive arrangements, a concept of “Post Regime Period”, where the previously set Floor revenue level is maintained. Where income is under that Floor level, payback payments would not be required, with equity distributions also prohibited. The consultation does not outline how this would be implemented, or whether these would be the only features of the regime that would be extended. While the lack of detail prevents a comprehensive response it does raise a number of questions, including:

- How do the Payback Mechanism payments fit within the permitted revenue use categories within the Retained Electricity Regulation?
- Would the Post Regime arrangements allow flexibility so that the Floor level can be reset for the post-regime duration, where necessary to avoid triggering the payback payments, where they would push the business into financial distress? (noting Footnote 5 in the Annex 2 - Minded-to Policy associated with the Statutory consultation states flexibility for the licensee to choose how to set the repayments, which not clear within this consultation)
- How is the Payback mechanism being designed to minimise the risk of negatively impacting the projects, e.g. due to timing differences or the accounting treatment of the top-up receipts and subsequent repayments?

It may be simpler to seek to implement a straight-forward 'lock-up' mechanism preventing distributions to equity until the specific conditions are met, eliminating the need to monitor and regulate the revenues against a Floor level set decades earlier.

We think the incentive arrangements could be improved to deliver enhanced benefits for consumers. Instead of requiring the project to carry the penalty for unapproved delays for over two decades through the regime duration. We believe the consumer would be better served if projects were incentivised to reduce the length of the Exposure Period by taking actions that deliver earlier or additional benefits to consumers, for example, where the project returns above Cap revenues early, such that consumers receive accelerated benefits or increased capacity availability.

Chapter 3 - Minded-to Policy Decision on our Reasonable Delay Event Mechanism Questions

Q1: Do you agree with the proposal to implement a Reasonable Delay Event mechanism as a means of assessing and managing delays in early project development?

Yes, we support the introduction of the Reasonable Delay Event Mechanism, on the assumption that it broadens the scope of delays that will be considered by Ofgem. Specifically, this should allow delays resulting from the action or inaction of other electricity transmission licensees that is explicitly excluded from Pre-Operational Force Majeure, but is outside of the project's control.

Q2: Do you believe that there are any improvements that could be made to the development of the Reasonable Delay Event?

While Ofgem does not expect projects to seek relief from delays simultaneously, ("in tandem"), the policy consultation and proposed licence drafting (in the accompanying Statutory Consultation) would allow projects to seek relief through both mechanisms, but not to use them concurrently.

Therefore, we are supportive of the new delay mechanism assuming they are useable, as follows:

- simultaneously pursuing a Reasonable Delay Event and Pre-Operational Force Majeure mechanisms for different delay events, noting each should be submitted at a reasonable time following the event;
- sequentially using one mechanism then the other, e.g. if an event is rejected under the Reasonable Delay Event mechanism, it would be possible (if qualifying) to later seek approval for Pre-Operational Force Majeure (e.g. where additional information becomes available); and
- sequentially for different delay events, such that they are approved in a reasonable timeframe after they occur, with the overall delay accumulating over time.

An accumulation of approved Reasonable Delay events may see a situation where the Regime Start Date is pushed beyond the Backstop. Ofgem's policy appears to suggest in that case, the final RDE causing the project to exceed the Backstop date would trigger the Payback Mechanism and an Exposure period relating only to the last RDE. However, if that last event were a Pre-Operational Force Majeure event, it would not trigger the Payback Mechanism. The effect on the consumer is identical, however, the impact on the project is very different. Equally, if there were one Pre-Operational Force Majeure and an RDE, would the trigger for exceeding the Backstop be regarded as the final event (which could be an RDE) or already approved Pre-Operational Force Majeure event?

In the case of an RDE pushing the project beyond the Backstop Date, it would be right to reassess the needs case, but, on approval of the delay, appears illogical to apply the Payback Mechanism simply because of the choice of regulatory mechanism assessing the event.

There should be no different outcome for the same sets of events simply due to the timing or choice of regulatory process through which the delay relief is sought. We would therefore propose that through whichever mechanism the delay is approved, it avoids the payback mechanism, whether it is within or beyond the backstop.