

# Consultation

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## Consultation on policy updates to Early Competition in onshore electricity transmission networks

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We are consulting on our latest thinking on several important policy points relating to the development of Early Competition for the delivery of key electricity transmission projects. This includes elements that we referenced for further consideration in our March 2022 decision on Early Competition. We also give our views on the National Grid ESO's proposed amendments to the Early Competition model in its recently published Early Competition Implementation Update. We welcome views from people with an interest in the development of electricity network solutions, technical and commercial innovation, and competing for the design, construction and operation of solutions to solve network problems. The consultation closes on 20/03/2024. We particularly welcome responses from potential bidders in the Early Competition processes and network companies. We would also welcome responses from other stakeholders and the public.

This document outlines the scope, purpose and questions of the consultation and how you can get involved. Once the consultation is closed, we will consider all responses. We want to be transparent in our consultations. We will publish the non-confidential responses we receive alongside a decision on next steps on our website at [ofgem.gov.uk/consultations](https://www.ofgem.gov.uk/consultations). If you want your response – in whole or in part – to be considered confidential, please tell us in your response and explain why. Please clearly mark the parts of your response that you consider to be confidential, and if possible, put the confidential material in separate appendices to your response.

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## Executive Summary

### Background and context

Competition has an important role to play in driving innovative solutions and efficient delivery that can help us meet our decarbonisation targets at the lowest overall cost to consumers. Early Competition refers to a competition to determine a solution to a need on the network that is run before detailed design of the preferred solution has been carried out. By introducing competition into the detailed design of the relevant projects, consumers should benefit from additional innovation and cost efficiencies in the delivery of critical electricity transmission investment projects.

In April 2021, the National Grid Electricity System Operator (**ESO**) published its Early Competition Plan (**ECP**),<sup>1</sup> and in March 2022 we published our decision to continue the development of an Early Competition model (March 2022 decision).<sup>2</sup> Our March 2022 decision sets out the roles and responsibilities of the ESO, Ofgem and the Transmission Owners (**TOs**), confirming Ofgem as the Approver (responsible for ensuring that the project advancing to Early Competition is, and remains, in the interest of consumers) and Licence Counterparty (awarding and managing any licence awarded to a successful bidder).

Our March 2022 decision also identified areas where further policy development was required before we could reach a decision. These included the cost benefit analysis (**CBA**) methodology to identify suitable projects for competition, conflict mitigation arrangements to ensure the TOs receive no unfair advantage through their tender support role and options for circumstances of CATO failure.

In February 2024, the ESO published its Early Competition Implementation - Update (**EC-I Update**).<sup>3</sup> This consultation summarises our views on the changes in the ECP as proposed in the EC-I Update, as well as our latest thinking on various important

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<sup>1</sup>ESO's Early Competition Plan (ECP), sets out a plan for introducing early competition into the onshore electricity transmission network April 2021. Further information is available here, ESO final Early Competition Plan, April 2021; <https://www.nationalgrideso.com/document/191251/download>

<sup>2</sup> March 2022 decision: Ofgem decision on Early Competition, summarises our decisions on various elements of the early competition regime in onshore transmission networks March 2022 [Decision on early competition in onshore electricity transmission networks | Ofgem](https://www.ofgem.gov.uk/consult/condocs/earlycomp/earlycomp1222/earlycomp1222.pdf)

<sup>3</sup> EC-I Update, Early Competition Implementation Update by ESO setting out further developments in their Early Competition Plan (ECP) published in February 2024 <https://www.nationalgrideso.com/document/301786/download>

supporting policy points that we referenced we would consider further in our March 2022 decision on Early Competition.

## **What this consultation covers**

This consultation sets out our views/proposals regarding the following important areas:

### **Amendments to the Early Competition model proposed by the ESO under its EC-I Update**

The ESO has proposed key adjustments to the Early Competition model previously developed under its ECP. Specifically, it proposes that the tender is specified in additional detail based on the output of the transitional Centralised Strategic Network Plan (tCSNP/CSNP)<sup>4</sup> and Strategic Spatial Energy Plan (SSEP) that have been further developed since our 2022 decision. We agree with the ESO that this will provide more certainty to bidders, local stakeholders and will allow an easier comparison of bids. We also agree that the resulting removal of the TOs' role in bid assessment should increase bidder appetite to participate. The amended model will remove the scope for non-network and network solutions to directly compete in Early Competitions. As such, we are keen to understand stakeholders' views, including non-network solution providers.

### **CBA model used to identify suitable projects for Early Competition**

We consider that the ESO's proposed CBA methodology is suitable for determining the appropriate projects to target for Early Competition. When reaching our decision on relevant projects identified in the 2024 tCSNP, we will also work with the ESO to consider any additional qualitative considerations outside of the CBA methodology that are particularly relevant to the projects in question.

### **TOs conflict mitigation in supporting Early Competition tender process**

To address potential and perceived conflicts identified in our 2022 decision, we propose that TOs are obliged through their licence to act fairly and transparently in supporting the tender process. We propose that TOs be required to submit a conflict mitigation methodology statement for Ofgem approval ahead of a tender to be able to bid. We expect the conflict mitigation statement to cover the separation of the bidding unit and the associated management structures, as well as the separation of costs, assets and financing of the project subject to the tender process. It would also cover limits on the

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<sup>4</sup> The aim of the CSNP is to provide an independent, coordinated, and longer-term approach to wider network planning in GB to help meet the government's net zero ambitions. [Decision on the framework for the Future System Operator's Centralised Strategic Network Plan \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/consultation/decision-on-the-framework-for-the-future-system-operator-s-centralised-strategic-network-plan)

transfer of TO staff with knowledge of relevant projects through the CSNP process to the TO bidding unit, with additional obligations around sharing of confidential and potentially sensitive information through tender process activities.

### **TNUoS under/over recovery for CATOs**

We propose that it is not in consumer interests to expose CATOs to TNUoS over and under recovery like the incumbent TOs.<sup>5</sup> Such revenue uncertainty for the expected financing structures of the CATOs would otherwise likely lead to increased costs to consumers.

### **Dealing with CATO/tender failure**

Alongside proposals for avoiding reaching the point of a tender failure, our consultation sets out the range of regulatory approaches available in the case of a CATO failure for any reason during the project's lifecycle. Depending on the circumstances at timing of any failure, we may consider re-tendering, funding TOs to carry out works under RIIO arrangements and the transfer of assets via a CATO of Last Resort process.

### **Next Steps**

Following consideration of responses to this consultation, we expect to reach our decision on the policy areas covered by this consultation by early summer. We will separately consult on the ESO's proposed commercial model and the tender regulations we are developing in support of the Early Competition implementation.

Following the publication of the tCSNP by the ESO in March 2024, we aim to identify at least one project as being suitable for Early Competition by the end of 2024.

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<sup>5</sup> An existing TO winning an Early Competition tender would also be treated as a CATO

## **1. Introduction**

### **Section summary**

Chapter 1 provides an overview of this consultation and lists related publications.

### **What are we consulting on?**

1.1 We are consulting on our latest thinking and proposals on several important supporting policy points that further support our March 2022 decision on Early Competition. This document also summarises our views on the ESO's proposed changes to the Early Competition model in its recently published EC-I Update.

### **Section 2: Early Competition context and overview**

1.2 Chapter 2 provides background on what Early Competition means, progress since our March 2022 decision on the development of an Early Competition model and what this consultation covers.

### **Section 3: ESO's proposed amendments to Early Competition Plan in the EC-I Update**

1.3 Chapter 3 explains the amendments to Early Competition model proposed by the ESO in its recently published EC-I Update.

### **Section 4: Conflict mitigation**

1.4 Chapter 4 summarises the ESO proposals and our initial proposals on arrangements to mitigate conflicts of interest during the tender process.

### **Section 5: Cost benefit analysis (CBA)**

1.5 Chapter 5 summarises the ESO proposals and our views on the CBA methodology developed by the ESO to advance projects for Early Competition.

### **Section 6: Transmission network use of system (TNUoS) revenue over/under recovery**

1.6 Chapter 6 explains our proposal for the TNUoS revenue recovery for Competitively Appointed Transmission Owners (CATOs) under the Early Competition model.

### **Section 7: Options for dealing with CATO failure**



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1.7 Chapter 7 explains our proposed range of options for dealing with CATO/tender failure and the conditions necessary for appointment of CATO of last resort under the requisite circumstances.

## Context and related publications

ESO Early Competition Implementation – Update: Onshore Electricity Transmission Networks (February 2024): [Early competition | ESO \(nationalgrideso.com\)](#)

Ofgem Update on Development of Competition in Onshore Electricity Transmission (December 2023): [Early Competition Onshore Transmission Update \(ofgem.gov.uk\)](#)

Ofgem Decision on the Framework for the Future System Operator’s Centralised Strategic Network Plan (December 2023): [Decision on the framework for the Future System Operator’s Centralised Strategic Network Plan \(ofgem.gov.uk\)](#)

DESNZ Transmission Acceleration Action Plan (November 2023): [Transmission Acceleration Action Plan: Government response to the Electricity Networks Commissioner’s report on accelerating electricity transmission network build \(publishing.service.gov.uk\)](#)

Energy Act 2023 (October 2023): [Energy Act 2023 \(legislation.gov.uk\)](#)

Report from Electricity Networks Commissioner Nick Winser CBE (August 2023): [Accelerating electricity transmission network deployment: Electricity Networks Commissioner’s recommendations - GOV.UK \(www.gov.uk\)](#)

Ofgem Decision on the Development of Early Competition in Onshore Electricity Transmission Networks (March 2022): [Decision on early competition in onshore electricity transmission networks | Ofgem](#)

ESO Early Competition Plan – Onshore Transmission (April 2021): [download \(nationalgrideso.com\)](#)

## Consultation stages

**Figure 1: Consultation stages**

<b>Stage 1</b>	<b>Stage 2</b>	<b>Stage 3</b>	<b>Stage 4</b>
Consultation open	Consultation closes (awaiting decision). Deadline for responses	Responses reviewed and published	Consultation decision/policy statement
<b>21/02/2024</b>	<b>20/03/2024</b>	<b>March/April 2024</b>	<b>May/June 2024</b>

## How to respond

1.8. We want to hear from anyone interested in this consultation. Please send your response to the person or team named on this document's front page.

1.9. We've asked for your feedback in each of the questions throughout. Please respond to each one as fully as you can.

1.10. We will publish non-confidential responses on our website at [www.ofgem.gov.uk/consultations](http://www.ofgem.gov.uk/consultations).

## Your response, data and confidentiality

1.10. You can ask us to keep your response, or parts of your response, confidential. We'll respect this, subject to obligations to disclose information, for example, under the Freedom of Information Act 2000, the Environmental Information Regulations 2004, statutory directions, court orders, government regulations or where you give us explicit permission to disclose. If you do want us to keep your response confidential, please clearly mark this on your response and explain why.

1.11. If you wish us to keep part of your response confidential, please clearly mark those parts of your response that you do wish to be kept confidential and those that you do not wish to be kept confidential. Please put the confidential material in a separate appendix to your response. If necessary, we'll get in touch with you to discuss which parts of the information in your response should be kept confidential, and which can be published. We might ask for reasons why.

1.12. If the information you give in your response contains personal data under the General Data Protection Regulation (Regulation (EU) 2016/679) as retained in domestic law following the UK's withdrawal from the European Union (UK GDPR), the Gas and Electricity Markets Authority will be the data controller for the purposes of UK GDPR. Ofgem uses the information in responses in performing its statutory functions and in accordance with section 105 of the Utilities Act 2000. Please refer to our Privacy Notice on consultations, see Appendix 3.

1.13. If you wish to respond confidentially, we'll keep your response itself confidential, but we will publish the number (but not the names) of confidential responses we receive. We won't link responses to respondents if we publish a summary of responses, and we will evaluate each response on its own merits without undermining your right to confidentiality.

## General feedback

1.14. We believe that consultation is at the heart of good policy development. We welcome any comments about how we've run this consultation. We'd also like to get your answers to these questions:

1.1.1. Do you have any comments about the overall process of this consultation?

1.1.2. Do you have any comments about its tone and content?

1.1.3. Was it easy to read and understand? Or could it have been better written?

1.1.4. Were its conclusions balanced?

1.1.5. Did it make reasoned recommendations for improvement?

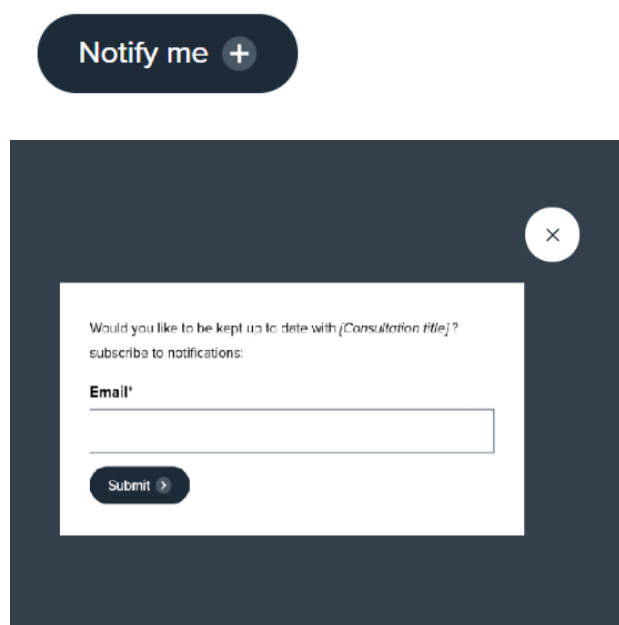
1.1.6. Any further comments?

Please send any general feedback comments to [stakeholders@ofgem.gov.uk](mailto:stakeholders@ofgem.gov.uk)

## How to track the progress of the consultation

You can track the progress of a consultation from 'upcoming' to 'decision status' using the 'notify me' function on a consultation page when published on our website.

[Ofgem.gov.uk/consultations](https://www.ofgem.gov.uk/consultations)



Once subscribed to the notifications for a particular consultation, you will receive an email to notify you when it has changed status. Our consultation stages are:

**Upcoming** > **Open** > **Closed** (awaiting decision) > **Closed** (with decision)

## 2. Early Competition context and overview

### Section summary

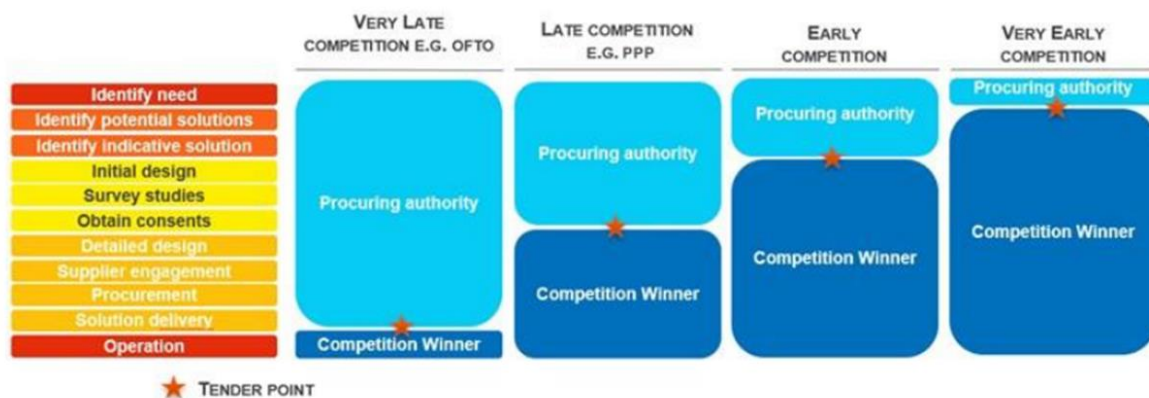
Chapter 2 sets out the context on Early Competition in onshore electricity transmission networks, what this consultation covers and next steps related to the implementation of Early Competition.

### Background

2.1 Competition in the delivery of onshore electricity transmission investment has an important role to play in driving innovative solutions and cost efficiencies while also providing opportunities for new investment in our onshore networks. It has the potential to play a key role in efficient delivery of our decarbonisation targets at the lowest cost to consumers.

2.2 We intend to concentrate our work in 2024 on finalising an “early model” of competition. Early Competition refers to a competition that happens before detailed design work has been carried out. For wider reference, “late competition” refers to a tender for delivery of a project that will already have planning consents approved. “Very late” competition refers to an Offshore Transmission Owner (OFTO)-type competition for the operation and maintenance of existing assets. We consider that Early Competition can maximise the level of innovation delivered through the competitive process, while also allowing for earlier supply chain engagement from bidders relative to late competition. This is an important consideration in the context of the importance of timely delivery of electricity network upgrades to minimise constraint costs as we transition to Net Zero.

**Figure 2: Tender point under various models of competition**



2.3 To enable competition in the design and delivery of onshore energy networks, the Energy Act 2023 received Royal Assent on 26 October 2023. This enacted the changes in primary legislation to provide for competitive tendering of onshore electricity transmission projects. This regime will appoint and license a Competitively Appointed Transmission Owner (CATO) to design, construct, own and operate assets on the electricity transmission network.

2.4 On 22 November 2023, the government's Transmission Acceleration Action Plan (TAAP) was published. The TAAP outlines the government's commitment to introduce competition as soon as is reasonably possible to save consumers up to £1 billion by 2050 and encourage greater levels of inward investment into the energy networks.<sup>6</sup> The TAAP also states the ambition to identify the first eligible project(s) for competition in onshore electricity transmission in 2024.

### **ESO's proposed changes to the Early Competition Plan (ECP)**

2.5 Since the ECP was published in April 2021, the Centralised Strategic Network Plan (CSNP) assessment process has been further developed. The CSNP will act as the framework for identifying and assessing transmission investment options. In July 2023, Ofgem consulted on how the Future System Operator (FSO), now called the National Energy System Operator (NESO),<sup>7</sup> will identify future system needs and the associated options to develop a strategic network investment plan. Our CSNP decision was published in December 2023 following the TAAP publication. The publications set out the expectation that:

- The NESO should carry out an appraisal of the technical, economic, social and environmental aspects of each option, including considerations of routing options
- The CSNP should enable and consider a wider range of potential solution types, and
- The role of NESO in undertaking environmental appraisals and public consultation as part of the new spatial element of its network planning will

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<sup>6</sup> Energy Security Bill Factsheet [Energy Security Bill factsheet: Competition in onshore electricity networks - GOV.UK \(www.gov.uk\)](https://www.gov.uk/government/factsheets/energy-security-bill-factsheet-competition-in-onshore-electricity-networks)

<sup>7</sup> Previously denoted as the Future System Operator (or FSO), the new National Energy System Operator (NESO) will be the independent, public corporation responsible for planning Britain's electricity and gas networks and operating the electricity system.

give more certainty on the planning and consenting process for the delivery of new infrastructure.

2.6 These developments in network planning, alongside a recognition of several risks within the ECP model that need to be carefully managed from a planning and procurement perspective, have led the Electricity System Operator (ESO) to conclude that there would be benefit in making the following two notable changes to the ECP Model:

- a) The competition should build on the optioneering carried out in the CSNP rather than redo it, meaning that:
  - i. The technical specification should be aligned to the indicative solution identified in the CSNP
  - ii. The location of the connection points should be defined
  - iii. Spatial constraints including environmental and social impact constraints should be provided as part of the technical requirements specification; and
- b) Non-network solutions should be considered as part of the initial network planning processes. Where they are identified as the best option, they can be more effectively procured through the ESO's Network Services Procurement (NSP) rather than Early Competition.

2.7 The amended Early Competition would move away from competing a network need, eg X Giga Watt (GW) boundary uplift across Y boundary with potentially geographic limitations, to a more explicit requirement as identified in the CSNP, eg a new X GW circuit between substation A and substation B and geographically confined within a study area used to set a wide route corridor defined within the CSNP. The conceptual comparison between the original ECP and the amended version is shown in Table 1 below.

**Table 1. Characteristics of ECP v amended Early Competition model (EC-I Update)**

<b>ECP Early Competition model</b>	<b>Amended Early Competition model</b>
Non-network and network solutions considered	Network solution only. Non-network options to be procured through Network Services Procurement (NSP)
Technology agnostic	Solution type known (ie new circuit)
Connection points determined by bidder	Connection points identified through CSNP
Route corridors determined by bidder	Wide study area determined by CSNP. Bidder does detailed design and narrows route corridor

2.8 The ESO has concluded that the amended ECP model under the EC-I Update will allow for a **shorter tender process**. The ECP contained a three-stage assessment process: pre-qualification questionnaire (PQ), invitation to tender stage 1 (ITT1) and invitation to tender stage 2 (ITT2) while allowing for bids of a wide variety of potential solutions. The logic behind a two-stage tender was to allow for bidders to undertake their own network studies and development of options including network vs. non-network options, alternative connection points, route options, and for the NESO to evaluate that the bidders' proposals met the requirement at ITT1 prior to bidders spending significant resources developing their detailed proposal.

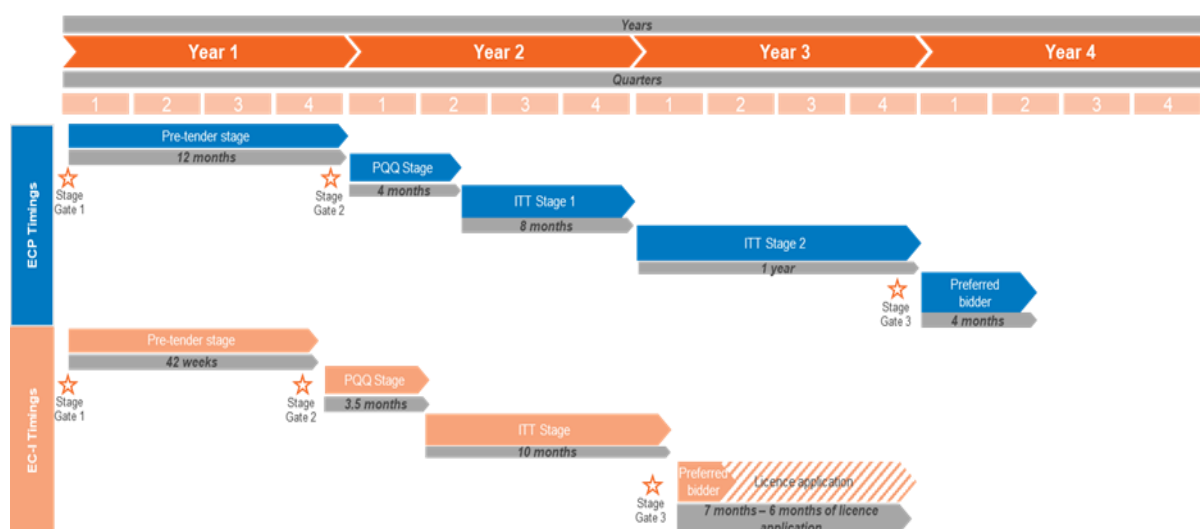
2.9 In support of this amendment, the ESO draws attention to the CSNP undertaking high-level design and setting the allowable solution space, thereby greatly reducing the need for this assessment. Since all bids will be based on a particular reference solution and likely connection points, it will lead to a simpler assessment of meeting the need criterion. This could allow combining the two ITT stages into a single assessment process which is estimated to reduce the tender process timescales by 20 weeks (Table 2).

**Table 2. Comparison of timing for stages of competition for ECP model and amended Early Competition model (EC-I Update).**

	<b>Early Competition / weeks</b>	<b>Amended Early Competition / weeks</b>
Project identification (Stage gate 1)	25	25
Pre-tender (Stage gate 2)	42	42
Tender release	2 – 3	2 – 3
PQQ stage	16	16
NDA	2	2
ITT Stage 1	24	41
ITT Stage 2	37	
Preferred Bidder	29	29
<b>TOTAL</b>	<b>177-178</b>	<b>157-158</b>

2.10 The following is a high-level exhibit of tender timescales proposed in the EC-I Update compared with the initial ECP estimates:

**Figure 3: Tender timescales**





## **What this consultation covers:**

2.11 This consultation focuses on those policy areas relating to Early Competition that have evolved since our March 2022 decision.

2.12 Specifically, this consultation sets out our views regarding the following important areas:

- Amendments to the Early Competition model proposed by the ESO under its EC-I Update
- TOs conflict mitigation in supporting Early Competition tender process
- The ESO proposed cost benefit analysis (CBA) model and wider methodology for identifying candidate projects for Early Competition
- TNUoS under/over recovery for CATOs
- Dealing with CATO/tender failure.

## **What work is required before a competition tender can be run?**

2.13 The ESO will publish the second transitional Centralised Network Plan (tCSNP2)<sup>8</sup> in March 2024, identifying the reinforcements required on the electricity transmission network. The ESO will assess these projects against the Early Competition eligibility criteria and a competition CBA to identify the projects that are likely to provide the greatest benefit to consumers if subjected to an early model tender. Based on this analysis and recommendation, Ofgem intends to identify a suitable project(s) for Early Competition later in the year.

2.14 The ESO is continuing to develop the commercial model and tender process and is engaging regularly with relevant industry stakeholders and Ofgem to ensure the Early Competition framework is well thought through and can attract the required investment on the transmission network to deliver the expected benefits for consumers. We intend to consult on the commercial arrangements for Early Competition in early summer 2024.

2.15 This consultation seeks input from stakeholders on several outstanding policy issues, including the amended competition model, the TO conflict mitigation measures,

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<sup>8</sup> tCSNP2 is the 2024 transitional network planning publication. It is the second transitional CSNP ahead of the first full CSNP, which is expected in 2026.

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the early competition CBA, dealing with CATO/tender failure, and TNUoS revenue recovery process.

### **3. ESO's proposed amendments to Early Competition Plan in the EC-I Update**

#### **Section summary**

This Chapter explains the amendments proposed by the ESO to the version of early competition identified in its Early Competition Plan along with our views on these amendments.

#### **Questions**

- Q1. Do you agree that the proposed amendments by the ESO represent good value for money for consumers?
- Q2. Do you agree with the ESO's proposal of alignment of Early Competition with the Centralised Strategic Network Plan (CSNP)?
- Q3. Do you agree with the ESO's proposal that only network solutions should be eligible for Early Competition?

#### **Introduction**

3.1 We are working to continue development of Early Competition with a view to finalising the model, allowing the first project(s) to be identified by the end of 2024.

#### **ESO's Early Competition Plan (ECP)**

3.2 The ESO's ECP was developed through multiple stages of consultation over a period of more than a year, spanning 2020 and 2021. Workshops were carried out throughout this period with input from a full range of stakeholders including existing TOs, investors, non-network solution providers and other interested stakeholders.

3.3 The ECP set out the ESO's view on how an Early Competition tender process could work, and how it could be incorporated into the electricity transmission network planning process. The ESO's proposals for Early Competition were designed to build on the benefits unlocked by its Pathfinders process and following the required changes to primary legislation, allowed for a full range of network and non-network solutions to participate in the competition.

3.4 The ECP included the ESO's view on the following important considerations for an Early Competition model:

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- The process followed to determine whether specific projects that meet the criteria for Early Competition should advance to an Early Competition tender process
- The criteria that should be used to identify projects from this process that are suitable for Early Competition
- The high-level tender policy and arrangements (and market offering)
- Identification of the main roles within Early Competition and the parties best placed to play those roles; and
- Additional thinking around potential changes to industry codes needed to implement Early Competition, and draft heads of terms that could be used for a licence or contract awarded as a result of the tender process.

## **Rationale for changes to the ECP under EC-I Update**

### **Alignment with CSNP and consenting risk**

3.5 The Electricity Networks Commissioner has identified the spatial and environmental elements that will support CSNP output as being an important means of reducing consenting risk and providing certainty for stakeholders on the need for projects to proceed (recommendation NP2).<sup>9</sup>

3.6 The ECP was designed to allow each bidder to do individual optioneering based on a localised rather than a Strategic Environmental Assessment in the wider network plan context. This approach could lead to increased consenting risks across different proposed solutions. The ESO attempts to avoid such an outcome by incorporating the output of the CSNP process into the early model tender. This process reflects an indicative solution by defining connection points and a wider route corridor, which have already taken relevant environmental constraints into account.

3.7 To support the decisions made during the options assessment of the CSNP process, the ESO recommends:

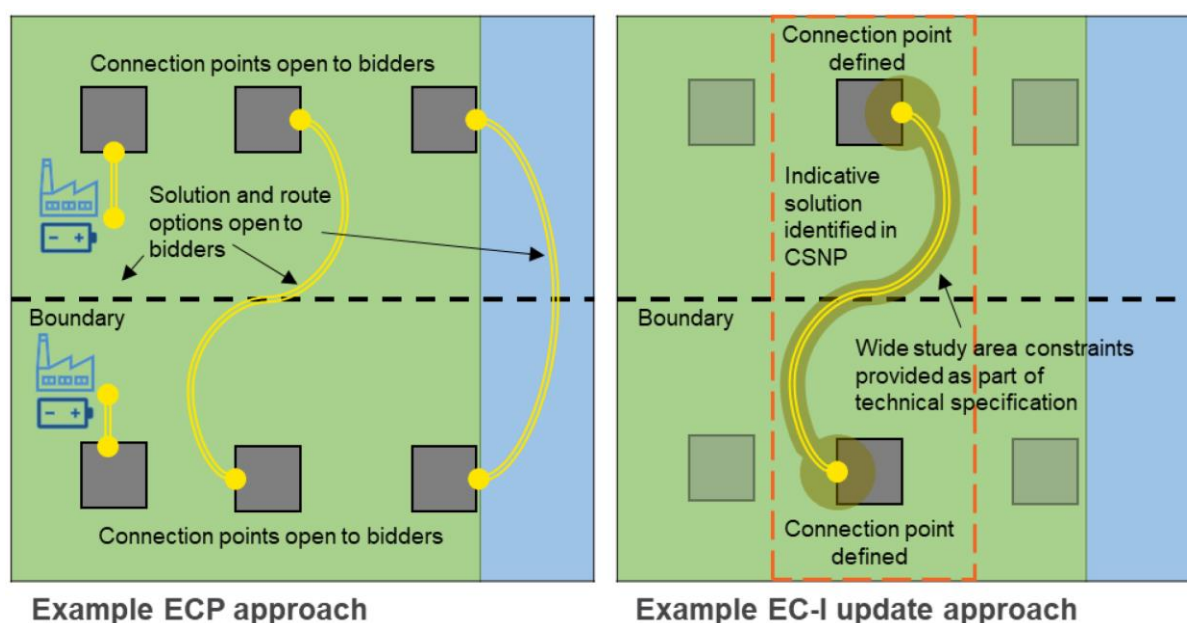
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<sup>9</sup> Electricity Networks Commissioner's recommendations [Accelerating electricity transmission network deployment: Electricity Networks Commissioner's recommendations - GOV.UK \(www.gov.uk\)](https://www.gov.uk/government/consultations/accelerating-electricity-transmission-network-deployment)

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- The technical specification should be aligned with the indicative solution identified in the CSNP
- The location of connection points should be defined
- Study area (used to set a wide route corridor) constraints including environmental and social impact constraints should be provided as part of the technical requirements and specification.

**Figure 4: Comparison between ECP and EC-I Update approach**



3.8 The ESO states that the proposed amendment to counter these delays and additional costs remains compliant with the Early Competition model concept. Following the wide study area determination under the CSNP, bidders would still need to identify an appropriately detailed solution, including narrowing the route corridor within the broad boundaries identified for the indicative solution. The winning bidder would still need to do the detailed design and detailed planning and consenting work during the preliminary works phase. Scope for innovation in technology, contracting and delivery remain as main drivers for consumer value under Early Competition.

**Removal of need for TOs' assessment of bids**

3.9 Under the ESO's original ECP proposals, there was scope for the wider potential range of solutions to have different influences on the local incumbent TO network. As

such, TOs would have needed to assess the influence of each bid on the network to be sure of its ability to maintain network compliance and assess any wider network costs. This would have required significant conflict mitigation arrangements where TOs are also able to bid into competitions. Under the proposed changes to the model, the upfront specification of connection points and indicative solution will negate the need for TOs to undertake wider works assessments on each bid during the tender process, with any variation between potential technical solutions being considered by the ESO at the earlier initial design stage.

3.10 This proposed arrangement has the potential to mitigate the conflict-of-interest concerns bidders may have had in having to share competitively sensitive information between competitors (ie between a bidder and the TO who may also bid). Although there may need to be consideration of some details to enable an appropriate connection to the existing network (eg detailed planning data which stipulates the electrical characteristics of the solution), this is not considered material to a bid and therefore would not be required until the preliminary works stage, ie post-award.

3.11 Reducing the need for TOs' involvement in the bid assessment process will help address stakeholder concerns about the TOs' ability to influence the competition outcome and intellectual property protection. This is not a driver for the proposed ESO change to the model but is a benefit. However, appropriate separation of TOs bidding resource from TO activities funded through the price control still needs to be appropriately considered<sup>10</sup>. It may also allow the TOs to manage the process of undertaking wider works assessments without standing up separate internal teams. The ESO further states that its proposal will improve market confidence in the fairness and transparency of the competitive process by encouraging bidding parties who may have been put off by the participation of incumbent TOs in the bid assessment process.

### **Network vs non-network solutions**

3.12 It had been envisioned under the ECP that in the case of some tenders, non-network solutions may have been able to directly compete alongside network solutions. The ESO has flagged two notable challenges with this approach in the EC-I Update. Firstly, there is considerable complexity in attempting to design a procurement event that enables an objective comparison of two (if not more) fundamentally different

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<sup>10</sup> Our conflict mitigation proposals are set out in Chapter 4 of this consultation.

offerings. Secondly, the award for a successful non-network bidder is likely to look different to that for a successful network bidder: a licence for successful network bids and a contract for non-network bids. Both factors create notable complexity which it considers would lead to the need for more time to run a compliant procurement event. In the context of a more tightly defined tender scope defined by the CSNP, the ESO recommends a change to the ECP proposals.

3.13 The ESO now recommends that non-network solutions should be considered solely as part of the CSNP process that identifies the needs on the network and not again as part of the Early Competition model used to finalise solutions. It sees an additional advantage for the procurement of non-network solutions through the Network Services Procurement (NSP) route leading to shorter tender timelines. Typically, a tender is completed within two years of the need being identified and communicated to industry. This timeframe is attractive to the investors and developers in building their business case. The ESO therefore proposes that non-network solutions are considered solely as part of the CSNP process and not again as part of the Early Competition model. This proposal removes uncertainty, provides the opportunity to better tailor procurement events to encourage innovation and supports the decision-making process undertaken during the CSNP.

3.14 Under this revised approach, there would be different competitive processes for different types of solutions. The CSNP process would assist in identifying the most appropriate solution followed by a competitive process tailored to different solutions, eg for transmission solutions or for non-transmission solutions. Transmission solutions will be procured through the Early Competition process and will also need to be granted a licence by Ofgem, whereas non-transmission solutions would be competed through the ESO's NSP processes and result in a contract with the ESO. The NSP process enables the ESO to provide longer-term contracts to third parties for voltage, stability and constraint management services.

## **Summary of our views**

3.15 We agree with the ESO's proposal to use CSNP optioneering in the EC model due to its desired benefits. This approach simplifies planning and consenting due to endorsement of the solution by the CSNP. It can also result in reduced risk for bidders as a defined scope of solution and connection points being already known can assist network planning for all the involved parties. Not undoing CSNP optioneering may also

lead to reducing the conflict of interest as the TOs won't have to assess bidders' options under the competition owing to clarity on connection points and solutions; whereas bidders will be able to concentrate on a pre-defined study area used to set a wide route corridor. In addition, potential reduction of tender stages from two stages to one can speed up the process.

3.16 We also agree with the ESO's logic that this revised approach will be best supported by different competitive processes for different solution types, ie transmission solutions and non-transmission solutions. We consider that interactions with the NSP for procuring non-network services will need to be suitably clear and anticipate seeing non-network solutions are identified as part of the CSNP process in a meaningful manner. We welcome views from relevant stakeholders, in particular non-network solution providers on this proposed amendment to the EC model.

3.17 Our view is that all viable solution types should be considered in the development of the electricity transmission network. Assessing the most appropriate solution types to address a specific requirement can lead to tailoring the competitive process in either Early Competition or network services.

3.18 We recognise that adopting such an approach may lead to less scope for innovation in design, but scope for innovation in solution delivery will still be possible. Overall, we think that the proposed amendments in the EC-I Update are the best options on balance.



## 4. Conflict mitigation

### Section summary

We summarise our initial views and proposals on arrangements to mitigate Transmission Owners (TOs) conflicts of interest in this chapter.

### Questions

- Q4. Do you have any material concerns with the conflict mitigation measures proposed by Ofgem for incumbent TOs and other bidders?
- Q5. What are your views on our proposed modification to put in place timing requirements for when the TO must confirm its intention to bid and put in place conflict arrangements?
- Q6. What are your views on our proposed modification to restrict the transfer of TO employees between the Bidding Unit and the team undertaking the Tender Support Activities and pre-construction activity?
- Q7. What are your views on the proposed information sharing framework and, on the roles, assigned therein?
- Q8. Do you have any material concerns with the company structure proposed for raising debt for Early Competition?

4.1 In our March 2022 decision, we explained that we want to ensure as many bidders are encouraged to participate in the competition process as possible. The TOs have a significant amount of knowledge and experience in the delivery of electricity transmission infrastructure. As such, as long as the appropriate conflict mitigation arrangements can be put in place, we still consider they should be able to enter bids into competitions.

4.2 In our March 2022 decision, we identified the following as potential or perceived risks that would need to be addressed for the TOs to be allowed to bid:

- TO influence on options considered in analysis that determines the required network upgrades
- TO role in initial network design allowing them more time than rival bidders to develop proposed solutions
- TO role in reviewing other bidders and access confidential bidder information

- Risk of cross-subsidy from RIIO funding to lower bids/manipulate competition.

4.3 The arrangements considered in our March 2022 decision focused on specific obligations and business separation requirements for the incumbent TOs, who may decide to bid on projects. This chapter sets out our updated position on arrangements to mitigate conflicts of interest in the context of the Electricity System Operator's (ESO) updated proposals for Early Competition.

### **ESO updated proposals and their influence on conflict mitigation**

4.4 As explained in Chapter 3, the amended Early Competition eliminates the TOs role in assessing potential bids which was one of the central points of conflict within the Early Competition model as described in the Early Competition Plan (ECP). The role of the TOs is limited to providing feasibility studies, connection studies and tender support activities.

### **Ofgem proposals for the role of TOs within Early Competition and conflict mitigation arrangements**

4.5 Based on the ESO's Early Competition Implementation Update (EC-I Update), we expect the TOs to undertake the following roles in support of an Early Competition tender:

- Provide relevant network information to the ESO in line with existing obligations
- Share relevant site-specific technical information with ESO (and third-party bidders) to run a transparent and efficient tender process. For example:
  - Substation fault levels - Busbar fault details at point(s) of interconnection
  - Fault level - Infeed details at point(s) of interconnection (if applicable)
  - System impedance
  - Site layout and bay details

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- Operational diagrams for existing TO substations at point(s) of interconnection (if applicable)
- Existing protection key line diagrams for existing TO substations at point(s) of interconnection (if applicable)
- Interfaces with existing and future TO projects (if applicable)
- Integration into existing automation schemes (if applicable)
- Line connections into existing (if applicable, for new connections)
- Respond to queries from ESO/third-party bidders during the invitation to tender (ITT) stage
- Working with successful bidder during development phase to facilitate the interface and commissioning of the assets (as done currently with other TOs)
- TOs should consider the tenderers proposal and the potential impact on their own network access and outage planning expectations.

4.6 Where the above roles and responsibilities for the TOs require modifications to existing TO licence conditions, we will, subject to the outcome of the consultation, work with licensees and wider stakeholders to enact the relevant licence changes.

4.7 In the discharging of the above roles supporting the consultation process, we propose that the following conflict mitigation requirements will need to be implemented for the incumbent TOs to also bid into the tender process:

- 1.) Overarching licence obligations on TO conduct when providing information to bidders and in their other tender support activities:
  - i. To act in a way that does not give the TO bidding party, or any other party, an undue advantage over any other participants in the tender process

- ii. To act transparently, making all relevant information available and clearly setting out the measures taken to mitigate conflicts of interest and protect sensitive information. As such we would expect the TOs to sign a confidentiality agreement with the ESO for participation in the tender
  - iii. Facilitate the tender process in a manner such that it may proceed timeously and efficiently.
- 2.) In addition, we propose that the TOs will be required to submit a conflicts mitigation methodology to us ahead of any tender they wish to bid into. This methodology will set out the steps they will take and the associated monitoring to ensure that the highlighted conflicts of interests, and risks are suitably mitigated in line with the requirements proposed in the rest of this chapter.

4.8 Given the TO role within the Centralised Strategic Network Plan (CSNP) analysis that will help define the scope of any resulting early competition tender, it is important to ensure that this role does not give the TOs an unfair, or a perceived unfair advantage, over other bidders. We consider that business separation measures with limits on the movement of TOs' employees involved in supporting the CSNP analysis will be critical in mitigating this potential conflict. With clear delineation between the TO team supporting the CSNP and the tender process, and the TO bidding team and the prevention of employees moving between them, bidders should gain confidence that the TO will not benefit from holding any information back from bidders, nor gain an unfair advantage from the work carried out to support the CSNP.

### **Business separation measures**

4.9 Given the ESO's suggested changes to the Early Competition model, we do not consider that the full legal separation of the bidding unit is necessary. Rather, we suggest that the TO 'bidding unit' can be either a separate company within the TO group (including an 'associate', as defined in Standard Condition A1), or a unit within the TO's transmission business (or that of an associate).

4.10 This is consistent with our previous consideration in November 2016 in the context of the late competition model.<sup>11</sup> We similarly proposed that the full legal separation of any bidding unit from the TO project development team would not be a requirement. Given the similarities in the potential conflict, it seems sensible, in the context of the ESO amended model, to propose the equivalent requirements.

### **Employee transfer restrictions**

4.11 Although we do not see the requirement for full legal separation of the bidding unit as necessary, we consider that some restrictions are required. Our proposal is that the bidding unit must not comprise any employees of the TO who are involved in a project's initial CSNP design or tender support activities (full time or part time), from the earliest date of implementation of separation arrangements viable. There is also to be no transfer of employees from the bidding unit to the TO until the completion of a tender to mitigate the risk of the bidding unit influencing the TO's approach to the tender.

4.12 **We expect the timing and specific details of employee separation to be set out in a final approved conflicts methodology statement.** We will also require details of any involvement of other employees of the TO in the bidding unit to be specified in the methodology, including rules governing this involvement, in line with the obligations on conduct. In particular, this includes shared services employees and employees of central legal teams.

### **Managerial separation**

4.13 Our proposal is to require separation of management structures between the TO and any bidding unit up to, but not necessarily including, the TO parent board. Specifically, we will require the management of the bidding unit to be organised in such a way as separates it from the rest of the TO. Practically this will mean the creation of discrete management structures for the bidding unit. We do not consider that the additional protection that would be achieved by requiring separation at parent board level would be proportionate to the disruption involved for the TO, but welcome stakeholder views on this consideration.

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<sup>11</sup> Ofgem decision, covering the role of Transmission Owner (TO) and measures to manage potential conflicts of interest, November 2016 [ECIT November 2016 Decision \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/consult/condocs/ecit/ecit_november_2016_decision_ofgem.gov.uk)

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## **Information sharing**

4.14 We consider it important that the TO takes the necessary steps to protect the confidentiality of all information that it holds in relation to its tender support activities.

4.15 We will require the TOs to treat information related to tender support activities, and any other information it comes into possession of during a tender (for example information about the content of bids or bidder strategies), confidentially. We will require that the TO does not disclose such information to any bidding unit or other participant in a tender, outside of what is required as part of the tender process or under its licence.

4.16 We propose to work closely with the ESO and the Department of Energy Security and Net Zero (DESNZ) to identify the risks arising from the flow of information during the Early Competition tender process and if required **create an Information-Sharing Framework** that is compliant with all applicable competition legislation and doesn't confer an unfair advantage on the TOs. We intend for the ESO to act as an information-exchange intermediary, anonymising communication between third parties, Bidding Units and the TOs assessing the impact on their network. We also expect third party bidders and TOs to sign a Non-Disclosure Agreement (NDA) letter before obtaining access to any commercially sensitive information. The NDA templates will be provided by the ESO as part of the tender pack.

4.17 We are not formally proposing a requirement on the TOs and any bidding unit to have separate IT systems, unless this is identified through the information sharing framework as being required for compliance with all applicable competition legislation.

4.18 We welcome stakeholder views on the proposed information sharing framework and the roles assigned.

## **Financial separation**

4.19 In line with our November 2016 policy decision on the equivalent arrangements for late model competition, we will require that the TO and its bidding unit are financially separated, meaning that the costs incurred by the bidding unit are not recovered from regulated revenue related to any other of the TO's activities or assets. We consider that financial separation is covered by the obligations contained in Standard Licence

Condition B5 (prohibition of cross-subsidies) and B6 (Restriction on Activity and Financial Ring Fencing).

4.20 We expect the TOs to demonstrate through the proposed **conflict methodology statement** and **independent audit** that their conflict mitigation measures are sufficient and compliant with our policy.

4.21 We welcome stakeholders' inputs on audit, conflicts methodology statement and separation requirements placed on TOs.

### **Compliance approval and monitoring obligations**

4.22 We have proposed a variety of measures, outlined below, to enable scrutiny and approval of a TO's conflict mitigation arrangement. This is so we and other parties involved in the competitive process can be assured that the TO's arrangements are in place and effective. These proposals involve internal scrutiny by an independent appointed person within the TO, and scrutiny and approval by Ofgem.

4.23 The licence change consultation will provide further detail on the implementation of these requirements.

4.24 We propose that for each tendered project a compliance methodology statement should be submitted to us for approval as soon as possible before the tender commences, and that it should describe the steps the TO has taken, and/or intends to take, to fulfil all its obligations to mitigate potential conflicts of interest. We propose that we would assess the methodology and request changes where needed.

### **Scrutiny**

4.25 The measures the TO has committed to will require oversight and scrutiny to ensure they are in place and effective. This can come from many sources: internal scrutiny from the TO or designated personnel, external scrutiny and oversight from us, or external scrutiny from an independent auditor or industry panel.

4.26 We think there should, at a minimum, be internal scrutiny by a person appointed by the TO to oversee its compliance with the conflict mitigation measures. This person should:

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- be independent from the TO preliminary works team and the TO bidding unit.
- prepare a report on the measures put in place and how they achieve the overall obligations on the TO to be sent to Ofgem to scrutinise the outcome
- suggest any additional relevant measures to mitigate conflicts of interest effectively; and
- have access to the resources needed to assess compliance.

4.27 There may also be value in having an independent party scrutinise and audit the arrangements the TO has in place. While the internal scrutiny is likely to identify any issues or shortcomings in the TO's compliance with the arrangements, independent scrutiny could provide additional assurance for us and other bidders. It would, however, add cost to the process, so we would need to be satisfied that it has brought significant additional value to the competitive regime. We are interested in stakeholders' views on this.

4.28 If TOs are found non-compliant, we have a range of possible remedies depending on the seriousness of the non-compliance. We could, for example, require the TOs to change their processes. For more serious matters, we could consider whether it would be appropriate for the TO or their associated business to continue participating in the competition.

### **Other bidders**

4.29 Other bidders could also gain an unfair advantage if they have prior knowledge or experience of the project to be tendered. An example could be where an employee of a bidder worked with the incumbent TO on project development before joining the prospective bidder.

4.30 We propose that all bidders comply with the same level of requirements as Offshore Transmission Owners (OFTO) bidders. OFTO bidders are required to sign confidentiality agreements to gain access to confidential information on a project, and a 'conflicts of interest' declaration. We propose that the NDA be submitted to the ESO and the conflicts of interest declaration be submitted for our approval no later than the start



of the ITT stage of the tender. Where a bidder has highlighted conflicts of interest in making this declaration, we would ask for and assess information from the bidder on separation measures in place, which could include a memorandum of understanding.

4.31 We will require mitigation measures for all 'other bidders' with potential conflicts of interest, proportionate to the role that the bidder has played and information it has had access to in relation to the project to be tendered. If a bidder adds a new party to its bidding group at later stages of the tender process, we expect the bidder group in its new form to be covered by a confidentiality agreement and a conflicts of interest declaration. We would also expect to consider information on measures to mitigate any new conflicts of interest that adding the new party has given rise to.

4.32 We encourage bidders to engage with us as soon as practicable after we have selected a project for Early Competition to inform us of potential conflicts of interest and to ensure any conflicts are mitigated. Any bidder with potential conflicts of interest that has failed to implement appropriate conflict mitigation arrangements may be excluded from bidding.

4.33 If a bidder is unable to demonstrate that it has mitigated conflicts of interest appropriately, they will be unable to bid.

### **ESO's views on company structure**

4.34 The ESO identified cross-subsidy from RIIO price control funding as a potential risk to a fair competitive process. Without the ability to clearly delineate the costs and financing of the project that is subject to competition, there is a risk that other TO funding, through RIIO, could be used to unfairly reduce the cost of their bids. The ESO emphasises the importance of delineated cost capture and a project-specific debt-raise to reduce the risk of unfair outcomes.

4.35 The ESO has identified five areas that are important when considering what arrangements should be put in place to meet the ECP requirement to run a debt competition:

- **Cost to consumers** – costs to consumers should be minimised as far as possible

- **Risk of cross-subsidy/unfair commercial advantage** – the risk of this must be minimised, as per TO Standard Licence Conditions B5 and B6
- **Efficiency of debt** – as there is no incentive to minimise costs as a preferred bidder, the ESO as the party running the tender needs to be able to review the debt competition process
- **Control of project assets** – should the Successful Bidder be unable or unwilling to continue with the project, the counterparty must be able to step in and enact appropriate measures in a clear and efficient way
- **Level playing field** – whatever arrangements are implemented must ensure that there is a level playing field between commercial bidders and regulated bidders.

4.36 After identifying the five main areas, the ESO in its EC-I update mentions two potential approaches that bidders can use to secure debt on a project and compares their respective impacts and advantages in the five areas identified above. The two approaches mentioned are:

- a) By creating a Special Purpose Vehicle (SPV) for the project; or
- b) By implementing specific arrangements under a corporate borrowing approach.

### **Ofgem views on company structure:**

4.37 We agree that the two approaches suggested by the ESO represent appropriate options to address the potential risks. The key principles that need to be reflected to ensure a level playing field are as follows:

- There should be no advantage to the TO bidding team as a result of tender support activities
- As per SLC B5/B6, there should be no RIIO cross-subsidies to artificially lower bids
- There should be separation between assets/finance from wider TO activities.

4.38 An SPV allows for the isolation and ring-fencing of the project-specific assets from the wider TO asset base. It allows debt to be raised against a specific project and reflect project-specific risk. Specific project generated cashflows can be monitored and allocated to lenders and investors. Assets can potentially be easily transferred (ie re-tendered at the end of revenue period). These conditions are difficult to recreate effectively under a corporate structure, potentially leading to an arrangement that could be difficult to assess against cross-subsidy requirements, deterring market participation. The SPV approach should provide the optimal level of clarity for all bidders and therefore provide confidence that the competition being undertaken will take place fairly. For this reason, our preferred approach is that the TOs and potential bidders create an SPV to bid into Early Competition and we welcome views from stakeholders.

4.39 Notwithstanding this, there may be certain aspects of bidder business structures and regulatory requirements that make this option unappealing for new entrants or the existing TOs. If this is the case, we particularly welcome views from stakeholders on this matter.

4.40 If the results of this consultation reveal that our preferred approach will lead to a narrower pool of potential bidders being able and willing to bid, in the interests of maintaining overall consumer benefit we are open to considering allowing bidders to raise debt in a corporate capacity where bidders can provide clear evidence that they can do so whilst still:

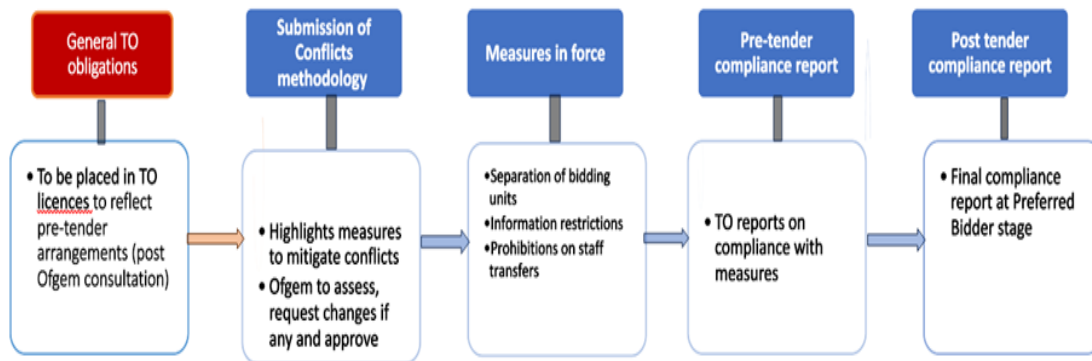
- Allowing project risk to be accurately priced in the debt competition
- Demonstrating absence of cross-subsidies in pricing equity and debt; and
- Demonstrating ability to ring-fence and transfer assets.

4.41 We would welcome views from stakeholders on the company structure and level of separation proposed to ensure a fair Early Competition regime.

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**Figure 5: Stages of conflict mitigation measures**



## 5. Cost benefit analysis

### Section summary

The Electricity System Operator's (ESO) proposals and our initial views on the cost benefit analysis (CBA) methodology developed by the ESO to advance projects for Early Competition are presented in this chapter.

### Questions

Q9. Do you have any material concerns with the ESO's proposed methodology of its CBA model and the elements considered therein?

### Introduction:

5.1 As explained in our March 2022 decision, the criteria for Early Competition is:

- New,
- Separable,
- Certainty, and
- likely to deliver an anticipated benefit to consumers if early competition is applied (via CBA).

5.2 The ESO will carry out a CBA on each project identified in its Central Strategic Network Plan (CSNP) that meets the rest of the criteria for Early Competition.<sup>12</sup> This CBA will be used to indicate whether running an Early Competition is likely to provide an outcome that is beneficial to consumers, compared to the counterfactual TO delivery under RIIO (referred to as "The RIIO counterfactual" within this Chapter).

5.3 The ESO has been developing a suitable CBA framework that can be used to test projects against this criterion since the conception of the Early Competition Plan (ECP). This chapter sets out ESO's conclusions on this CBA methodology and our views on it.

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<sup>12</sup> This includes the second Transitional Central Strategic Network Plan which will be published in March 2024.

## **Overview:**

5.4 The ESO's proposed CBA methodology is set out in detail in its EC-I update.<sup>13</sup> It centres on the consideration of a range of costs and benefits that could occur from applying Early Competition to a project rather than the RIIO counterfactual. Where these costs and benefits have been able to be quantified through comparative benchmarks or other evidence sources, they have been captured within a quantitative CBA model. Additional costs and benefits that cannot be robustly quantified are considered within the qualitative element of the CBA which is used alongside the quantitative modelling to make a recommendation of whether Early Competition should be used to deliver an electricity transmission project.

5.5 This CBA framework will be used by the ESO to make a recommendation to us of which projects it considers should advance to pre-tender market engagement as part of the Early Competition model process.

5.6 The CBA would then be updated following the pre-tender market engagement stage. This could include adjustments to quantitative model inputs, or the reconsidering of qualitative elements prior to the ESO's final recommendation on whether to launch an early model tender.

## **The quantitative CBA model**

5.7 The ESO's consultants, KPMG supported the ESO in developing an Excel-based financial cost benefit analysis model. This model captures and compares all quantifiable costs and benefits for development, procurement and delivery across the two approaches.

5.8 The CBA model derives an indicative estimate of the revenue that would be recovered from consumers if a qualifying project is funded through an Early Competition model. This is referred to as the factual case which is compared on a Net Present Value (NPV) basis to the equivalent modelled cost to consumers of delivering a qualifying project under the RIIO counterfactual.

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<sup>13</sup> ESO cost benefit assessment methodology, sets out the methodology for assessing which needs and associated reference electricity transmission projects are potentially suitable to be delivered via early competition February 2024 <https://www.nationalgrideso.com/document/301781/download>

5.9 The modelled revenue for the factual case is built up from an extensive range of benchmarks capturing the indicative range of potential costs throughout the life cycle of the project. Financing cost benchmarks are based on a range of comparably large competitively delivered investments within the UK which have been delivered through a project finance approach and reflect how the ESO expects projects to be financed under its proposed Early Competition model. Benchmarking evidence from across a range of comparable projects was used to identify an indicative range of potential cost savings that can be achieved through a more competitive approach to project delivery.

5.10 The factual case also includes the costs that arise in running the tender process as well as, in the case of projects where competition is expected to lead to delays, a forecast of any additional constraint costs that consumers incur as a result of the delay. A detailed list of costs and benefits can be seen in Appendix 1.

5.11 The RIIO counterfactual is modelled based on the funding arrangements in place for the current RIIO-2 price control. Project costs are recovered over 45 years with the allowed Weighted Average Cost of Capital applied each year as an annual return on the project costs that have yet to be recovered.

5.12 To ensure a fair comparison of factual and counterfactual revenues with different timing profiles, a common discount rate is used to allow a fair comparison of the overall cost of both approaches on a fair basis. In line with the Treasury's Green Book guidance on CBA, the Spackman approach (as described in the assumptions in the ESO's methodology document)<sup>14</sup> and the social time preference rate is used to arrive at an NPV of the cost or benefit to consumers of competition relative to the counterfactual for each qualifying project.

### **Sensitivities:**

5.13 The data and evidence used to build up the factual case provide a benchmarked range, rather than specific point estimates. The model runs a base case for the ESO's view of the most likely outcome based on the benchmark data. Typically, this uses points towards the middle of the benchmark range to provide a central view of the likely impact. The model includes the following sensitivities, to allow for the impact of the

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<sup>14</sup> The Spackman approach is the most practical for cases involving private investment but public benefit. It ensures that the financing costs of investments are adequately reflected as part of the costs in the CBA. [discounting-for-cost-benefit-analysis-involving-private-investment-but-public-benefit.pdf \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/discounting-for-cost-benefit-analysis-involving-private-investment-but-public-benefit.pdf)

points at the high and low end of the benchmark ranges to also be assessed against the RIIO counterfactual:

- Cost of Equity: High and Low from the benchmark range
- Cost of Debt: High and Low from the benchmark range
- Gearing: High and Low from the benchmark range
- Capex Efficiency: High and Low from the benchmark range
- Procurement cost: High and Low from the benchmark range
- Bidder Cost: High and Low from the benchmark range
- Constraint cost from delay: High and Low (see below)

### **Constraint costs:**

5.14 The ESO will use its wider network planning analysis to capture the CBA impact of any potential delay to commissioning driven by the Early Competition tender process and associated constraint costs for each of the projects which are assessed for Early Competition. The ESO concludes that since the process undertaken through the Early Competition model effectively replicates the stages of development undertaken in the RIIO counterfactual, there should not be an inherent level of risk caused to projects at a suitably early stage of development.

5.15 In case of projects that are likely to be at a later stage of development at the point they are considered in the CBA, it is more likely that there will be a duplication of this development work between the incumbent TO and then through the Early Competition process. This duplication will potentially cause a delay that can be calculated as a level of additional constraint costs faced by consumers. Currently this wider network planning analysis captures the optimal date of required projects across four potential future scenarios, referred to as the Future Energy Scenarios (FES). This means that projects can have different optimal dates across the four FES. For the base case, the earliest of the optimal dates for a project across the FES will be used to determine the constraint impact of any delay. For the model sensitivities, the same calculation will be



used to set the high constraint cost sensitivity. The FES with the latest optimal date will be used to set the low constraint cost sensitivity.

5.16 The ESO anticipates that future CSNP processes will move away from multiple scenarios to more defined pathways and therefore the most appropriate scenario for that pathway will be used in any constraint cost calculation.

## **Qualitative Assessment**

5.17 The approach set out by the ESO provides a comparative assessment framework for qualitative costs and benefits of delivering solutions which address transmission needs under an Early Competition framework versus a regulated framework. Factors proposed for use in the CBA model for qualitative assessment include large consortium costs, additional system costs, bidder portfolio effect and innovation in delivering system, processes, technology and ecological benefits. Detail on the proposed qualitative assessment elements can be seen in Appendix 2. The qualitative assessment process is the final step in the CBA. The factors set out in this section and the total score from the framework described above will supplement the results from the quantitative assessment and help determine the delivery route that provides best value to consumers.

## **Results interpretation**

5.18 The CBA will compare the base case and full range of sensitivities against the RIIO counterfactual. This will provide a range of estimated consumer cost impacts of using Early Competition that is compared against the equivalent estimated cost impact under the RIIO counterfactual. Important considerations that the ESO proposes to consider to reach a recommendation for Ofgem include the following:

- Whereabouts in the range of outcomes across the sensitivities for the factual Early Competition approach does the RIIO counterfactual sit?
- Through the sensitivity analysis, are there any specific elements or benchmarks that are having undue influence on the overall results, and to what extent are the best and worst early competition outcomes across the sensitivities comparably likely?

5.19 When testing the robustness of the quantitative results the ESO would also expect to consider the following:

- the number of model runs where the factual case was determined to be better value for money compared to the counterfactual case
- the level of divergence from the mean average of the sensitivities. The wider the range of potential outcomes, the less confidence the ESO might have in the base case
- the main value drivers. If for example all benefit is driven by a single value driver, then the ESO may want to place more weight on the sensitivities which relate to that driver.

5.20 The results of the qualitative assessment and the relative strength of answers to the qualitative factors between counterfactual and factual provide an additional perspective on the solutions presented for each need. The outcome from this assessment when compared with the results of the CBA model is an important part of the decision-making process.

5.21 The results from the quantitative assessment must be considered in conjunction with the results of qualitative assessment to determine the total influence on consumer value.

### **Project assessment under tCSNP**

5.22 As part of the tCSNP process, all projects meeting the new, separability and certainty criteria defined for Early Competition will be identified and considered through the ESO's CBA. The ESO notes that the identification of the first suitable project(s) for competition from the tCSNP, may require additional examination, including consideration of additional project-specific factors not captured within the CBA. This could include consideration of the level of maturity within the development of a project included in the tCSNP. This is the result of the evolving nature of network planning and the processes to support CSNP, which will mature further ahead of future CSNP publications.

## **Ofgem views on proposed CBA model**

5.23 Overall, we consider that the ESO's CBA model and wider CBA methodology is fit for the purpose of identifying suitable projects for Early Competition. It uses suitable, well thought out benchmarks, and through the sensitivity analysis captures a range of potential outcomes from a competitive process in a proportionate manner.

5.24 Experience from other competitive models, such as the OFTO regime and DPC<sup>15</sup> in the water sector, suggests there are likely to be various "unknown unknowns" in terms of potential costs and benefits which may be discovered as solutions are developed. When discovered or realised, these factors should be considered in future iterations of the methodology.

5.25 As with most CBA models, the interpretation of results and qualitative factors will need to be carefully considered. In our view, the ESO's qualitative analytical framework will help the ESO to assess whether any of the qualitative costs and benefits identified affect the overall conclusions from the quantitative assessment. This will deliver a more holistic, rounded assessment of the likelihood of Early Competition to deliver value for consumers.

5.26 Alongside the qualitative assessment within the CBA methodology, there may be wider qualitative considerations that are hard to monetise which may not be fully captured in the ESO qualitative methodology. Without wider consideration of such factors, and too strong a focus on the quantitative results there could be a risk that the CBA will simply favour the projects with the highest capital cost, even where these may not be the type of projects third parties are interested in bidding for. We will work with the ESO to ensure that both its recommendations, and our final decision on projects taken forward for an Early Competition consider all relevant considerations alongside the CBA assessment.

5.27 In considering wider factors and potential risks, it is important to distinguish between whether these are specific to the Early Competition model or inherent in the delivery of large infrastructure projects. For example, delay or non-delivery could occur

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<sup>15</sup> Direct procurement for customers (DPC) involves a water or wastewater company competitively tendering for services in relation to the delivery of certain large infrastructure projects, resulting in the selection of a third-party competitively appointed provider (CAP). [Direct Procurement for Customers - Ofwat](#)

for several reasons at different stages in a project's development depending on the nature of the project, independent of whether an Early Competition model is used. There could be unforeseen ground conditions, planning consents may be delayed, associated generation projects may fall away or be delayed, or there may be major issues with contractors (eg insolvency) or other supply chain bottlenecks (eg lack of equipment supply). These project-specific risks are inherent in the development of high-value projects and apply to both the status quo and the Early Competition model and so are not specifically quantified in the ESO's CBA methodology.

5.28 Nevertheless, in the context of the recommendations of the Transmission Acceleration Action Plan (TAAP) and the importance of timely delivery, it is likely to be helpful in the case of some projects, to further understand the underlying assumptions around the project-specific risks before reaching a final decision. For example, more detailed assessment might identify that an assumed delivery date may be particularly conservative or optimistic compared to other projects, meaning there could be higher or lower risk of delay from Early Competition than would be identifiable through the CBA. We propose to work with the ESO to determine an appropriate and proportionate approach that allows us to supplement the CBA result with consideration of such factors in a sufficiently timely manner. This would ensure that these considerations are appropriately considered before a final decision is made to start an Early Competition tender.

5.29 We do not see the CBA methodology as developed by the ESO as something that should remain static. The commercial, regulatory and legislative arrangements for Early Competition are in the implementation phase. We expect the ESO to continue working with internal stakeholders, the Department for Energy Security and Net Zero (DESNZ), ourselves and others to refine its approach and integrate it into the network planning processes and help make Early Competition a transformative delivery model in the sector.

## **6. Transmission network use of system (TNUoS) revenue over/under recovery**

### **Section summary**

We summarise our proposals for the TNUoS revenue recovery for CATOs under the Early Competition model in chapter 6.

### **Questions**

Q10. Do you have any material concerns with the proposed TNUoS revenue recovery model for a CATO similar to the OFTO model?

### **Introduction**

6.1 The Electricity System Operator (ESO) recovers the cost of provision, maintenance, upgrade and expansion of the transmission system through TNUoS charges. Approximately £4.1 billion of charges a year is levied on generators (c.£1 billion) and demand users (c.£3.1 billion).

6.2 Under Early Competition, Competitively Appointed Transmission Owners' (CATOs) revenues will be recovered via TNUoS charges in the same manner as Transmission Owners' (TOs) and Offshore Transmission Owners' (OFTOs) are currently. The ESO is responsible for calculating TNUoS charges such that they aim to recover the aggregate of each TO and OFTO's annualised allowed revenues which will not exactly align with the amount spent by each TO or OFTO. Similarly, ESO will set TNUoS charges with an aim to recover the total relevant transmission revenue, but as charges are based in part on forecasts (eg of demand), they will not always recover the total annualised revenue in practice.

### **OFTO TNUoS revenue recovery model**

6.3 Under RIIO, in any year in which there is an under-recovery of TNUoS, a TO will receive less than the annualised allowed revenue to which it is entitled, and the ESO will adjust future TNUoS charges so that they are made whole. By contrast, OFTOs receive their full stipulated revenues even during the periods of under-recovery of TNUoS by the ESO. The rationale behind this model is that as opposed to the TOs, OFTOs could suffer more severe financial repercussions from a short-term fall in expected cash flow. Since the TOs are much more highly capitalised than the OFTOs, therefore they are not as severely influenced by annual revenue drop during TNUoS under-recovery periods and

can manage their affairs until they are paid back the arrears when the ESO adjusts future TNUoS in subsequent periods.

## **Ofgem's proposal for CATO TNUoS revenue recovery**

6.4 Under Early Competition, we need to consider whether CATOs<sup>16</sup> should be:

- Treated as TOs, with over and under recovery corrected for over time, or
- Treated like OFTOs and receive their full revenue within-year.

6.5 We are of the view that exposing CATOs to such an uncertainty in revenue is not in consumers' interest. We expect bidders (including TO bidders) to structure the financing of the projects in a typical project finance approach. This will require revenue certainty to ensure timely payment of debt obligations. Revenue uncertainty will make this more difficult and lead to less efficient bids to cover this risk. Therefore, we propose that due to likely similarities in company structure and capitalisation, CATOs should be treated like OFTOs and receive revenues in full without being influenced by periods of TNUoS under-recovery by the ESO.

6.6 Our proposal is based on the consideration that CATOs will be significantly smaller in size and structure than the incumbent TOs. Ensuring that the CATO revenues are secured within-year is better suited to the financing structure expected to be delivered through Early Competition. This includes where a TO wins a project-specific CATO licence via early competition tender, meaning that all successful bidders will be treated equally.

6.7 Success of the Early Competition model for onshore transmission network projects is in the interest of consumers and we need to ensure that the Early Competition framework is attractive to bidders. We are therefore seeking to minimise the impact of any avoidable risk(s) to the Early Competition to widen bidder participation and promote effective competition. Our proposal in para 6.5 above also takes this important factor into account.

6.8 We will carefully consider responses to this consultation before reaching a decision on this proposal. Furthermore, we will remain open to reconsidering this

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<sup>16</sup> An existing TO winning an Early Competition tender would also be treated as a CATO

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position in the future depending on the level of subsequent CATO penetration in onshore network ownership.

## 7. Options for dealing with CATO/tender failure

### Section summary

We present our range of options for dealing with CATO/tender failure and conditions required for appointment of CATO of Last Resort (CATO OLR) under the necessary circumstances.

### Questions

Q11. Do you have any material concerns about the proposed approach and principles in dealing with a situation of CATO/tender failure?

### Introduction

7.1 We consider that delivery of critical projects in a competent and timely manner is in the interest of consumers. To this end, just like the incumbent Transmission Owners (TOs), Competitively Appointed Transmission Owners (CATOs) will be governed under a specific set of obligations and requirements to act in an efficient and sensible manner while delivering the essential services. Tender documents will specify clear requirements on bidders in terms of their financial resilience as well as monitoring and reporting arrangements to ensure that measures can be implemented at all project stages to avoid and prevent a CATO failure.

7.2 As is currently the case with the Offshore Transmission Owner (OFTO) developers, we expect that successful bidders will need to provide and maintain intervention plans to address emerging financial concerns or performance issues as soon as possible.

7.3 Within this chapter, CATO OLR specifically refers to the transfer of existing CATO assets and revenue to a new CATO (including TOs potentially) where the original CATO is unable to deliver the requirements in its licence. A CATO OLR process is a competitive process and will only be run where we consider that it is in the interest of consumers to do so.

7.4 The aim of the CATO OLR mechanism is to minimise the risk of an asset becoming stranded or delayed in connecting to the onshore electricity network and provide certainty to all stakeholders that, should a CATO business fail, another CATO would be in place for the entire period of the original revenue term. The flexibility of the CATO OLR



mechanism is intended to enable a seamless transition of obligations throughout the revenue term.

7.5 While we reserve the right to implement the CATO OLR mechanism at any stage during the project lifecycle should the need arise, we view this option as being one of the extreme elements at the end of the framework spectrum. For example:

- if there are failures ahead of energisation, we would always consider re-tendering the project if sufficiently early
- in some cases, we may consider whether it is in consumer interests for a failing CATO project to be delivered by an existing TO through the prevailing RIIO price control arrangements before considering implementation of the CATO OLR mechanism.

7.6 However, there are a number of circumstances where it may be necessary for Ofgem to appoint a CATO OLR to build/operate a project that was chosen for an Early Competition tender:

- The failure of a CATO during construction due to financial distress
- The failure of a CATO during construction due to a significant breach of licence conditions
- The failure of a CATO during operations due to financial distress
- The failure of a CATO during operations due to a significant breach of licence conditions
- CATO awarded the tender decides not to proceed with project construction
- CATO requires amendments to its regulatory arrangements that undermine the integrity of the early competition tender process
- We are unable to appoint a CATO due to failure of Early Competition tender exercise

- End of tender revenue period.

## **Our approach in appointing CATO OLR**

7.7 Given the different circumstances where it may be necessary to appoint a CATO OLR, it is not possible to have an overly prescriptive 'one-size-fits-all' approach. Instead, we intend to set out the principles we will apply when appointing a CATO OLR and the different options we could consider will depend on the project-specific details. For example, a different approach will likely be required where:

- There is no existing CATO (ie tender fails)
- There is a CATO with no assets
- There is a CATO with assets at the end of the Tender Revenue Stream (TRS)
- There is a CATO with assets and an ongoing TRS.

## **Principles for appointing CATO OLR**

7.8 We believe that before employing CATO OLR process, other options for ensuring un-interrupted transmission of electricity should be exhausted, including:

- Engaging with CATO (including its financiers) to resolve issues
- Enforcement action to rectify performance issues and ensuring licence compliance
- Re-tendering the project.

7.9 Approach to appointing CATO OLR will be decided by Ofgem dependent upon circumstances and specific failure of the incumbent CATO.

7.10 The CATO OLR appointed should be the party able to provide the required network services at the lowest cost to consumers.

7.11 The CATO OLR will be appointed in a timely manner in a way that seeks to limit (i) project delays and consumer exposure to constraint cost impact, or (ii) outages/drop in service levels on the transmission network.

### **Options for appointing CATO OLR**

7.12 We consider it more appropriate to retain a range of potential options alongside a CATO OLR process to best reflect the specific circumstances of the project in question. Options include:

1. Ofgem directly appoints an incumbent TO if assets are in its Transmission Area
2. Ofgem directly appoints an incumbent TO to operate assets outside its Transmission Area
3. Ofgem appoints an existing CATO with an existing transmission licence
4. Option to appoint a third-party without a current transmission licence will be left open, for example the Reserve Bidder that was appointed following a competitive tender. However, given the time taken to assess and licence a third-party, appointment of an existing licensee as CATO OLR will be the default option.

### **Valuation and transfer of assets**

7.13 The Electricity System Operator's (ESO) Early Competition Implementation - Update (EC-I Update) assumes a fixed-term revenue period of 35 years (against an asset life of 40 years), with the residual asset value (5/40ths of opening asset value) to be paid in a lump sum at the end of the revenue period. The residual value payment would need to be made from Transmission Network Use of System (TNUoS) charges to avoid the need for the incumbent to raise new finance for the last five years. If the ESO determines that either (i) the assets should be decommissioned, (ii) there's a negotiated extension with the incumbent TO, or (iii) the operation/maintenance of the assets are re-tendered and a new CATO appointed, then there is no requirement to enact a CATO OLR process.

7.14 However, if there is still a network requirement for the assets and the existing CATO is not continuing to maintain/operate them, and it is not possible to re-tender and appoint another CATO, it will be necessary to transfer the assets to a CATO OLR. Since we have the legislative ability to order a Property Transfer Scheme, in the process we will ensure that:

- Assets can be valued at different stages of project development/construction and competition to finish delivering
- Assets can be ring-fenced and transferred

7.15 In a CATO OLR scenario where there is a difference of opinion between Ofgem and the incumbent CATO as to the value of the transmission assets, the terms of a property scheme will be as the CATO OLR and the incumbent CATO agree in the first instance. If they fail to agree, Ofgem will set the terms. Where Ofgem has to set the terms, Ofgem will determine whether compensation should be paid either from the incumbent to the CATO OLR or vice versa.

7.16 Where the CATO has been set up as a Special Purpose Vehicle (SPV), there will need to be a contractual obligation to transfer shares in circumstances where a CATO OLR needs to be appointed.

7.17 As is the case with the current OFTO of Last Resort regime, Ofgem proposes that:<sup>17</sup>

- Incumbent CATO would receive a transfer value reflective of the net asset value after regulatory depreciation (unless such value was negative, in which case the CATO OLR would be the recipient)
- CATO OLR will receive an annual revenue stream sufficient to fund an efficiently operating business and to meet the cost of purchasing the assets (where such cost falls to the CATO OLR).

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<sup>17</sup> OFTO of Last Resort Mechanism, this guidance outlines the steps we would follow prior to initiating an OFTO of Last Resort process, such as proactively engaging with the licensee and funders or other regulatory and statutory options such as Energy Administration. [Guidance on the Offshore Transmission Owner \(OFTO\) of Last Resort Mechanism \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/guidance-on-the-offshore-transmission-owner-of-to-of-last-resort-mechanism)

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7.18 We would welcome stakeholders' feedback on our proposed approach for dealing with CATO/tender failure.

## **8. Conclusion and next steps**

8.1 Following consideration of responses to this consultation, we expect to reach our decision on important policy areas highlighted in this consultation by early summer. We will separately consult on the Electricity System Operator's (ESO) proposed commercial model and the tender regulations we are developing in support of the Early Competition implementation.

8.2 Following the publication of transitional Centralised Strategic Network Plan (tCSNP) by the ESO in March 2024, we aim to identify one project as being suitable for Early Competition by the end of 2024.

## 9. Appendices

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## Appendix 1 – Material costs and benefits considered in ESO proposed CBA

Table 1: List of costs considered in the CBA

<b>Costs</b>	<b>Difference between factual and counterfactual</b>
Pre-tender costs	Costs incurred by the procurement body associated with preparing for a tender under the factual case (e.g., staff time/hire, tender design/calibration).
Tender costs	Costs incurred by the procurement body for running the tender under the factual case (e.g. bid assessment, due diligence, external support fees, commercial negotiation and Post Preliminary Works Cost Assessment (PPWCA)).
Bidder costs	Costs associated with developing bids (e.g. initial design, building bid teams, supplier engagement, surveys) for the successful bidder under the factual case.
Large consortium costs	Costs incurred by the bidder for assembly of large consortium which do not apply to sole or small consortia under the factual case.
Project cost estimate	Under the factual case these are bidder's initial design costs following the PPWCA. These costs are in comparison to the counterfactual cost allowance under RIIO-T2 regime.
Constraint costs	Additional costs incurred by the ESO under the factual case due to the timescales of delivery of the scheme relative to the counterfactual (e.g. these can be driven by varying construction time periods, potential for delay, time to tender, etc.).
Additional system costs	Additional costs incurred by the system operator under the factual case in relation to implementation (e.g. outage requirements), operation (e.g. availability) or existing system reinforcements. This is effectively netted off against any system costs associated with counterfactual delivery.
Financing costs	Under the factual case this is benchmarked cost of debt (i.e. base rate plus margins and any reserve costs (e.g. Lifecycle Reserve Accounts (LRA) or Lifecycle Reserve Facilities (LRF)), cost of equity incurred by the bidder and levels of gearing. Under the counterfactual case this will be the WACC for the relevant regulatory period. The difference in financing costs is driven by the overall WACC achieved.
Contract/ License management	Costs incurred by the procurement body under the factual case, associated with preliminary works stage, PPWCA, performance monitoring, payments, conflict resolution, etc.



Table 1: List of costs considered in the CBA

<b>Costs</b>	<b>Difference between factual and counterfactual</b>
Difference in terminal value	These costs are incurred under both cases to operate assets beyond the revenue period. For example, the counterfactual case may have a RAB at the end of the revenue period when there is no residual value in the factual case. The additional return on the WACC and depreciation in the counterfactual would be post-revenue period cost to consumers which would exist under the counterfactual case and not under the factual case.
Incentives	These are potential additional costs incurred by the procuring body due higher incentives. How incentives are set for the factual case is described in the ECP. Under the counterfactual this would be RIIO incentives mechanisms and rates.
Planning cost	Visual impact of early competition design may involve additional costs for stakeholder management, time in planning process and changes to design under factual case in relation to the counterfactual case.
TO portfolio costs	Under the counterfactual case, incumbents may have lower costs due to economies of scale and scope (e.g. having local operations teams and in-house expertise, avoidance of interface costs). Whereas under factual these could be additional construction or operational costs to meet obligations.
Additional regulatory costs	Additional costs associated with award of network solutions under the factual case including licencing, oversight, monitoring, engagement, reporting etc.
First of a Kind premium	This is applicable to the first few tender rounds as they may not be fully efficient due to lack of precedents, knowledge and higher risks from adopting new delivery route. As the process is repeated bidders and the procuring authority would gain more experience and knowledge and be able to more accurately price and manage risks leading to reductions to the FOAK premium.

Table 2: List of benefits considered in the CBA

<b>Benefits</b>	<b>Difference between factual and counterfactual</b>
Innovative technology, process or system	Benefits from more efficient / innovative technology, processes or systems that could be introduced by bidders under the factual case that is typically not used by the incumbent. This could result in capex or opex efficiency adjustments to the counterfactual project cost estimate.
Access to a wider pool of expertise and capital	Bidders could bring in a wider pool of experience (including international) and capital (including financial instruments) which TOs do not typically use. This could result in a lower cost of equity under the factual case.  Cost of equity would be an input to the model as a cost under the factual and the counterfactual. The benefit would be captured as the delta between these two inputs
Detailed allocation of risk	The use of project finance structures under the factual case will enable detailed allocation of risk which can allow for higher levels of gearing but with potentially higher cost of senior debt compared to notional in counterfactual. This is still likely to mean a net benefit driven by the delta in overall cost of debt and gearing between the factual and counterfactual.
Bidder portfolio effect (economies of scale)	This could appear when the bidders have economies of scale (e.g. a large transmission company with expertise in a particular geography or skills which is new or not accessible by the incumbent TO).
Revenue start point	Under the counterfactual case, consumers bear the cost as expenditure for development of the need begins whereas under the factual revenues for bidders start post commissioning of the asset. This timing difference in cash flow results in a benefit under the factual.
Reduced overrun exposure	Under the factual case, the costs are fixed following a PPWCA so consumers do not pay for additional costs incurred post that stage. Under the counterfactual there is a cost sharing mechanism. This could result in a potential benefit to consumers.
Ecological impact	Consumers could benefit from increased biological and ecological diversity from construction and operation of the asset compared with the solution proposed by the incumbent under the counterfactual case.
Carbon emissions	Consumers could benefit from potentially reduced carbon emissions from construction of the asset proposed under the factual case compared to the counterfactual case.
Social benefits	Consumers could receive social benefits such as job creation or some form of diversity benefit from the factual solution compared to the counterfactual.

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Table 3: How these costs and benefits are classified in the CBA

<b>Classification</b>	<b>Costs</b>	<b>Benefits</b>
Elements that are excluded from the methodology and model. These are not considered relevant for the methodology	Differences in terminal value Incentives Planning costs	Innovation in social benefits Reduced overrun exposure
Elements that are included in methodology but not the model. Impact of these factors on total value for consumers will be assessed qualitatively	Large consortium costs Additional system costs TO portfolio effect	Innovation in ecological impact Reduced carbon emissions Bidder portfolio effect
Elements that are quantifiable and included in the CBA model subject to additional sensitivity analysis.	Project costs Constraint costs Financing costs	Innovation in technology, process and system Access to wider pool of debt and equity capital Detailed allocation of risks
Elements that are included in the CBA model without additional sensitivity analysis.	Pre-tender costs Tender costs Bidder cost First-of-a-kind premium Contract/ License management costs Additional regulatory costs	Revenue starting point

## Appendix 2 – List of ESO proposed qualitative assessment factors

Title	Description
Large consortium costs	Costs involved in assembling and managing large consortia. For very large projects (in excess of £1bn) there is limited market precedent of delivery by sole bidders or small consortia. Lenders typically prefer to lend to projects of this nature in syndicates which typically leads to longer negotiation, more contracts (e.g. intercreditor agreements, ISDAs <sup>14</sup> etc.), increased due diligence etc which would not necessarily exist if there were only a single lender.
Additional system costs	These additional costs range depending on the solution and could include varying system reinforcement costs. The key point for consideration for early competition is whether a different solution would likely drive materially different outcome for additional system costs given the underpinning assumption that the counterfactual and factual solutions are functionally the same.
Bidder portfolio effect	The need being tendered may have characteristics which make it more efficient for the incumbent TO to develop compared with a third party due to economies of scale. The ESO will need to consider feedback from the pre-tender process to assess this factor. If the market is of the view that it is not able to be more efficient than the TO then that need may be less suitable for competition.
Innovation – ecological impact	This factor would depend on whether a bidder is likely to propose a solution which could deliver ecological benefits which the TO's reference design would not. Similar to the portfolio effect factor the ESO will need to rely on feedback from the market in the pre-tender process to inform the assessment for this factor. Additionally, the ESO will need to consider the policy steer from government and Ofgem on what level of weighting ecological impact should have in the tender process.
Innovation – systems, processes and technology	This is a benefit expected to be realised from the introduction of early competition. Whilst some of the benefits from improved systems, process and technology are captured as part of the cost efficiency adjustment, the ESO will need to consider other qualitative benefits such as improved adaptability to future changes, smoother operability etc compared to the solutions proposed by the incumbent. As this benefit is captured under both the qualitative and quantitative analysis caution is needed to ensure that this benefit is not overstated. The ESO should consider the scope for potential innovation versus the benchmarks.

## **Appendix 3 – Privacy notice on consultations**

### **Personal data**

The following explains your rights and gives you the information you are entitled to under the General Data Protection Regulation (GDPR).

Note that this section only refers to your personal data (your name address and anything that could be used to identify you personally) not the content of your response to the consultation.

#### **1. The identity of the controller and contact details of our Data Protection Officer**

The Gas and Electricity Markets Authority is the controller, (for ease of reference, “Ofgem”). The Data Protection Officer can be contacted at [dpo@ofgem.gov.uk](mailto:dpo@ofgem.gov.uk)

#### **2. Why we are collecting your personal data**

Your personal data is being collected as an essential part of the consultation process, so that we can contact you regarding your response and for statistical purposes. We may also use it to contact you about related matters.

#### **3. Our legal basis for processing your personal data**

As a public authority, the GDPR makes provision for Ofgem to process personal data as necessary for the effective performance of a task carried out in the public interest. ie a consultation.

#### **4. With whom we will be sharing your personal data**

We may share consultation responses with the Department for Energy Security and Net Zero. Please note that responses not marked as confidential will be published on our website. Please be mindful of this when including personal details.

#### **5. For how long we will keep your personal data, or criteria used to determine the retention period.**

Your personal data will be held for six months after the project is closed, including subsequent projects or legal proceedings regarding a decision based on this consultation, is closed.

#### **6. Your rights**

The data we are collecting is your personal data, and you have considerable say over what happens to it. You have the right to:

- know how we use your personal data
- access your personal data
- have personal data corrected if it is inaccurate or incomplete
- ask us to delete personal data when we no longer need it
- ask us to restrict how we process your data
- get your data from us and re-use it across other services
- object to certain ways we use your data
- be safeguarded against risks where decisions based on your data are taken entirely automatically
- tell us if we can share your information with 3<sup>rd</sup> parties
- tell us your preferred frequency, content and format of our communications with you
- to lodge a complaint with the independent Information Commissioner (ICO) if you think we are not handling your data fairly or in accordance with the law. You can contact the ICO at <https://ico.org.uk/>, or telephone 0303 123 1113.

**7. Your personal data will not be sent overseas** (Note that this cannot be claimed if using Survey Monkey for the consultation as their servers are in the US. In that case use “the Data you provide directly will be stored by Survey Monkey on their servers in the United States. We have taken all necessary precautions to ensure that your rights in term of data protection will not be compromised by this”.

**8. Your personal data will not be used for any automated decision making.**

**9. Your personal data will be stored in a secure government IT system.** (If using a third party system such as Survey Monkey to gather the data, you will need to state clearly at which point the data will be moved from there to our internal systems.)

**10. More information** For more information on how Ofgem processes your data, click on the link to our “[ofgem privacy promise](#)”.