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10 July 2015

Dear Cathryn,

**Re: Criteria for onshore transmission competitive tendering**

I am writing on behalf of Scottish Hydro Electric Transmission plc (SHE Transmission) regarding the above consultation. In line with our previous responses to the work undertaken as part of the Integrated Transmission Planning and Regulation (ITPR) workstream, we do not oppose the introduction of competition to onshore transmission. However, it is our view that any significant regulatory development of this nature delivers meaningful benefit to consumers and that the regime introduced is robust, workable and developed in conjunction with those industry parties most likely to be affected. To that end, we appreciate the opportunity to respond to Ofgem's latest thinking on the proposed criteria and are willing to work with Ofgem and DECC on the further steps needed to demonstrate that the proposed benefits are achievable and can be realised.

The consultation letter poses a number of direct questions. Our response to these is provided in Appendix 1. As discussed with members of Ofgem's Transmission Competition Policy team, there are three areas that we believe merit further consideration. Our views on these matters are set out on the following pages and summarised below. We welcome further discussion with yourself and the team on these points.

Our key concerns are as follows:

1. the treatment of Projects currently in Advanced Development such as the Scottish Islands' Links;
  - a. any delay to delivering these projects could impact on the viability of the developers' projects that they are responding to;
  - b. our analysis suggests a potential delay of at least 24 months;
2. the proposed High Value Threshold;
  - a. for the remainder of RIIO-T1, using a £100million threshold could be considered discriminatory;
  - b. more generally, we remain unconvinced that sufficient benefits will be realised at a £100million threshold;
3. the suggestion of potential Asset Transfer;
  - a. we do not believe this is necessary to ensure competition in onshore transmission is effective;
  - b. importantly, we do not believe Ofgem has the powers to require the transfer of assets from an existing owner to a third party.

### **The treatment of Projects currently in Advanced Development**

We acknowledge and welcome the statement within the consultation letter that the decision regarding whether or not specific RIIO-T1 Strategic Wider Works (SWW) projects are tendered will be made by Ofgem following consideration of their needs cases. Based on discussions to date, it is our understanding that this includes the two projects to provide transmission links to Scottish Islands, namely the Shetland Link and the Western Isles Link. It is our view that these projects are too far developed to make them suitable for competitive delivery. We will provide further information on this within our Needs Cases, to be submitted in Q3 2015/16, but highlight our key concerns below.

As you are aware, the delivery dates for these projects are determined by the need of developers whose generation projects are awaiting connection to the transmission system. We believe the works programmes to meet these dates are challenging but achievable. We are very concerned that any potential delay from the introduction of a competitive regime could impact on the viability of these projects. Our initial analysis indicates that tendering these specific projects could introduce a delay of at least 24 months, although, from our discussions with developers, we are aware that there are concerns that this could be significantly longer with consequential impacts to their projects. This would take the delivery date well beyond what has been agreed with these developers and we do not believe this is appropriate or acceptable.

In order to meet our delivery date for these projects, we have and will continue to enter into all relevant agreements to deliver these works. Our estimate of potential delay assumes that all of these agreements could be transferred to a third party. However, we do not believe that all of these agreements can be transferred as a matter of course and discuss this further in response to Question 3 (see Appendix 1). This is likely to further impact on any delay.

We have already provided Ofgem with our high level programme to deliver these projects and this will be set out in detail in our Needs Cases. In the meantime, we welcome further discussion with you and the team on this matter.

### **The proposed High Value Threshold**

We note that Ofgem is currently proposing a requirement for £100million of capital expenditure as the threshold for determining whether a project is suitable for further consideration for competitive delivery. However, only projects funded under the SWW mechanism will be considered during the RIIO-T1 period. This presents two concerns for us: firstly, that this level has the potential to be considered discriminatory for the remainder of the RIIO-T1 period as it will result in different treatment of projects in Scotland compared to the remainder of Great Britain (GB) and, secondly, that the transactional costs associated with tendering projects at this level may outweigh any potential benefits arising from the introduction of competition.

As a consequence of the different thresholds set for the SWW mechanism, the proposal to set the high value threshold this way has the effect of creating different thresholds between Scotland and the remainder of GB which we believe has the potential to be discriminatory. Our SWW threshold was proposed by us as part of our Business Plan and sought to balance the risk and uncertainty associated with delivering large projects, where the timing and value was uncertain at the time of developing the Business Plan, whilst ensuring the financeability of SHE Transmission during a range

of potential outturn scenarios for the RIIO-T1 period. There was no consideration of the appropriateness of this level for setting a threshold for competitive delivery at this time.

Given the differences in scale of the three transmission licensees, a higher threshold was set for SWW in England and Wales, with a further uncertainty mechanism (Incremental Wider Works) used to trigger additional allowances for projects below £500million (09/10 prices). As a result, Ofgem's proposal means that works in Scotland valued between £100 and £500million could be subject to competition, whereas an identical project in England and Wales would not be. In our view, this could be considered discriminatory.

The first mention of the potential for SWW projects to be competitively tendered was published on the day we submitted our revised Business Plan<sup>1</sup>. Prior to this, Ofgem's documentation had indicated that competition would be used in RIIO-T1 only where Ofgem had concerns that a project was not delivering value for money for consumers. A timeline of relevant excerpts is provided in Appendix 2.

In our Final Proposals for RIIO-T1, Ofgem stated "We will aim to ensure that a company who is fast-tracked does not secure a settlement that means it is worse off than if it had remained in the price control process."<sup>2</sup> Transmission Owners (TOs) who remained in the price control had the opportunity to factor in this publication on competition to their proposals. However, this opportunity was not available to the fast-tracked licensees. As such, to use the SWW thresholds in the manner proposed goes against Ofgem's stated principle.

We recognise that, without unpicking the price controls further (which would significantly undermine the principle of regulatory certainty), SWW are the only projects where Ofgem can look to introduce competition during the RIIO-T1 period. However, this can be considered an 'accident of history' rather than a conscious regulatory development and it is essential for the credibility of the regime that the criteria introduced to determine the suitability of projects for competitive delivery is more robust than an accidental threshold, introduced into the price control settlement for different reasons.

In the March Impact Assessment, Ofgem acknowledged "the difficulties and uncertainties involved in trying to quantitatively predict the costs and benefits of introducing competitive delivery in new areas."<sup>3</sup> This significant uncertainty around the potential costs associated with competitive delivery suggests that, at least in this instance, a higher threshold is likely to ensure maximum consumer benefit for lower cost. We have undertaken some basic sensitivity analysis on the Bidder Costs within Ofgem's Impact Assessment as published in March 2015 that implies cost savings in the order of 9% may be necessary if only a single £100million project is tendered. More detail is provided in response to Question 2 (see Appendix 1).

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<sup>1</sup> Ofgem, 'RIIO-T1: Competition in Onshore Electricity Transmission', December 2011

<sup>2</sup> Ofgem, 'RIIO-T1: Final Proposals for SP Transmission Ltd and Scottish Hydro Electric Transmission Ltd', April 2012, para 1.9

<sup>3</sup> Ofgem, 'ITPR final conclusions: Impact Assessment', March 2015, para 3.4

One approach that merits further consideration is to break the high value threshold into two parts: firstly, use the high value threshold as an initial indicator that a given project may be suitable for competitive delivery; and secondly, run a full Impact Assessment to justify that the project in question has the potential to result in the benefits from competitive delivery that Ofgem expects. Notwithstanding this, we continue to believe that a more robust Impact Assessment than that carried out in March 2015 is required to justify the expected benefits of moving to competitive delivery for onshore transmission assets.

In addition, we suggest that an approach which tests the potential benefits on a case-by-case basis may lead to a more meaningful assessment of the likely costs and benefits of the regime and therefore provide a more appropriate justification of whether or not it is appropriate to tender a given project, rather than just a simplistic consideration of a project's capex requirement.

### **The suggestion of potential Asset Transfer**

We were surprised to read within the open consultation letter that Ofgem are considering potential Asset Transfer. We believe that as a general principle, new should mean 'new' with only works to install new assets being subject to competitive delivery. Any works required on existing assets should be undertaken by the existing TO.

Neither the Consultation document nor Jacobs' report sets out the basis under which Ofgem would have the powers to require the transfer of assets from the existing owner to a third party and we do not believe that Ofgem currently has this ability under its statutory powers. As importantly, we do not believe it is necessary.

The discussions at the Ofgem-hosted workshop on 12 February 2015 indicated to us that there was no appetite, either from potential CATOs or the existing TOs for this, and this is noted in Jacobs' summary of the meeting<sup>4</sup>. As a party interested in the potential to compete more widely within GB, we would be very concerned about any requirement to take on another party's assets, especially if they were aged or there was limited information available on the asset condition. Jacobs also state its own view that "transferring ownership from an existing regulated party would be complex and lead to potential uncertainty."<sup>5</sup>

As discussed with members of Ofgem's team, Figure 1 in the consultation document is unhelpful as it appears to suggest that up to 25% of an existing TO's assets could be transferred. Having reviewed the consultation letter and the Jacobs' report, we do not believe this is the intention and suggest that two matters are being confused here. It is our understanding that the percentage referred to relates to what proportion of a project costs could be for work on existing assets before it is considered to be outwith the new and separable criteria. We do not believe that this should be combined with whether or not it is appropriate to transfer assets.

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<sup>4</sup> "A clear view emerging from the workshop was that the transfer of assets, while possible, would lead to increasing complexity, particularly the transfer of older existing assets." Jacobs, 'Technical Report on Enabling Competition', May 2015, p.12

<sup>5</sup> Ibid, p.7

Further, we do not believe that the proportion of costs on existing assets should be as high as the suggested 25% and discuss this further in our response to Question 3 (see Appendix 1). More importantly, we do not believe that any asset transfer is required to give effect to competitive delivery of a project that includes both new and existing assets. We suggest that there are enough examples of existing arrangements that render this proposal unnecessary. One such example is if licensees see merit in transferring an asset to simplify a particularly complex project then this can already be achieved, with Ofgem agreement, under the Disposal of Assets licence condition. Alternatively, introducing an isolation point between TO and CATO assets may achieve the desired outcome with less cost or complexity involved than would be triggered from introducing an asset transfer requirement.

In our opinion, this is one aspect of the proposals where there are significant differences between the existing arrangements offshore and what may be practical onshore. The offshore regime has been developed with specific intent to tender new transmission assets, purchased and installed solely for the purpose of creating that part of the offshore transmission network, within a matter of months of commissioning. This is clearly understood by all involved parties, allowing for appropriate assessment of the risks associated with this. Any potential transfer of existing, and potentially aged assets, has a significantly different risk profile that cannot be standardised and will therefore require significant and costly work to be undertaken to facilitate any transfer. This additional work will impact the benefits Ofgem is seeking to realise and yet has not been factored in to the Impact Assessment.

We hope that this response will be useful and are happy to discuss any of the points raised in further detail. Please contact me on the details above. We also remain committed to working with Ofgem, DECC and other industry parties to develop the regime further over the coming months.

Yours sincerely,

Jen Carter  
**Networks Regulation, Transmission**

## Appendix 1: Response to Consultation Questions

### Qu 1: What are your views on the analysis and conclusions in Jacobs' report?

We have reviewed the Jacobs' report with considerable interest. Our main observations in respect of Jacobs "Summary of Recommendations" in chapter 5 are as follows:

The "New" criterion:	We do not agree that an allowance for up to 25% of non-new content is appropriate.
The Separable criterion:	The recommendations are reasonable and correctly recognise that any additional assets included for separability should require to be justified in detail.
The High value criterion:	Capex, rather than whole life cost, is a more appropriate quantity for expression of a high-value threshold criterion.
"General" recommendations:	We agree that any package of works should be restricted to the smallest indivisible package of works, i.e. all element or none at all. Given the acknowledgement that the existing owner is typically best placed to undertake upgrade or refurbishment of existing assets, no asset transfer should be necessary.

#### The "New" criterion

In both its own deliberations and in its description of discussions at the workshop in February, the report captures the linked nature of the "new" and "separable" criteria. It also recognises that some reinforcements and developments may include an element of refurbishment and re-use of existing assets.

The report appropriately concludes that, "the existing asset owner is likely to be best placed to undertake any upgrade or refurbishment works required on existing assets." Existing third party works arrangements already provide the technical and commercial framework for such work, which is likely to be undertaken on significantly less than 25% of any total project costs.

Furthermore, we do not consider it appropriate or necessary to transfer assets for the purposes of refurbishment and re-use.

#### The "Separate" criterion

Page 12 of the report notes that, "No attendees expressed any significant concerns with transfer of an existing route corridor (i.e. land) provided it did not include physical assets, e.g. towers". This was not SHE Transmission's position. In line with correspondence previously provided to Ofgem, the majority of our route corridors are secured on voluntary wayleaves. Under Scots law, these are personal rights and, as such, can not generally be transferred to a third party.

We do, generally, agree with the recognition that any commercial requirement for separability should not drive additional unnecessary asset provision.

### **The “High value” criterion**

Whole life costs are entirely appropriate for evaluation of project costs and comparison of projects. They are not however appropriate as a quantity in which a high value threshold could be expressed. The justification for a sufficiently high value threshold is that the transaction costs must be at least covered. Since transaction costs and financing is most closely related to capital cost, Capex, rather than whole life cost, is a more appropriate quantity for expression of a high-value threshold criterion.

### **“General” recommendations**

Asset transfer recurs as a theme and concern for existing owners as well as for prospective CATOs. However, SHE Transmission believes that no asset transfers should be necessary. As described under discussion of “new”, any refurbishment of existing assets can be undertaken by existing owners under existing third party works provision without any need for transfer of assets.

### **Qu 2: What are your views on using £100m as the high value threshold?**

As set out above, we firmly believe that it is inappropriate to set the high value threshold at £100million for the remainder of the RIIO-T1 period as we believe that this could be considered discriminatory. We are also unconvinced that this is an appropriate threshold on an enduring basis as we do not believe the benefits to consumers at this level will outweigh the transactional costs associated with tendering projects. Our views are provided in relation to the remainder of the RIIO-T1 period and on an enduring basis.

### RIIO-T1

As a consequence of the different thresholds set for the SWW mechanism, the proposal to set the high value threshold this way has the effect of creating different thresholds between Scotland and the remainder of GB which we believe has the potential to be considered discriminatory. Our SWW threshold was proposed by us as part of our Business Plan and sought to balance the risk and uncertainty associated with delivering large projects, where the timing and value was uncertain at the time of developing the Business Plan, whilst ensuring the financeability of SHE Transmission during a range of potential outturn scenarios for the RIIO-T1 period. There was no consideration of the appropriateness of this level for setting a threshold for competitive delivery at this time.

The first mention of the potential for SWW projects to be competitively tendered was published on the day we submitted our revised Business Plan. Prior to this, Ofgem’s documentation had indicated that competition would be used in RIIO-T1 only where Ofgem had concerns that a project was not delivering value for money for consumers. A timeline of relevant excerpts is provided in Appendix 2.

Given the differences in scale of the three transmission licensees, a higher threshold was set for SWW in England and Wales, with a further uncertainty mechanism (Incremental Wider Works) used to trigger additional allowances for projects below £500million (09/10 prices). As a result, Ofgem’s proposal means that works in Scotland valued between £100 and £500million could be subject to competition, whereas an identical project in England and Wales would not be. In our view, this could be considered discriminatory.



### Enduring basis

We are concerned that the benefits that Ofgem expects to realise on a project below this level are unachievable and the transactional costs associated with running a tender process are likely to outweigh the potential benefit. To this end, we do not believe it is appropriate to set the threshold at £100million level and suggest that further work is required to test the assumptions within the Impact Assessment to determine an appropriate threshold. The standardised nature of the offshore regime is likely to lend itself to a lower threshold than the proposals for onshore as the onshore regime will require a greater level of bespoke, case-by-case work, by Ofgem, its consultants, potential bidders and any other affected parties, including existing TOs.

Ofgem's Impact Assessment published in March 2015 contains a scenario analysis based on tendering projects with an average capital cost of £500million and notes that at this level savings in the region of 3.15-3.6% are required for competitive delivery to 'break-even,' excluding the costs that have not been quantified in this assessment. In the event that only a single project at the £100million threshold is tendered, savings of at least 6% are required to 'break-even'. Included in this assessment is an assumption that Bidder Costs will achieve a long-term average of 2% of capital cost. This assumption may be reasonable in the event that multiple tenders are run for relatively standardised projects, such as seen in the offshore transmission regime where projects are delivering a point-to-point connection. However, the bespoke nature of onshore transmission development to meet system needs suggests that it is unlikely that a long-term average of this level is achievable for onshore competition as the work required by a Bidder will vary substantially depending on the project in question.

To this end, we have undertaken some basic sensitivity analysis. In the event that Bidder costs are 3% of capital costs, the savings that will need to realise vary from 3.35% for four projects totalling £2billion to 7% if only a single project at £100million is tendered. If Bidder costs are 5%, which seems more realistic, at least for initial tenders, then the savings that will need to realise vary from 5.35% for four projects totalling £2billion to 9% if only a single project at £100million is tendered.

In the March Impact Assessment, Ofgem acknowledged "the difficulties and uncertainties involved in trying to quantitatively predict the costs and benefits of introducing competitive delivery in new areas.<sup>6</sup>" This significant uncertainty around the potential costs associated with competitive delivery suggests that, at least in this instance, a higher threshold is likely to ensure maximum consumer benefit for lower cost.

One approach that merits further consideration is to break the high value threshold into two parts: firstly, use the high value threshold as an initial indicator that a given project may be suitable for competitive delivery; and secondly, run a full Impact Assessment to justify that the project in question has the potential to result in the benefits from competitive delivery that Ofgem expects. Notwithstanding this, we continue to believe that a more robust Impact Assessment than that carried out in March 2015 is required to justify the expected benefits of moving to competitive delivery for onshore transmission assets.

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<sup>6</sup> Ofgem, 'ITPR final conclusions: Impact Assessment', March 2015, para 3.4



In addition, we suggest that an approach which tests the potential benefits on a case-by-case basis may lead to a more meaningful assessment of the likely costs and benefits of the regime and therefore provide a more appropriate justification of whether or not it is appropriate to tender a given project, rather than just a simplistic consideration of a project's capex requirement.

**Should this be whole life or capex?**

We believe that the high value threshold should be set on a capex basis as whole life costs are unlikely to be available at the time the System Operator is recommending to Ofgem which projects may be suitable for tendering. However, we believe there may be merit in a whole life assessment when comparing different tender submissions as this will allow for different solutions to be assessed on an equal basis.

**Qu 3: What are your views on defining new and separable? Are our principles clear? In your view, do they appropriately capture projects where competitive tendering would bring value to consumers? If not, please explain and suggest how we can improve them.**

As a general principle, we believe that new should mean new, with only works to install new assets being subject to competitive delivery. Any works required on existing assets should be undertaken by the existing TO. To that end, we agree with the proposal that investments should only be considered where:

- transmission assets don't currently exist (ie 'greenfield'), or where new transmission assets will completely replace existing ones; and
- ownership boundaries can be clearly delineated in industry codes and standards, so that it is clear who is responsible for each asset.

However, we do slightly disagree with Ofgem's point describing how these principles should be interpreted. Where appropriate and where the necessary consents and permissions can be agreed, we can and do reuse land and route corridors but this may not be so straightforward to transfer as the consultation indicates. As per previous correspondence<sup>7</sup>, the transfer of wayleaves in Scotland is problematic as these are personal rights and cannot readily be transferred to a third party. A further example is where existing contracts have options for future project delivery, agreed at the time to minimise future costs, where transfer of the option would be problematic and add potential delays to the overall programme. Whilst these examples do not in themselves preclude the projects being tendered, they do make this more challenging than the consultation suggests.

In addition, we understand that Ofgem is seeking to ensure projects are captured where the majority of the work is on 'substantially new' assets. However, we cannot agree with the suggestion that 75% constitutes substantial assets. Having reviewed the Jacobs' report, we cannot see any justification for the use of this arbitrary level and suggest it is far too low; it implies a project could be put out to competitive tender at £75million which, we believe, would not realise savings to consumers.

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<sup>7</sup> Letter from Jen Carter (SHE Transmission) to Gordon Hutcheson (Ofgem), dated 12 June 2015

**Qu 4: What are your views on the importance of electrical separability and electrical contiguity, including on the alternative approaches for considering electrical separability?**

In our view, it is the ability to define ownership boundaries, rather than electrical separability or contiguity, which is of greatest note here. There is sufficient precedent for the funding and delivery of projects that involved multiple licensees that do not require the introduction of means to separate assets. Examples that we have direct experience of include Beaully-Denny, Kintyre-Hunterston and third party works. In all of these examples, the ownership boundaries are clearly defined and adherence to the requirements of the Grid Code, industry standards, integration arrangements and affected parties' rights ensure that all those involved are required to consider the potential affect of their assets on the wider system and to act accordingly.

Whilst there may be some additional costs for a successful bidder in operating assets that are not electrically contiguous, that should be a factor that informs the bid and should not preclude works from being considered for competitive delivery. However, as set out in our response to Question 5 below, we would only expect works that are not electrically contiguous to be included within a package of works where they are required to meet the identified need.

**Qu 5: In thinking about how to apply the criteria, what should be taken into account when establishing different packages of works to address a given need?**

Based on our experience through the SWW process to date and in developing our projects, it is our view that the least worst regrets analysis that is undertaken to justify SWW projects generally drives the development of projects so they consist of the smallest amount of works to meet the identified need. Whilst this may be multiple elements, potentially dispersed over a given region of the network, they will represent a complete and justifiable solution to meet that given need.

In order to allow for the greatest scope for competition and innovation, it is our view that competing bidders should be able to identify the extent of works that they see fit with appropriate justification of how these meet the identified need. As such, we believe this may need to be considered on a case-by-case basis determined by the need in question and the range of potential options that could meet that need.

**Qu 6: What are your views on the three approaches we suggest for applying the criteria? Are there other options for applying the criteria that we should consider?**

Of the three approaches outlined, we believe Approach 2 is the most appropriate. This approach balances the need for transparency and simplicity, whilst ensuring alternative means for delivering works are considered.

- **Approach 1**

In our view, Approach 1 offers the most straightforward solution as it is transparent; straightforward; and minimises the potential for subjectivity. However, we can understand the concern that it may be too restrictive in some circumstances.

- **Approach 2**

On balance, we believe Approach 2 is the most appropriate. This approach has the potential to realise any benefits from the introduction of competitive delivery, whilst minimising the risks and costs associated with any potential asset transfer. It is also more in line with Jacobs' recommendation that "The existing asset owner is likely to be best placed to undertake any upgrade or refurbishment works required on existing assets."<sup>8</sup>

- **Approach 3**

In relation to Approach 3, and as set out in our covering letter and in response to Question 7 below, we strongly disagree with suggestions that Asset Transfer may be an appropriate approach.

**Qu 7: Are there any additional considerations that should be taken into account in relation to the new, separable and high value criteria?**

As set out in our covering letter, we are very concerned by the suggestion that Asset Transfer may be required, albeit in limited circumstances, to give effect to Ofgem's proposals. We do not think this is necessary and do not believe Ofgem has the powers to do this. In the event that any concerns are raised, either by the existing TO or the newly appointed CATO, then these could be addressed on the basis of the specific point/s rather than being resolvable in the overall regime design. The possibility that assets developed by a CATO could be subject to transfer as part of future tender has the potential to make transmission investment a riskier proposition. This could result in investors looking for a higher rate of return than might otherwise be required and erode the potential benefits to consumers.

Any works required on existing assets should be undertaken by the existing TO. This aligns with Jacobs' recommendation that "...asset transfer should be avoided unless essential to achieve the economic and efficient development of a project."<sup>9</sup>

Neither the Consultation document nor Jacobs' report sets out the basis under which Ofgem would have the powers to require the transfer of assets from the existing owner to a third party and we do not believe that Ofgem currently has this ability under its statutory powers.

As importantly, we do not believe it is necessary. We suggest that there are enough examples of existing arrangements that render this proposal unnecessary. For example, if licensees see merit in transferring an asset to simplify a particularly complex project then this can already be achieved, with Ofgem agreement, under the Disposal of Assets licence condition. Alternatively, introducing an isolation point between TO and CATO assets may achieve the desired outcome with less cost or complexity involved than would be triggered from introducing an asset transfer requirement.

The discussions at the Ofgem-hosted workshop on 12 February 2015 indicated to us that there was no appetite, either from potential CATOs or the existing TOs for this, and this is noted in Jacobs' summary of the meeting<sup>10</sup>. As a party interested in the potential to compete more widely within GB,

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<sup>8</sup> Jacobs, 'Technical Report on Enabling Competition', May 2015, p.22

<sup>9</sup> Ibid, p.17

<sup>10</sup> Ibid, p.12: "A clear view emerging from the workshop was that the transfer of assets, while possible, would lead to increasing complexity, particularly the transfer of older existing assets."

we would be very concerned about any requirement to take on another party's assets, especially if they were aged or there was limited information available on the asset condition. Jacobs also state its own view that "transferring ownership from an existing regulated party would be complex and lead to potential uncertainty."<sup>11</sup>

We believe there are an extensive list of factors that would need to be taken into consideration if this route was pursued and we do not believe it will result in sufficient incremental benefit to consumers to merit the costs and additional time during the tender process that will be incurred in resolving these. Our concerns, both as an existing TO and a potential bidder under the new regime, include:

- potential for assets developed under the CATO regime to be subject to transfer as part of a future (potentially unknown) tender;
- valuation of assets;
- due diligence to determine condition of asset;
- agreement of liabilities, warranties or other contractual remedies as part of transfer;
- whole life costs of assets, including assessment and treatment of preventative maintenance interventions;
- access to asset by current owner;
- interfaces with other assets on current owner's existing network;
- impact on Network Output Measures and Non-Load Related allowances;
- asset integrity; and
- system security.

As discussed with members of the team, Figure 1 in the consultation document is unhelpful as it appears to suggest that up to 25% of an existing TO's assets could be transferred. Having reviewed the consultation letter and the Jacobs' report, we do not believe this is the intention and suggest that two matters are being confused here. It is our understanding that the percentage referred to relates to what proportion of a project costs could be for work on existing assets before it is considered to be outwith the new and separable criteria. We do not believe that this should be combined with whether or not it is appropriate to transfer assets. However, as noted previously and for the avoidance of doubt, we do not believe 75% constitutes 'substantially new' assets.

In our opinion, this is one aspect of the proposals where there are significant differences between the existing arrangements offshore and what may be practical onshore. The offshore regime has been developed with specific intent to tender new transmission assets, purchased and installed solely for the purpose of creating that part of the offshore transmission network, within a matter of months of commissioning. This is clearly understood by all involved parties, allowing for appropriate assessment of the risks associated with this. Any potential transfer of existing, and potentially aged assets, has a significantly different risk profile that cannot be standardised and will therefore require significant and costly work to be undertaken to facilitate any transfer. This additional work will impact the benefits Ofgem is seeking to realise and yet has not been factored in to the Impact Assessment.

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<sup>11</sup> Ibid, p.7

## Appendix 2: Timeline of relevant excerpts re competition and SWW

The following table sets out Ofgem's key publications as it has developed and refined its thinking on the use of competition for the delivery of onshore transmission assets and the key submissions made by SHE Transmission as part of the assessment of its RIIO-T1 Business Plan.

Date	Document	Key Point/s & reference	Consultation?
October 2010	RIIO Decision	Document sets out the principles to underpin the RIIO model, including #9 "Options to give third parties a greater role in delivery"	N
31 March 2011	RIIO-T1 Strategy Decision	"where a company is fast-tracked, it will be able to get on with running its business during the price control review without being subjected to additional scrutiny from the regulator" (para 5.10)	N
31 March 2011	RIIO-T1 Strategy, Outputs Supporting Annex	Within period mechanism described in paras 7.53-7.68; referred to as 'streamlined mechanism'; no mention of competition within this section; not referred to as Strategic Wider Works at this stage.	N
31 March 2011	RIIO-T1: Greater role for third parties in electricity transmission	"We are not making the decision to utilise competition at this time. We would only choose to utilise this option following consultation and the completion of our review of the business plans submitted by the transmission companies. We are more likely to want to utilise the competitive option where we have concerns that the companies' plans do not represent good value for consumers." This document is referred to in the RIIO-T1 Strategy Decision document as the initial consultation on competition in T1.	Y (closed 18/05/11)
29 July 2011	SHE Transmission submitted its initial RIIO-T1 Business Plan to Ofgem		
24 October 2011	RIIO-T1 Initial Assessment Open Letter	Stated Ofgem's minded view position to retain SPT and SHETL in the fast track. No mention of within period determinations; SWW or competition.	Y (closed 21/11/11)
16 December 2011	SHETL submitted its revised RIIO-T1 Business Plan to Ofgem		
16 December 2011	RIIO-T1: Competition in Onshore Electricity Transmission	"for appropriate projects, where we have concerns about efficiency or value for money of proposals put forward by incumbent TO, we could hold a selection process" (para 1.3) "We expect that this regime could potentially apply to any wider reinforcement works for which construction funding has not been awarded to date and is not contained in the licensees RIIO-T1 baseline proposals. To clarify, projects treated as	Y (closed 10/02/12)

		strategic wider works in our RIIO final proposals could be subject to third party delivery. Provision of funding for one or more initial phases of these projects does not preclude the possibility of a competitive approach being taken for subsequent phases." (para 1.8)	
13 January 2012	SHETL submitted updated paper on SWW following SQs from Ofgem		
23 January 2012	RIIO-T1: Decision to fast-track	Letter setting out Ofgem's intention to fast-track SPT and SHETL. "we consider that the package put forward by SHETL provides good value for money" (p.4)	N
7 February 2012	RIIO-T1: Initial Proposals for SPT and SHETL	"we are considering whether each package as a whole delivers value for money to the consumer. We are seeking views on the appropriateness of the packages as a whole." (para 1.5) "if circumstances are appropriate, we will be able to instigate a selection process for a project, or specific works on a given project where the project comprises multiple elements, where we had concerns that the plans submitted by the company do not represent good value for consumers" (para 1.40) Para 1.41 refers to December consultation (still open at time of publication). Table 8 lists Wider Reinforcement Works as an uncertainty mechanism and refers to these as Strategic Wider Works.	Y (closed 20/03/12)
7 February 2012	RIIO-T1: Initial Proposals for SPT and SHETL – Supporting document	"The framework for competition in the delivery and operation of onshore transmission assets would operate alongside the arrangements for wider reinforcement works during the price control period...We expect that this regime could potentially apply to any wider reinforcement works for which construction funding has not been awarded to date and is not contained in the licensees' RIIO-T1 baseline proposals." (para 2.129 – specific to SHETL's proposals)	Y (closed 20/03/12)
23 March 2012	ITPR Open Letter	No mention of competition.	Y (closed 25/05/12)
23 April 2012	RIIO-T1 Final Proposals for SPT & SHETL	"It is our intention that this competitive framework could potentially be used to award the revenue stream for any wider reinforcement works for which construction funding has not been awarded to date and is not contained in the licensees' RIIO-	N

		T1 baseline funding. For the avoidance of doubt, projects treated as Strategic Wider Works (SWW) in our RIIO Final Proposals could be subject to this competitive process and therefore potentially delivered by a third party TO." (para 1.34) "We are currently developing a framework to enable competition in electricity transmission. For the avoidance of doubt, projects treated as strategic wider works in RIIO FPs could be subject to that competitive process and therefore potentially delivered by a third party TO." (footnote 18, p21)	
23 April 2012	RIIO-T1: Implementing competition in onshore electricity transmission - update	"For the avoidance of doubt, projects treated as strategic wider works in our RIIO final proposals could be subject to competition." (para 4)	N
5 March 2013	ITPR: Emerging Thinking	"The ITPR project builds on our intention as noted under RIIO to consider the use of so-called "third party delivery" (ie opening up delivery to parties other than just the incumbent TO) for onshore electricity transmission where it might be in the interest of consumers." (para 4.5)	Y (closed 2 August 2013)
29 September 2014	ITPR: draft conclusions	"We propose to extend the use of competitive tendering to onshore assets that are new, high value, and separable. We would run a competitive tender exercise to identify a party to construct, own and operate these assets." (para 3.10) "Assets that meet these criteria can be more easily scoped for tendering, have minimal interface costs, and because they are high value the potential gains are high compared to the transaction costs of the tender process." (para 3.11)	Y (closed 24/11/14)
17 March 2015	ITPR: final conclusions	"competition should be used to deliver transmission assets where it benefits consumers. There also needs to be a clear, predictable and fair regulatory framework for infrastructure development." (para 1.3)	N