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Dear Jon,

**The regulation of future interconnection: Proposal to roll out a cap and floor regime to near-term projects.  
Response from The Crown Estate**

Thank you for the opportunity to respond to the consultation on the proposed roll out of a cap and floor approach to near-term interconnector projects, published on 23 May 2014. The Crown Estate (TCE) welcomes this consultation given the anticipated increase in interconnector projects coming forward over the next decade or so, and the need to have certainty over the regulatory framework that would apply. We hope our response is helpful in refining your policy in this area.

**The Crown Estate**

The diverse portfolio of TCE comprises marine, rural and urban properties across the whole of the United Kingdom, valued in total at almost £10 billion. Under the 1961 Crown Estate Act, TCE is charged with maintaining and enhancing both the value of the property and the revenue from it consistent with the requirements of good management. We are a commercial organisation guided by our core values of commercialism, integrity and stewardship. Our entire revenue surplus is paid directly to HM Treasury for the benefit of UK citizens; in 2013/14 this amounted to over £267 million.

Our energy and infrastructure portfolio comprises virtually the entire UK seabed out to the 12 nautical mile territorial limit, in addition to the sovereign rights to explore and make use of the natural resources of the UK continental shelf, with the exception of oil, coal and gas. We also own around half of the foreshore and beds of estuaries and tidal rivers in the United Kingdom. Our expertise includes marine resource management (e.g. marine aggregate extraction, marine renewable energy installations, seabed infrastructure, aquaculture and new activities such as gas storage and carbon capture and storage) and its interplay with other marine activities such as defence, energy, navigation and marine safety. We have a strong understanding of the needs of a broad range of coastal and sea users, as commercial partners, customers and stakeholders.

**Overview comments**

We welcome and support Ofgem's proposal to roll out a cap and floor regulatory regime for near-term interconnector projects. Given only a limited volume of interconnector capacity has been delivered in recent years in GB, we see any move to unlock future investment for activity on the UK seabed as a positive development. As you are aware, TCE has an interest in the development of future interconnectors given our

role regarding the seabed, both in terms of spatial planning and also agreeing appropriate rights to undertake works out to the 12 nautical mile limit of the UK territorial waters. This is reflected to some extent in the table in Appendix 2 of the consultation document, which notes that TCE rental payments would be treated as a 'non-controllable cost'. As you may also be aware, we are currently considering our licensing arrangements and the commercial terms of our agreements for interconnectors (and also non-GB renewable energy import projects). This includes in terms of factors impacting on the value of such projects. The final form of the regulatory frameworks will likely be an input into decision-making in these areas. As such, we have an inherent interest in the outcomes of your work and we welcome the clarity that the consultation provides on future direction for the regulation of interconnectors.

In addition to confirming our interest, we also offer feedback on some of the questions raised in the consultation. We trust that you find these constructive, and we are happy to discuss further as required.

### **Response on issues raised**

#### Question 1: Do you agree that making the developer-led cap and floor regime available to near term projects would be in GB consumers' interests?

TCE welcomes the proposal to facilitate new investment in electricity interconnection. This is an important part of the overall GB energy system and is expected to become more so going forward, particularly from a system balancing and security of supply perspective as we see an increasing volume of renewables connected to the transmission system (such as offshore wind).

We note that recent reports from both DECC<sup>1</sup> and National Grid<sup>2</sup> identify potentially significant benefits to consumers from increased levels of interconnection, largely in terms of reducing electricity wholesale prices and improving security of supply. Whilst we understand there is uncertainty around deployment and therefore the precise level of benefits that could accrue, there appears to be a broad consensus emerging from these and other sources that increased levels of electricity interconnection should improve the net welfare position of GB consumers. On this basis, putting in place regulatory arrangements that both stimulates investment in new interconnector capacity and also retains incentives on efficient cost management is a welcome policy response.

#### Question 2: What are your views on the cap and floor regime design?

Given the design of the cap and floor regime set out in the document is based on the model being adopted for the Nemo project, we see no reason why the same overarching principles cannot be applied to other

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<sup>1</sup> DECC's report 'More interconnection: improving energy security and lowering bills' (December 2013) identified the potential for up to £9 billion (in NPV terms) of potential benefits from increased interconnection by 2040, under certain scenarios.

<sup>2</sup> National Grid's report 'Getting more connected: the opportunity from greater interconnection' (March 2014) suggested wholesale power prices could fall by 1-2% for each 1GW of new interconnector capacity brought online, and this could unlock up to £1 billion of benefit to consumers per year to 2020, assuming 4-5GW of new links coming forward.

projects as well. However, we do want to raise two specific points for further consideration in the detailed design:

- We note the comment in section 1 of the document regarding the interaction of the current proposals with the development of long term regulatory arrangements for transmission network development under the ITPR project. We would ask that in the application of the cap and floor regime to any particular project, it does not rule out the possibility for offshore generation projects to connect into the interconnector infrastructure in the future. We agree that further work is required on the practicality of this (not least from commercial and technical perspectives) and that such 'multiple purpose' projects are appropriately explored through the ITPR project. However, given the timescales over which the cap and floor regime may apply, it would seem prudent to build in optionality now to enable connections like this if they were beneficial to consumers and/or developers in the future.
- We note the intent to assess outturn revenues against the cap and floor every five years, and we understand the rationale for this. In refining the detailed design of the regime, we would ask Ofgem to consider inserting a provision within licences for interconnector developers to report out-turn revenue (and its component parts) on an annual basis, and for this to be published. This would be consistent with the approach for other network licensees<sup>3</sup> and improve the overall transparency of the performance of the regime for wider stakeholders outside of the five-year assessment period.

Question 4: Where do you think we may need to be flexible to accommodate the specifics of different projects and other national approaches?

Given interconnector projects will likely have different commercial drivers, technical requirements and regulatory arrangements (reflecting different national circumstances), we agree it will be important for Ofgem to retain sufficient flexibility in its approach. As per our comment above, we would like to see Ofgem retain specific flexibility within the regime to incorporate potential multiple purpose projects, which could appear over the timeframe within which these arrangements would apply (i.e. for projects connecting up to 2020).

Question 9: What are your views on the need for and timing of future windows?

The need for future windows should be driven by the requirements of projects and we suggest Ofgem retains sufficient flexibility to undertake further reviews as required, depending on projects coming forward.

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<sup>3</sup> For example the publication of the OFTO Revenue Report in December 2013, which could be replicated for interconnectors regulated under a cap and floor model.

Question 11: What are your views regarding the next steps?

We would ask Ofgem to confirm its position as soon as is practicable to enable projects to move forward with certainty around the applicable regulatory framework. It is encouraging to see that the implementation of the proposed regime would not need legislative change and therefore could be introduced quickly.

**Closing remarks**

We trust that you find our comments constructive in refining your policy positions. As you will be aware, we have been actively engaged in dialogue with Ofgem on interconnectors, non-GB renewable energy import projects and the related ITPR project over the past 12-18 months. We look forward to continuing this engagement as you move toward conclusions in these areas.

If you have any questions on our response, please contact my colleague Richard Clay on 020 7851 5336 or [richard.clay@thecrownestate.co.uk](mailto:richard.clay@thecrownestate.co.uk) in the first instance.

Yours sincerely,



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