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Dear Ian

**Response to the Open Letter: Update on the Integrated Planning and Regulation Project request for further views and evidence**

We welcome the opportunity to provide further evidence and input on what is needed to ensure that Britain's transmission system planning delivers an integrated transmission system onshore, offshore and cross border, and how the relevant institutions and incentives around them should evolve to support this activity.

As you are aware Drapers Gardens LLP, through our joint venture subsidiaries, Transmission Capital Partners and FAB Link Limited, is one of the few players that either is already involved in or has a desire to be closely involved in all of the overlapping regimes.

Our responses to the open letter questions are set out in the attachment.

We are happy for this response to be made available on the Ofgem website.

Yours sincerely

**Chris Veal**
Managing Director

Issue 1: The obligations and incentives on the multiple parties involved in transmission network planning and delivery may not align to ensure that individual networks or assets develop in line with the overall needs of the system.

***Q1 Do you think that the key issues, as described in the Open Letter, should be considered? What is the materiality of the issues identified?***

The four key issues identified are discussed briefly below:

i) *Operational efficiency*: this is not something that we have direct experience of to date other than through the outage planning process for OFTOs under the STC. Taken together with the availability incentive under the OFTO licence, this process appears to work reasonably well, although on some specific early projects there is an issue with respect to DNO outages that needs to be resolved (and on which we are dealing with Ofgem separately). We understand that there may also be a need for further clarity and definition of how transmission outages that impact upon interconnectors will be treated under the Network Code/Target Model, and we will be analysing this further and will discuss our views with Ofgem in due course.

ii) *Process for obtaining a connection to the onshore GB transmission system*: our experience of this in respect of interconnectors is that, whilst our joint studies with National Grid to determine the optimum design worked reasonably well, the process appears to be ad hoc and lacking definition. There is also a conflict of interest upon which we return to later in our response to Issue 3 below. That aside, we would note that the first come first served approach, under which changes to connection designs are minimised once the connection agreement has been signed, has worked reasonably well for over twenty years and we would caution against a system which may lead to a more optimal network but which causes great uncertainty and possible cost for either generation or interconnector project developers.

iii) *Long-term cooperation frameworks*: we note the concern that the STC is a short-term planning forum and would add that we would consider the ENSG and ETYS as channels through which NETSO and the onshore TOs will promote their vision of the future but not fora that provide for a two-way discussion or testing of the long-term plans. To the extent that a formal framework for planning is required we think that the STC is the most appropriate means to implement it. However we also note that the need for a forum where design decisions by onshore TOs and NETSO can be challenged by other industry participants would be reduced if the conflicts in the current system (see Issue 3 below) were to be removed.

iv) *Access to technical information*: we have not found access to technical information to be a problem to date. In relation to technical information such as harmonic parameters OFTOs and interconnector owners should have the same access rights, and the same confidentiality obligations, as onshore TOs.

In summary, we had not considered the above issues to be the key issues to be resolved by ITPR, and would instead expect the focus to be on Issues 3 and 4 below. We will however, analyse further the implications of transmission outages on interconnector availability.

***Q2 Are there any other issues to be considered in this area?***

We do not have any further points to add in this area.

Issue 2: The framework for GB transmission entities to engage in European transmission activities may not provide an effective means for all relevant parties to contribute, giving rise to a risk that the GB system is insufficiently represented at the European level.

***Q3 How effective are the current arrangements in representing all GB transmission entities' interests within ENTSO-E?***

From our discussions with ENTSO-E we understand that to be eligible to be a member of ENTSO-E, a party must have a 'Control Area' (i.e. must be responsible for system balancing within an area (although we recognise that the Scottish TOs are members, perhaps for historic reasons, even though they do not have Control Areas as such). This implies that as an OFTO we are not, and presumably as an interconnector licensee we would not be, eligible for ENSTO-E membership. We are not privy to how well NGET has represented other GB parties at ENSTO-E, although we see a clear conflict of interest in their role in doing so, for example where interconnectors, which may be developed by National Grid or by other competing interconnector developers, are being discussed for inclusion in the TYNDP. However, we also see that it may not be practical for the UK to have several representatives at ENTSO-E (one for each TO, each OFTO and each Interconnector licensee for example) and we would be satisfied with one party representing all GB parties, so long as it was independent and therefore was not prone to conflicts of interest.

***Q4 How material is the impact of these arrangements on representation of the GB transmission system developments in the TYNDP and other related European activities?***

These are potentially material as inclusion in the TYNDP could have a material bearing on the funding of that project and ultimately whether it proceeds, particularly if it subsequently affects whether a project achieves Project of Common Interest status.

Issue 3: There is a potential for conflicts of interest for parties undertaking transmission planning and delivery.

***Q5 How effective are the current business separation arrangements the transmission entities are subject to?***

Before answering this question we would first like to outline the potential conflicts of interest that could arise with the transmission entities. We summarise these below:

| ***Issue*** | ***Potential conflict*** | ***Parties affected*** |
|---|---|---|
| 1. Offshore network designs | NETSO may be incentivised to promote a design that benefits its affiliated TO.<br><br>(For instance this might involve proposing a design where more assets would be owned by their affiliated TO through monopoly rights, rather than being open to competition) | NGET and E&W TO<br><br>*To the detriment of*<br><br>Competing OFTO bidders |
| 2. Carrying out pre-construction works for offshore connections | If carried out by onshore TO, onshore TO may be incentivised to do it in a way that either: | Onshore TOs & their affiliated OFTOs |

| | | |
|---|---|---|
| | i) favours an affiliated OFTO bidder; or<br>ii) means only that onshore TO can deliver<br><br>(For instance this might involve adopting a technical approach most suited for a supplier with which an affiliated OFTO-bidder has an established relationship) | *To the detriment of*<br><br>Competing OFTO bidders |
| 3. Delivery of major onshore projects | Onshore TOs may be incentivised to accelerate the need for, and commitment to, these projects to prevent a competitive tender being run by Ofgem<br><br>(For example, the TO may argue that there is insufficient time for a competition, or that contracts must be placed before consents are in place). | Onshore TOs<br><br>*To the detriment of*<br><br>Competing ONTO bidders |
| 4. Providing connection offers to interconnectors | NETSO may be incentivised to give preferential connection offers to affiliated interconnector developers compared to competing projects<br><br>(For example giving affiliated interconnector projects access to connection points that allow the use of shorter cables, while competing projects are directed to more distant connection points requiring longer cables). | NETSO, onshore TOs and affiliated interconnector entities<br><br>*To the detriment of*<br><br>Competing Interconnector developers |

Whilst we would consider that existing business separation arrangements for NETSO/onshore TO affiliate OFTO bidders cannot be shown to have been ineffective (as to date no affiliate of these monopoly businesses has successfully competed for an offshore transmission licence), we would consider the business separation between the following are inadequate:

| ***Interface*** | ***Business Separation*** | ***Comment*** |
|---|---|---|
| NETSO v E&W TO | None | Insufficient |
| Onshore TOs and affiliated OFTO bidders | Significant arrangements in place but fall short of ownership unbundling or the level of separation between monopoly-transmission businesses and competitive business seen as appropriate in European legislation (e.g. ITO model). | With common ownership, potential conflict of interest still exists |
| NETSO/onshore TOs v affiliated interconnector developers | Only separate regulatory accounts | Insufficient |

***Q6 How material is the impact of the current arrangements on efficient network development?***

The materiality of the impact is difficult to quantify. However we would note that Ofgem itself has stated that the benefit of competition in the ownership and operation of circa £1.1bn of transitional tender round 1 OFTO projects was circa £300m. We believe that there could be significant savings also in the competitive procurement and construction of transmission and interconnection projects. It seems reasonably conservative therefore to assume that the consumer may benefit from a saving equivalent to 30-40% of capital costs of new transmission and interconnection, where competition can be applied in a transparent and fair way. With potential capital requirements on onshore and offshore transmission and interconnection spend in the region of £20-30bn over the next ten years getting this right is clearly material.

***Q7 Where networks are increasingly integrated, are there other areas where the question of conflicts should be considered?***

There are numerous other examples one could think of and which may arise from time to time. For instance the continued ownership of onshore TOs by companies with generation interests gives rise to concern when these TOs design connections for new generation owned by their parent companies or competitors. Another example would be the way that perceptions of conflict and unfair advantage (whether real or not) can influence investment decisions, discouraging new market entry and persuading foreign developers to partner with the affiliates of incumbent transmission companies in the belief that this will make connection easier.

Issue 4: The regime interfaces for transmission related multiple purpose projects are potentially unclear, giving rise to a lack of clarity around regulatory treatment for these assets.

***Q8 Do you agree that these issues associated with multiple purpose projects should be considered? What is the impact of the issues you identify as relevant? In particular how do they affect multiple purpose projects?***

The onshore transmission, offshore transmission and interconnector regimes were designed for assets that could be classified as falling only into one of those categories at a time. These regulatory regimes are not sufficient for multiple purpose projects which have assets that cross more than one category. The open letter correctly identifies the areas where regulatory frameworks need to be clarified or devised for these multiple purpose projects:

i) Type of licence (and associated licence obligations);
ii) Regulatory treatment – in particular how revenue is regulated;
iii) Access and charging arrangements for users.

In our view interconnectors should be regulated less like generation assets (as they have in the past) and more like transmission assets. We welcome the proposed cap & floor model of revenue regulation that takes interconnectors in this direction, but we also believe it could and should be extended into the other regulatory areas as well. As such an interconnector could:

i) Fall under the STC rather than the CUSC; and
ii) Have a licence obligation to connect users in the same way as an OFTO.

The implications of this would be that users would have the opportunity to apply (to NETSO) for connection to an interconnector, and NETSO could take into account this option in its co-ordination role on the GB transmission system.

We would consider that this form of regulation is a “least change” means of implementing multiple purpose projects as it builds upon codes and processes already used by OFTOs.

Similarly we see the OFTO regime as offering the best approach for the regulation of all types of asset that are physically offshore and not cross-border. Adopting this approach would avoid the complexities that would arise should an offshore asset, initially built outside of the OFTO regime, have renewable generation connected to it – an action that we understand would otherwise require a switch to the OFTO regime.

***Q9 Do the issues capture all the potential regulatory barriers? Are there any other issues to be considered in this area?***

There are regulatory constraints that derive from European Union regulations that need to be taken into account, in particular the apparent conflict between the Renewables Directive which requires priority access for renewables and other European legislation which requires access onto interconnectors to be non-discriminatory. We have been in discussion with the European Commission on a model that resolves this apparent conflict and are pleased to have received a letter agreeing to our proposed solution.

We intend to work up our proposed solution to the issues outlined under Issue 4 in some detail, taking into account the agreement we have had from the European Commission, and present shortly to Ofgem a model for consideration that we believe would allow these multiple purpose projects to proceed.

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