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Contact  
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By email:

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Dear Jon,

**SP Transmission (SPT): Response to Ofgem's consultation on the onshore electricity transmission Early Competition commercial framework.**

SPT welcome the opportunity to respond to Ofgem's consultation on the onshore electricity transmission Early Competition commercial framework. SPT are the Transmission Owner (TO) for Central and South Scotland, and we work closely with the current National Energy System Operator (NESO) and Ofgem. Currently we support a significant amount of competition on our network, with c.96% of our regulated transmission activities being delivered by the market.<sup>1</sup> We have reviewed the commercial framework consultation and have deep reservations with certain elements and narratives that are prominent throughout. In particular, we are concerned that Ofgem's position on fair treatment between bidders, as well as the need to ensure a level-playing field appears to have been relaxed. We would welcome clarity from Ofgem on all the key concerns we have raised in this response and to consider that it is essential that the competitive process remains fair and transparent for all parties involved.

A summary of our response can be viewed below alongside our detailed comments in response to the consultation questions, which are set out in Annex 1 of this response.

**Summary:**

**Fairness and transparency, ensuring a level-playing field, in the early competition commercial framework is essential.**

We have deep reservations with the current proposals which introduce the narrative that Ofgem and the NESO will be able to treat certain bidders different from others, particularly in terms of preliminary works payments. The consultation does not provide clarity on what criteria must be met to evidence justification for the different treatment of certain bidders. We seek clarity from Ofgem in this regard.

Additionally, we are concerned that allowing for up to 50% of preliminary work costs to be paid by consumers, only for certain bidders, would introduce potential conflicts of interest. It would undermine the competitive tendering process as consumers would have a financial interest in the bidder who received public finances to be the successful bidder. We see this as an unnecessary and

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<sup>1</sup> [https://www.spenergynetworks.co.uk/userfiles/file/Annex\\_18\\_Competition\\_Plan.pdf](https://www.spenergynetworks.co.uk/userfiles/file/Annex_18_Competition_Plan.pdf)

avoidable consumer risk which ultimately jeopardises Ofgem's position to deliver net zero at the lowest cost to consumers.

We are of the opinion that if a bidder is unable to cashflow the preliminary works stage of the process, then that bidder does not belong in the market. We would encourage Ofgem to consider the following points and to provide clarity where possible:

- What costs would be considered as "costs of doing business" and what programme of works will the cashflow be evaluated against?
- Whether there is a marginal rate of return/profit on this early overhead that should be offset by any funding?
- Costs should only be provided where they can demonstrate they will enable progress on the early construction phase aspects of project delivery; not merely as a seed fund for removing a theoretical barrier to enter the market.

**Standard industry practices should be considered in terms of post award securities.**

We encourage Ofgem to provide clarity on the nature of the security, i.e. whether it will be mandatory or subject to commercial negotiation. It is pertinent that Ofgem factors in standard industry practices when determining how the securities will work in practice. We would support the concept of these securities being collateral to a nominated third party, specifically the incumbent TO. This benefit would de-risk concerns around the awarding party not being able to enforce these for any reason.

Please do not hesitate to reach out should you wish to discuss any of the issues raised in this response.

Yours sincerely,

A handwritten signature in black ink, appearing to read "David Boyland".

David Boyland  
*Head of Transmission Regulation and Policy*

## Annex 1 – Responses to Consultation Questions

### Q1 - Do you agree with NESO's proposed approach to a CATO's post-award security obligation?

Generally, we are supportive of this concept to ensure that all aspects of the contract are independently insured, and both the network and end consumer is protected from any financial exposure to either contractual malfeasance or poor performance. However, it is not clear if this security is mandatory or is subject to commercial negotiation i.e. what the market can provide at a reasonable price. For example, SPEN will often require a retention bond of between 10-15% of the total contract price for projects that (i) have innovative technology where a standard or extended warranty period is unavailable or the cost of that is prohibitive/disproportionate, and/or (ii) where there is a strength of covenant concern around the counterparty being able to fulfil future warranty obligations. These are standard commercial practices but equally, are cost components that are paid for. Access to these bonds can be expensive and may also be a barrier to entry.

We would also support the concept of these securities being collateral to a nominated third party, specifically the incumbent TO. This benefit would de-risk concerns around the awarding party not being able to enforce these for any reason.

### Q2 - Do you agree with NESO's proposed approach to preliminary works payments?

We appreciate Ofgem and the NESO's position of having to ensure that there are reduced barriers to entry. However, we do not believe that the current proposals are the most appropriate way to ensure participation in the competitive process. The proposals will allow Ofgem and the NESO to treat certain bidders differently from others. It is unclear from the consultation on what the qualifying criteria would be to allow for Ofgem and the NESO to provide preliminary work payments to a bidder. We would encourage Ofgem to provide clarity on the qualifying criteria for receiving preliminary work payments as well as clarity on the treatment of a TO backed bidding unit or SPV. It should be stressed that whether a TO opts to bid into the process through a bidding unit or an SPV, the barrier to entry will be the same as other non-incumbent TO backed bidders, which is ensured by the extensive conflict mitigation measures placed on TOs to ensure complete separation from the TO's regulated and business as usual (BAU) activities and that of any bidding unit or SPV.

We are also concerned that there will be an apparent conflict of interest considering that public finances will have been used to support preliminary works, albeit capped at 50% of projected costs, to allow for a bidder in this scenario to compete. It erodes stakeholder confidence in the principles of fairness and transparency, while undermining the commitment from Ofgem to ensure a level-playing field between all parties in the competitive process. We view this approach introducing unnecessary consumer risk which could have a material impact on Ofgem's commitment to achieve the delivery of net zero at the lowest cost to consumers.

We would encourage Ofgem to consider the following key points, questions and concerns we have in terms of the commercial framework. In order for the process to be competitive and ensure corporate strength of covenant, we would welcome clarity on what costs would be considered as "costs of doing business" as well as what programme of works the cashflow would be evaluated against. We would further encourage Ofgem to provide clarity on whether there is a marginal rate of return/profit on this early overhead that should be offset by any funding, thereby reducing finance costs? It is essential that costs should only be provided where they can demonstrably enable progress on the early construction phase aspects of project delivery - not as a seed fund to remove a theoretical barrier to enter this market. It is our view that if a bidder is unable to cashflow this phase of the competitive tender, then the bidder does not belong in the market.

### Q3 - Do you agree with NESO's proposed approach to the PPWCA process?

Broadly we agree with this process to the extent that is consistent with the approach for existing licence holders and that indexation is pegged against indices that are well known and understood by large scale construction operations. The concept of "reasonably foreseeable" does seem to be a fair test, but we would question if this concept is sufficiently well defined as a concept to ensure that scope of works that are submitted at the ITT stage provide for sufficient granularity and do not promote an inflated risk premium or allocation of undisclosed provisional sums that could create a work around or inflate price.

Whilst we appreciate the NESOs view of not rewarding further stakeholder activity to inform and shape the ITT, caution is required here to ensure that this does not act as a deterrent for this type of activity which will drive a better quality of tenders and outcomes.

### Q4 - Do you agree with Ofgem's proposed adjustments to NESO's approach?

We have no comment to make on this.

### Q5 - Do you agree with NESO's proposals regarding the payment mechanism and performance incentives to apply to a CATO?

We agree with payment mechanism and performance incentives approach to the extent that they are consistent with the approach to existing licence holders. We are however not clear on the link between performance, specifically availability, and TRS adjustment, and also the cap and floor mechanism that is intended. The revenue model seems to be conglomerate of other revenue regimes and not consistent with the regulatory reward/oversight/penalty regime that other licence holders are subject to. This would appear to confer an advantage to other organisations for which the basis of which (either market lead or consumer protection) is not clear.

In some respects, the approach being taken is innovative, but raises questions on approach, specifically consistency and preferential treatment.

### Q6 - Do you agree with NESO's proposals regarding the additional works obligations?

We consider that a CATO should hold all the equivalent responsibilities, accountabilities and duties that exist for present licence holders, including management of STC responsibilities and compliance with any industry change programmes.

We do not understand the approach on financing additional works and that payment by present consumers for future consumers to receive benefit is a risk. This seems to be an absurdity in that someone will always need to pay for the work to be done.

### Q7 - Do you agree with NESO's proposals regarding the revenue period and end of revenue process?

We have no comment to make on this.