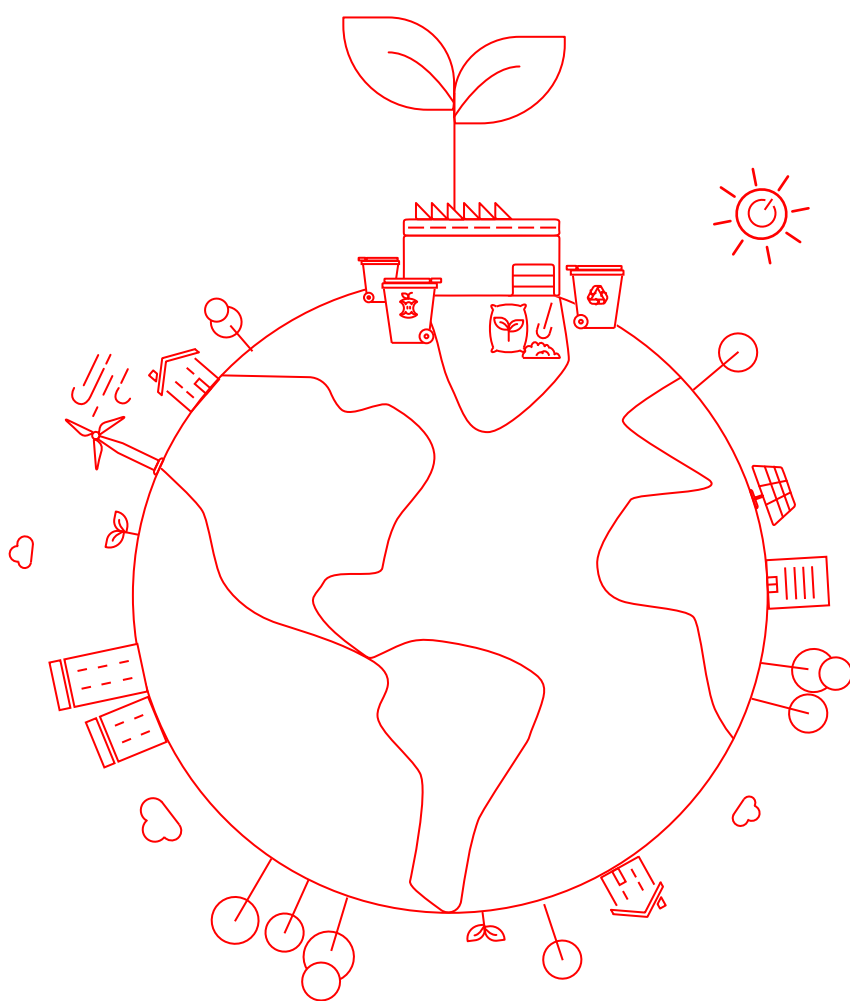




## RESPONSE TO:

### CONSULTATION ON THE ONSHORE ELECTRICITY TRANSMISSION EARLY COMPETITION COMMERCIAL FRAMEWORK



Early Competition commercial framework

**ACCIONA\_ Consultation on commercial framework** [Estado]

02/12/2024

Client:

**ofgem**

Making a positive difference  
for energy consumers

## ABOUT ACCIONA

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**ACCIONA** is a global leader in sustainable infrastructure and renewable energy, with over a century of experience in engineering and construction. The company operates through its two main divisions: **Energy (ACCIONA Energía)** and **Infrastructure (Corporación ACCIONA Infraestructuras)**. Renowned for its commitment to sustainability, ACCIONA has been ranked as the most sustainable company in its sector in Spain and **second globally by the S&P Global Sustainability Yearbook for three consecutive years**.

ACCIONA's infrastructure division, ACCIONA Infraestructuras, includes its investments arm, ACCIONA Concesiones, a global investor in infrastructure and private capital projects. With operations spanning over 40 countries, ACCIONA Concesiones has developed an extensive portfolio in transportation, social and health infrastructure, energy transmission, and sustainable solutions.



*Current portfolio of Transmission projects under execution: +USD 6.9 billion*

In the energy transmission sector, **ACCIONA has over 20 years of experience in financing, designing, and constructing transmission networks and substations of varying scales**. Currently, ACCIONA is executing transmission projects worth **more than USD 6.9 billion worldwide**. ACCIONA's strong financial position, with 2023 revenues of €17 billion and an EBITDA of €2.1 billion, along with its global presence and proven track record, positions the company as a **competitive and reliable partner for the proposed NESO scheme**. With its focus on long-term value creation and alignment with the UK's infrastructure needs, ACCIONA is well-prepared to contribute to the success of this initiative.

# RESPONSES ON CONSULTATION

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## 1. POST-AWARD SECURITY OBLIGATION

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

This type of requirements (i.e bid bond before starting the Preliminary Works) is indeed relatively usual across various regions, including the South American market where **ACCIONA** also has strong presence. But it should be noted that those transmission schemes often benefit from higher levels of certainty in processes such as land acquisition, permitting, and easements, mostly derived from the accumulated experience of decades of these schemes being implemented by the private sector. These factors are also typically supported by previous substantial preparatory work from authorities, contributing to shorter project timelines (from award to commercial operation typically within 35 to 60 months). While NESO's proposal incorporates mitigating measures during the Preliminary Works phase, the combination of the bond requirement and extended timelines represents a less familiar proposition for bidders operating in markets with different structural dynamics such as the UK.

In contexts of greater project complexity, such as our recent (and relatively similar to CATO scheme) experience in Australia, **longer bidding phases** that allow for more comprehensive planning, environmental and social studies, and technical evaluations have proven effective. These extended preparatory stages not only help reduce the risk of significant unforeseen changes during execution but also serve as a robust foundation for selecting a bidder. As a result, even in the rare event that a selected bidder is unable to continue beyond the next phase, the work undertaken during such a detailed bidding process will retain value for the project. This, together with the alignment of interests given by the large amount of costs incurred during bidding and Preliminary Works phases in our opinion guarantees that even without the need of initial securities being in place, the overall impact on stakeholders and the final customer is minimized.

A **stipendiary element** for bidders, particularly in cases where detailed preparatory work is required, is also quite common in similar international schemes. By compensating bidders for part of the upfront effort, such mechanisms **encourage participation**, especially in complex schemes, and ensure that competitive pressure is maintained to deliver value for money. This approach is observed in other markets and has proven effective in achieving robust competition while safeguarding consumer interests.

While we recognize that NESO's approach is designed to address the specific challenges of the UK market, **we believe that extending the pre-tender study phase could provide additional certainty and avoid reliance on large financial securities**. A framework that enables bidders to submit proposals based on well-developed studies could lower the likelihood of project disruptions while maintaining strong consumer protections.

## 2. PRELIMINARY WORKS PAYMENTS

*Q2. Do you agree with NESO's proposed approach to preliminary works payments?*

Ofgem has noted that paying 100% of the estimated preliminary works cost upfront may reduce cost control incentives during this phase. However, in our experience, particularly when the proposal phase is sufficiently detailed, this concern may not be as pronounced. When bidders have already invested significant resources (both financial and human) during the preliminary works phase, their **focus naturally aligns with achieving returns by progressing to commissioning as quickly as possible**. In addition, the opportunity costs incurred by specialist **contractors operating globally, who often have access to less complex and more direct schemes**, further strengthen this alignment of interests.

The combination of these factors (early investment, incurred costs, and the high opportunity cost of participation) serves as a strong incentive for bidders to deliver on their studied plans in a timely manner. In such contexts, the need for capped payments may not have the intended impact, **especially when payments are deducted from the Tender Revenue Stream (TRS) during recalculation**. This could reduce the attractiveness of the framework and may limit competition, ultimately impacting value for money.

As a company accustomed to executing large and complex projects with long timelines and multifaceted challenges, we have a proven track record of delivering successfully in diverse and demanding environments. That said, **companies like ours are generally risk-averse when it comes to exposures that fall outside our direct control**, even when addressed with the highest levels of professionalism and competence. This is a key consideration that we believe should be factored into the proposed framework and may require further discussion in subsequent phases.

As we noted in our response to Q1, while there are markets where the entirety of these costs is borne by the bidder, attracting a sufficient pool of participants, and where **ACCIONA** has operated successfully, the certainty in cost and timelines during this phase is not equivalent to those contexts. For this reason, we emphasize the importance of adopting a framework that shields bidders from risks beyond their control.

We understand, though, that there may be value in schemes that set clear milestones, objectives, and KPIs during the preliminary works phase to ensure that work is being conducted effectively and represents real value to the project. In our view, collaborative frameworks during Preliminary Works phases observed in other countries with similar complexities provide a valid alternative approach. These frameworks align interests effectively without requiring bidders to assume risks that, in certain cases, are beyond their direct control.

### 3. POST PRELIMINARY WORKS COST ASSESSMENT (PPWCA)

*Q3. Do you agree with NESO's proposed approach to the PPWCA process?*

*Q4. Do you agree with Ofgem's proposed adjustments to NESO's approach?*

We appreciate the thoughtfulness in NESO's approach to the PPWCA process, particularly the separation of inflationary effects from design-specific changes. This distinction provides clarity and helps ensure a more transparent recalibration of costs. Additionally, we find the framework around "reasonably unforeseeable" events to be reasonably well-defined. NESO's conclusion that any information discovered by the CATO during the Preliminary Works stage, leading to design changes, can be categorized as "reasonably unforeseeable" appears logical and aligned with practical considerations.

However, we agree with Ofgem that this definition will need further refinement to provide clear guidelines and reduce the risk of misinterpretation. In particular, we support the proposal to evaluate "specific high impact, low probability events" separately. Scenarios such as the need to underground a line or significant rerouting outside the bidder's control should be treated distinctly to avoid undue penalization and ensure that the framework accounts for extraordinary circumstances.

That said, **our main concern lies in the combination of the relatively short selection phase and the concept of the 40% cap itself**, even with provisions to account for individual high-impact events. While the cap is designed to balance risks and incentives, in practice, it may deter bidders from participating or lead to inflated risk premiums in initial bids. This approach could unintentionally limit competition and undermine the framework's objective of achieving value for money for the end customer.

We believe that a reconsideration of the cap mechanism is warranted, especially in combination with an extended pre-tender phase. A longer preparatory phase with more detailed studies could reduce the uncertainty inherent in early-stage bids, thereby decreasing reliance on caps to manage unforeseen costs. This adjustment would enhance bidder confidence and improve the likelihood of robust participation.

### 4. PAYMENT MECHANISM AND PERFORMANCE INCENTIVES

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

**ACCIONA** finds NESO's proposed payment mechanism and performance incentives framework to be generally well-structured and aligned with practices seen in other competitive markets. The inclusion of clear availability targets, performance incentives, and supplementary measures shows a thoughtful approach to driving efficiency and aligning CATOs' interests with those of the end consumer.

## Availability Targets and Incentives

The proposed availability target of 98% appears reasonable as an initial benchmark. Additionally, the incentive to exceed the target availability is a positive element that rewards strong performance and offers an opportunity to recover potential losses from underperformance in other years.

The approach to penalties also appears fair and proportionate. If anything, we anticipate the need for careful consideration of the specific terms and conditions around the potential events of default under exceptional circumstances which, by nature, tend to be out of any reasonable control.

## Deferral Period and Seasonality Adjustments

The deferral period for TRS adjustments during the first year is pragmatic and aligns with the operational realities of new infrastructure. Similarly, the seasonality adjustment mechanism incentivizes planned outages during periods of lower demand, which is reasonable although we would note that clear implementation guidelines will be required to ensure these adjustments support efficient operations without unnecessary constraints.

## Late Delivery

We agree that no financial penalties for late delivery are necessary given the alignment of interests created by the lack of revenue until commissioning.

## Equity Gain Share

The Equity Gain Share mechanism raises some concerns. While we understand the intention to protect consumer interests and ensure a fair distribution of financial benefits, we believe this approach could have unintended consequences for project teams.

CATO consortia will likely consist of multiple partners, each contributing specific expertise and resources. **Limiting potential financial upside through an Equity Gain Share mechanism might discourage participation from some key players.** These measures could make projects less attractive to certain partners, reducing the diversity and strength of consortia. In turn, this might impact the level of innovation and expertise available for these projects, which could ultimately affect value for money for consumers.

Additionally, limiting upside potential changes the risk-reward equation for participants. Complex projects inherently involve significant risks, and the possibility of financial upside is a key motivator for many investors and operators to take on these challenges. Without it, the overall attractiveness of the framework might decrease, limiting competition and participation.

As a company committed to long-term partnerships and delivering high-quality infrastructure, we focus on creating sustainable value in every market we operate in. While we are not driven by short-term financial gains, we believe it is essential to maintain a balanced framework that attracts the best partners and ensures competitive outcomes.

## 5. ADDITIONAL WORKS OBLIGATIONS

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

We find NESO's proposals regarding additional works obligations to be well-considered in principle, but we believe some distinctions are necessary to ensure that such obligations remain practical and deliver value for money at each stage of the project lifecycle.

#### **Pre-Financial Close Changes**

Changes required before financial close are generally reasonable to implement. At this stage, the project is still in a development phase, and adjustments to design or scope can be accommodated without significant disruption or cost escalation. We believe this approach aligns with standard practices in similar markets.

#### **Post-Financial Close Changes**

Changes required after financial close, however, present additional challenges. At this point, project financing and contracting structures are typically locked in, and implementing changes can introduce complexities and potential costs that may not deliver value for money for consumers.

#### **Post-Commissioning Changes**

For changes occurring after commissioning, we believe that the approach should allow for flexibility and align with practices observed in other markets. **Typically, smaller-scale reinforcements or additions are negotiated directly with the incumbent transmission owner.** In these cases, pre-agreed profitability conditions, combined with expert-reviewed proposals for CAPEX and OPEX, allow for efficient negotiation. The transmission owner is often in the best position to deliver these works cost-effectively and on time, but there should be provisions to ensure the system does not add significant risks to either party.

For example, if the transmission owner does not accept the proposed terms for additional works, some frameworks allow for these projects to be competitively tendered to third parties. While the incumbent operator is likely to offer the most efficient service in most cases, this may not always hold true over the 30+ year duration of these contracts.

The proposed use of unit costs plus indexation where the additional works are comparable to the bid design introduces a potential risk given the long-term nature of these contracts. Indexation mechanisms must be carefully calibrated to reflect market realities and ensure that costs remain fair and competitive over time. Additionally, allocating up to 20% of project value for such scale of works through direct awards could be seen as a significant threshold. While this approach can streamline processes for smaller or routine reinforcements, higher-value works may benefit from alternative mechanisms.

## 6. REVENUE PERIOD

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

We agree with NESO's proposals regarding the revenue period and the end of revenue process. The suggested approach is in line with practices observed in other competitive markets and aligns well with ACCIONA's experience and capabilities in delivering and operating projects under similar frameworks.

In most markets where ACCIONA operates, revenue periods typically range between 27 and 30 years.



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