

# TRANSMISSION CAPITAL PARTNERS

Joe Baddeley  
Transmission Competition Policy  
9 Millbank  
London  
SW1P 3GE

22<sup>nd</sup> July 2016

Dear Joe,

## **Extending competition in electricity transmission: arrangements to introduce onshore tenders**

Transmission Capital Partners manages one of the largest offshore electricity transmission portfolios in terms of the capacity of offshore wind connected. Our managed portfolio of Offshore Transmission Owner (OFTO) assets includes the connections to the Robin Rigg, Gunfleet Sands, Barrow, Ormonde, Lincs and Westermost Rough offshore wind farms - a portfolio of over 1000MW (circa £800m in capital employed).

We remain strong advocates of introducing competition into the delivery of onshore transmission and we continue to support the development of the required arrangements *inter alia* through industry groups, responding to consultations such as these and, when called upon, providing evidence to parliament.

We understand the difficulty in providing visibility on a potential CATO project pipeline given that many of the projects that could be tendered are themselves dependent on generation projects proceeding. Nevertheless we think it would be beneficial for potential bidders for there to be a single comprehensive list of potential projects, regularly updated and perhaps noting the drivers and uncertainties behind each project, so that bidders can suitably prepare themselves.

We note that the government is still reviewing the role of the System Operator and whether greater independence in that role is required. We continue to believe that the System Operator not only needs to be independent it also needs to be seen to be independent, and that the only clear way to achieve this is through separation in ownership terms from any party taking part in a competitive transmission activity.

Our response to your specific questions is attached as Annex 1.

Yours sincerely,



**Chris Veal**

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## Annex 1 – Responses to specific questions

QUESTION	TCP RESPONSE
<b>CHAPTER: Two</b>	
<p><b>Question 1:</b> What are your views on our proposed arrangements for asset ownership and responsibilities? In particular can you provide examples of specific scenarios where it may be necessary for ownership transfer of existing physical assets to occur between network operators?</p>	<p>We agree that access should be generally achievable through the normal industry arrangements such as interface agreements.</p> <p>We also agree that generally the assets to be transferred by the TO (in RIIO-T1) or SO (in RIIO-T” and thereafter) should be non-physical assets. The transfer of these non-physical assets will need to be documented legally through some form of Transfer Agreement (aka Sale and Purchase Agreement) to clearly deal with all rights, obligations and liabilities (pre-and post-transfer).</p> <p>We believe that the “completely new” requirement in respect of physical assets will be workable in most scenarios and indeed it is difficult to think of circumstances in which physical assets could need to be transferred. Some examples of physical assets that may need transferring could include:</p> <ul style="list-style-type: none"> <li>• Spare bays at substations, particularly if there is a restriction on space at a substation and the construction of new bays would be difficult or require new landowner permissions or consents (this example is already cited in the consultation document);</li> <li>• Possible transfer of some existing assets in a project which (almost) completely replaces an existing asset (for example re-use of some cable sections in a predominantly overhead line route, perhaps with the addition of some new cabling) – we think this is theoretically possible although unlikely in practice;</li> <li>• Re-use of some long life civil structures (such as tunnels) – these may actually be considered as part of the land rights in any event.</li> </ul> <p>In conclusion we believe that the transfer of physical assets is not likely but we would still regard it is prudent that some allowance is made for this in the unlikely event that it is required.</p> <p>We would also note that should assets be reusable in a new scheme then these assets should be made available to all bidders on the same terms (and not for example reserved for the use of the incumbent TO or its affiliate.</p>

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<p><b>Question 2:</b> Do you agree with our proposed principles for packaging projects?</p>	<p>We agree in general with the proposed principles for packaging as they include both a logical approach based on a common need or driver together with some degree of flexibility to ensure the best outcome for the consumer by bundling, splitting or repackaging.</p> <p>It would be helpful if decisions on packaging could be taken at an early stage, so long as the decision would remain robust, as this is likely to provide most certainty to incumbent TOs and potential bidders.</p> <p>Consideration could be given to splitting where projects include special features that would not naturally fit within a turnkey construction package – for example where a project includes both a very large and challenging civil construction element (such as a tunnel) and also a large high voltage electricity transmission element. A better outcome for consumers may be obtained by procuring delivery of these separately as long as the interface issues can be clearly defined and managed.</p> <p>We note that bundling is only expected to be carried out where projects were already above the high value threshold in the first place. There could also be consumer benefits in bundling projects so that the aggregate bundle is above the high value threshold even if the individual elements were not. We would though expect there to be some commonality in the individual elements to provide the logic for bundling.</p>
<p><b>Question 3:</b> Do you consider the processes we have set out for determining which projects to tender are appropriate?</p>	<p>The process for determining which projects to tender during RIIO-T1 appears to be relatively simple involving:</p> <ol style="list-style-type: none"> <li>1. the TO making an Initial Needs Case to Ofgem for a SWW project</li> <li>2. Ofgem deciding whether the project needs case stands up and also whether it is suitable for tendering</li> <li>3. Ofgem consulting</li> <li>4. Ofgem makes a decision</li> <li>5. Preliminary works are undertaken by the TO (presumably until appointment of successful bidder)</li> </ol> <p>The key features we derive from this are:</p> <ul style="list-style-type: none"> <li>• The incumbent TO should not influence whether the project is suitable for tendering (other than through the consultation process)</li> <li>• The SO appears not to have a role in the process</li> <li>• The tender is only commenced after the Ofgem decision on the Initial Needs Case</li> </ul>

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	<p>We would consider that an independent SO could play a valuable role in assessing whether the proposed SWW project is the right project (or whether the incumbent TO has devised the SWW project in a way so as to avoid a tender). We also consider that some mitigation is required to ensure that incumbent TOs do not only bring SWW projects forward for the Initial Needs Case at a time when it is difficult to run a tender process.</p> <p>The process for determining which projects to tender during RIIO-T2 appears to be similar except:</p> <ol style="list-style-type: none"> <li>1. The SO recommends the solution</li> <li>2. Preliminary works are undertaken by the SO (presumably until appointment of successful bidder)</li> </ol> <p>It is not clear to us at present as to how the SO captures all of the possible projects that meet the new, separable and high value criteria. As the consultation document notes these projects are not all identified through the NOA process. It would be beneficial if there were a single process to capture all projects which may be eligible for tendering, or at least for all processes that may result in such projects to feed into a single process and for there to be oversight over all processes to ensure that none slip between the gaps. Alternatively a restriction could be placed on incumbent TOs that capital expenditure on projects in excess of £100m (or perhaps a lower value to ensure compliance) would be disallowed unless that project had previously been considered for tendering.</p> <p>An independent SO is fundamental to this process working and for bidders to have confidence in it.</p>
<p><b>Question 4:</b> Beyond the NOA and the connections process, what other routes should we be utilising to identify suitable projects for competition, e.g. for non-load projects?</p>	<p>It appears to us that there will be conflicts of interest with incumbent TOs whilst they are responsible for planning extensions to their systems. As such there is a need to either have close scrutiny of this process or to provide the right incentives on the TOs (e.g. potential disallowed expenditure as set out above). One alternative would be for an independent SO to have a role in supporting (or otherwise) all new projects that have a capital value in excess of (say) £50m. It could be argued that direct like-for-like asset replacement should be carved out of this requirement although we would note that the SO should be involved in this as well in case an alternative to like-for-like presented a better solution for the consumer.</p>

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	<p>The SO should be fully involved in projects that result from new generation or demand connections (and therefore offers made by the SO) or from the NOA process.</p> <p>In summary we are advocating a role for the (independent) SO in scrutinizing all capex plans by TOs above a certain threshold to ensure that the best projects are being brought forward by the TOs given the conflicts of interest with which they might be faced.</p>
<p><b>Question 5:</b> What do you consider should constitute 'early development works' for options ahead of their assessment in the NOA process, i.e. what works should be undertaken in order to ensure that the most appropriate tendered options are developed for submission at the initial tender checkpoint?</p>	<p>We would consider that the early development works should include those works that could provide information on the costs (capex and opex), timescales and risks of project options. We agree that generally this should be desk based work but could include:</p> <ul style="list-style-type: none"> <li>• Desk-based environmental studies of sites and routes;</li> <li>• Desk-based engineering routing studies (onshore and offshore if applicable);</li> <li>• Cost estimates (capex and opex);</li> <li>• Benefit estimates (to the extent that they differ between options);</li> <li>• Identification of specific technical and environmental risks (largely to come out of the above but possibly also to do with technology);</li> <li>• Identification of other risks (e.g. landowners against whom CPO powers cannot be used or similar).</li> <li>• Likely project timelines and risks to achieving these.</li> </ul>
<p><b>CHAPTER: Three</b></p>	
<p><b>Question 6:</b> What are your views on the suggested process for carrying out the pre-tender roles?</p>	<p>We agree with the allocation of roles pre-tender in both the RIIO-T1 and RIIO-T2 and thereafter phases.</p> <p>However, it should be recognised that the incentives on incumbent TOs in the RIIO-T1 phase may not be perfect and therefore we believe that some oversight of the work they carry out in preparing the tender specification and in specifying and carrying out pre-tender works (e.g. surveys) would be beneficial. An independent SO would be well placed to carry out this role but in the absence of that it should fall to Ofgem and its advisers.</p>
<p><b>Question 7:</b> Regarding preliminary works and the tender specification: <b>(a)</b> What are your views on the scope of the baseline tender specification?</p>	<p>(a) We have responded to this question through the ECIT Tender Specification Working Group meeting on 20<sup>th</sup> June 2016. In summary our views were that the TNEI report in general adequately captured the tender specification requirements, but that the following items should also be included:</p> <ul style="list-style-type: none"> <li>• Land agreements (including The Crown Estate for offshore, crossing agreements etc.);</li> </ul>

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<p><b>(b)</b> How likely is it that additional preliminary works will be required, and if so, what types of works are likely to be required?</p> <p><b>(c)</b> What are your views on:</p> <p><b>(i)</b> The role of bidders in identifying the need for further information / additional preliminary works (e.g. additional independent surveys) to inform robust bid assumptions?</p> <p><b>(ii)</b> The most efficient process for enabling this?</p>	<ul style="list-style-type: none"> <li>• Onshore field-based geotechnical site investigations at tower locations and substation sites;</li> <li>• Offshore geotechnical and geophysical field-based site surveys (to an appropriate specification) where projects involve offshore cable routes;</li> <li>• We did not consider that vessel availability was necessary and that bidders could source this information themselves.</li> </ul> <p>(b) Additional works are noted in our response to (a) above.</p> <p>(c)</p> <p>i) Ideally bidders should not need to identify further information or additional preliminary works as it should be possible for a TO with suitably experienced staff and advisers to identify the key issues that would enable robust bids and risks to be managed. However, we agree that as a safety net allowing bidders to suggest additional preliminary works could be useful so long as it does not lead to an extended tender process. It may be worthwhile setting out how such suggestions from bidders would be treated, for example would the additional preliminary works only be undertaken if a significant proportion of bidders thought the additional work was beneficial?</p> <p>ii) It is unlikely that bidders will spend much time or money scrutinizing available data until they have been qualified to tender and it would also be most efficient if only the views of bidders qualified to tender were taken into account. However, this could give rise to delays as these bidders would only be selected part way through the tender process.</p>
<p><b>Question 8:</b> What are your views on the proposed arrangements for the data room and bidder clarifications?</p>	<p>We agree the virtual data room works well for the OFTO tender process and should also be used for the CATO tender process.</p> <p>We agree that the incumbent TO should populate this for the RIIO-T1 phase but we would consider this role should be undertaken by an independent SO in the RIIO-T2 and thereafter phases.</p> <p>It should be noted that an incumbent TO will not have the same incentives as an offshore wind farm developer has in respect of the OFTO tender process as the offshore wind farm developer does not (usually) have an affiliate OFTO bidder, is incentivised to make the process as competitive as possible, and seeks to provide information where possible so as to retain as little as possible residual risk from undisclosed information. This circumstances will not be the same for an incumbent TO and so there will need to be oversight of how it acts in this regard.</p>

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	<p>With respect to clarifications we would consider that Ofgem will need to act as an intermediary for these so as to be able to anonymise the questions so that the incumbent TO does not know from which bidder a question comes.</p>
<p><b>Question 9:</b> What are your views on our proposals regarding the funding of preliminary works and tender support activities in RIIO-T1?</p>	<p>We generally agree with Ofgem’s proposed approach to the funding of preliminary works and tender support activities. We would though like to understand, in the absence of a success payment, whether the incumbent TO in RIIO-T1 will be rewarded for taking the risk that costs may be disallowed and also how it is rewarded for financing these costs (to the extent that it does not receive cash funding up front for these costs).</p>
<p><b>Question 10:</b> Do you have any initial views on risk allocation across the preliminary works party and the CATO?</p>	<p>We understand that Ofgem will be consulting in detail on risk allocation later in the year and we will respond in detail at that stage. Our initial views are that:</p> <ul style="list-style-type: none"> <li>• CATOs should not be taking any risk on the correctness of data supplied to it through the tender process (i.e. via the data room);</li> <li>• CATOs should not be asked to assume any performance risk on contracts for supply chain procurement or construction work entered into by an incumbent TO or the SO;</li> <li>• In the late delivery model the CATO should not be assuming any risks for obtaining any consents or land rights.</li> </ul>
<p><b>CHAPTER: Four</b></p>	
<p><b>Question 11:</b> Do you agree with our proposed requirements for incumbent TOs to mitigate potential conflicts of interest, where they are both bidding for and developing a project in RIIO-T1?</p>	<p>We note that the SO business separation measures are awaiting outcome of the review that was being undertaken by DECC.</p> <p>We think the TO business separation measures go part of the way but we would consider for the measures to be effective and to be seen to be effective there should be a requirement that:</p> <ul style="list-style-type: none"> <li>• The TO bidding party is in a separate legal entity to the TO preliminary works team (i.e. the existing TO licensee);</li> <li>• Is located in a separate building to the TO preliminary works team with no shared facilities (such as canteens); and</li> <li>• Managerial separation should go up to the parent company board level.</li> </ul>
<p><b>Question 12:</b> Is internal scrutiny of the arrangements the TO has in place to mitigate conflicts of interest sufficient, or would there be significant additional value in having</p>	<p>Internal scrutiny is not sufficient and an independent external audit process is required if business separation measures are to be seen to be implemented as described. We do not consider that the cost should be high in relation to the scale of the tender process.</p>

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<p>an independent party scrutinise and audit the TO's arrangements?</p>	<p>We consider that any non-compliance with business separation measures should result in disqualification from any relevant tender processes and repeated breaches should lead to an extended tender ban.</p>
<p><b>Question 13:</b> Do you agree with our proposal to manage conflicts for other bidder</p>	<p>We are assuming that other bidders (e.g. contractors) will have ceased any work on a project being tendered prior to the commencement of the tender process. If this is not the case then the same measures as for the TO would need to be put in place.</p> <p>With that understanding the conflict of interest issue becomes one of ensuring that all relevant information that the other bidder has in relation to a project being tendered is transferred (via the data room) to all bidders.</p> <p>It is not clear to us that the measures suggested in the consultation document will be sufficient to achieve this and it may be necessary to have stronger business separation measures. For example ensuring that the same personnel cannot provide input into the project pre-tender and also be involved in a bidding team – perhaps this would be one of the subjects of an MoU.</p>

{End}