

Current and future electricity
transmission; gas transportation;
electricity interconnector; and
gas interconnector licensees

Email: unbundlingcertification@ofgem.gov.uk

Date: 17 March 2021

Dear Colleague,

Certification arrangements in Great Britain following amendments to the ownership unbundling provisions of the Gas Act 1986 and the Electricity Act 1989: End of the transition period

The UK left the European Union ('the EU') on 31 January 2020 at 11:00pm GMT ('Exit day'¹), when the EU-UK Withdrawal Agreement ('the Agreement') came into force. The Agreement sets out the transitional arrangements governing the UK-EU relationship. Article 126 of the Agreement provides for a transition period, which ended on 31 December 2020 at 11:00pm GMT. This date is reflected in section 39(1) of the European Union (Withdrawal Agreement) Act 2020² and is referred to as the 'IP completion day'.

This letter sets out information on our intended approach to processing applications for certification and undertaking reviews of certification following recent amendments to the ownership unbundling provisions of the Electricity Act 1989 ('the Electricity Act') and Gas Act 1986 ('the Gas Act'), as detailed in Annex 1 to this letter. The amending regulations, the Electricity and Gas etc. (Amendment etc.) (EU Exit) Regulations 2019 (the 'Amending Regulations')³ came into force on the IP completion day⁴.

The Amending Regulations amend the transposition of the EU unbundling requirements into GB legislation, including by:

- a) removing the requirement for the Authority⁵ to send a preliminary decision to the European Commission ('EC').
- b) change the timescales in which the Authority has to make its decision. With the removal of the need to send a preliminary decision to the EC, the Authority now has four months in which to make its final decision;

¹ As defined in section 20(1) of the European Union (Withdrawal) Act 2018, available at <https://www.legislation.gov.uk/ukpga/2018/16/section/20>.

² Available at <https://www.legislation.gov.uk/ukpga/2020/1/section/39/enacted>.

³ Please see <https://www.legislation.gov.uk/uksi/2019/530/made>. As amended by The Electricity and Gas etc. (Amendment etc.) (EU Exit) Regulations 2020, available at <https://www.legislation.gov.uk/uksi/2020/1016/contents/made>.

⁴ As provided by Schedule 5, paragraph 1 of the European Union (Withdrawal Agreement) Act 2020, available at <https://www.legislation.gov.uk/ukpga/2020/1/schedule/5/enacted>.

⁵ The Gas and Electricity Markets Authority ('the Authority'). In this document, the terms 'Authority', 'Ofgem', 'we', 'our' and 'us' are used interchangeably.

- c) place an obligation on the Authority to notify the Secretary of State where a person from outside the United Kingdom controls an applicant for certification; this notification was previously only required where the applicant was controlled by a person from outside the European Economic Area ('EEA');⁶ and
- d) removes the requirement on the Authority to notify the EC when a TSO⁷ is designated.⁸

The changes affect the following types of licensee in Great Britain ('GB'): (i) electricity transmission; (ii) gas transportation (high-pressure only); (iii) electricity interconnector; and, (iv) gas interconnector. Annex 1 to this letter explains the changes and their impact on TSOs currently certified as fully ownership unbundled and new certification applicants.

In addition,

- on 31 December 2020, the (i) electricity transmission and (iii) electricity interconnector licences were modified by The Electricity and Gas (Internal Markets) (No.2) Regulations 2020,⁹ to include the prohibition on those types of licensees owning electricity storage facilities, to reflect the requirements of Article 54 of Directive (EU) 2019/944,¹⁰ and
- on 31 December 2020, consequential licence modifications, as a result of the UK exiting the EU, were made to the GB (i) electricity transmission; (ii) gas transportation (high-pressure only); (iii) electricity interconnector; and, (iv) gas interconnector licences.¹¹

You can find copies of all licences on our electronic register, at [EPR 2013 - Index \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/epr-2013-index).

Our open letter of 23 August 2017 reflected the changes introduced by the Electricity and Gas (Internal Markets) Regulations 2017, that came into force on 24 April 2017 ('the 2017 Regulations').¹² This letter now updates and supersedes that letter.

It is important that you read Annex 1 to this letter carefully and consider any steps you may need to take as a result.

We ask that all applicants use the application form provided at Annex 2 (electricity) and Annex 3 (gas) to this letter.

We encourage applicants to seek legal advice on applying the legislation to their specific circumstances. Please email unbundlingcertification@ofgem.gov.uk if you have any questions about the certification process.

⁶ Regulations 14 and 45 of the Amending Regulations state that the Authority is not required to notify the Secretary of State of the application under section 8D of the Gas Act and section 10B of the Electricity Act, and that the Secretary of State is not required to prepare a report under section 8E of the Gas Act and 10C of the Electricity Act in relation to the application, where an application under section 8D of the Gas Act and/or section 10B of the Electricity Act is made before the end of the transition period and the applicant is a person from an EEA state or a person controlled by a person from an EEA state.

⁷ 'Transmission system operator' means a natural or legal person responsible for operating, ensuring the maintenance of and, if necessary, developing the transmission system in a given area and, where applicable, its interconnections with other systems, and for ensuring the long-term ability of the system to meet reasonable demands for the transmission of electricity.

⁸ Section 8J of the Gas Act and/or section 10H of the Electricity Act refers.

⁹ Available at <https://www.legislation.gov.uk/ukxi/2020/1401/contents/made>.

¹⁰ Directive (EU) 2019/944 of the European Parliament and of the Council of 5 June 2019 on common rules for the internal market for electricity.

¹¹ [Link to our decision "Preparing for the end of the transition period: Statutory consultation on consequential licence modifications due to the end of the transition period"](#).

¹² Note that our open letter of 23 August 2017 updated and superseded our open letter of 15 March 2015, which first set out our approach to exercising our discretion to treat the five unbundling tests as passed under section 10F of the Electricity Act 1989 and 8H of the Gas Act 1986.

Certification arrangements in Great Britain following amendments to the ownership unbundling provisions of the Gas Act 1986 and the Electricity Act 1989: End of the transition period

1. Summary

EU legislation requires ownership 'unbundling'. Unbundling means separating the ownership and operation of a transmission network from the activities of electricity generation, gas production and energy supply.

The government made some changes to the ownership unbundling provisions of the Electricity Act and the Gas Act. The UK left the EU on 31 January 2020 and entered into the transition period during which EU law still applied. The transition period ended at 11pm GMT on 31 December 2020, when the Amending Regulations¹³ came into force (IP completion day).

The Authority is responsible for administering the certification process in Great Britain ('GB') in accordance with the Electricity Act and the Gas Act. Although there are a number of certification grounds, ownership unbundling is the only certification ground considered here. Those applying for certification under the ownership unbundling ground¹⁴ must pass five tests¹⁵ for certification to be granted, and must continue to meet these tests to retain certification. Where one or more of these tests is not passed, an applicant can be certified under this ground if we exercise our discretion to treat these tests as passed,¹⁶ where we are satisfied that there is no risk of discrimination and it would be in line with our principal objective and general duties to do so (the 'discretionary power').

This document outlines the changes introduced by the Amending Regulations and explains our approach to the application of our discretion. This document is not a substitute for the requirements of the legislation. We encourage applicants to seek legal advice on applying the legislation to their specific circumstances.

The Amending Regulations apply to all applications for certification received on or after the end of the transition period.

2. Background

The Electricity Act and the Gas Act require the ownership unbundling of TSOs. Unbundling means separating the ownership and operation of a transmission system from the activities of electricity generation, gas production and energy supply. One of the aims of the provisions is to make sure that TSOs take their decisions independently, ensuring transparency and non-discrimination towards all network users.

The Electricity and Gas (Internal Markets) Regulations ('the 2011 Regulations'), which came into force on 10 November 2011, transposed the EU unbundling requirements into domestic law and provided the current legal framework for the structural separation of TSOs in GB.¹⁷ Our open letter of 10 November 2011¹⁸ detailed our procedure for processing applications

¹³ Please see <https://www.legislation.gov.uk/ukxi/2019/530/made>. As amended by The Electricity and Gas etc. (Amendment etc.) (EU Exit) Regulations 2020, available at <https://www.legislation.gov.uk/ukxi/2020/1016/contents/made>.

¹⁴ Section 10E of the Electricity Act and section 8G of the Gas Act.

¹⁵ Sections 10F of the Electricity Act and sections 8H of the Gas Act.

¹⁶ Section 10F of the Electricity Act and section 8H of the Gas Act.

¹⁷ There was a separate transposition for Northern Ireland.

¹⁸ <https://www.ofgem.gov.uk/ofgem-publications/59314/111110-open-letter-certification-post-legislation.pdf>.

Please note that Ofgem is currently reviewing the format of certification applications, and we will communicate any updates to the procedure described in this letter in due course.

for certification under the ownership unbundling requirements of the third energy package.¹⁹ Under the Electricity Act and the Gas Act, gas and electricity interconnector, electricity transmission and certain gas transporter licensees are required to be certified.²⁰

The Electricity and Gas (Ownership Unbundling) Regulations 2014,²¹ which came into force on 15 January 2015, amended the transposition of the EU unbundling requirements to allow us to treat one or more of the five unbundling tests as passed if we are satisfied that there is no risk of discrimination and it would be in line with our principal objective and general duties to do so. Our open letter of 6 March 2015 set out those amendments.²²

The Electricity and Gas (Internal Markets) Regulations 2017, which came into force on 24 April 2017 ('the 2017 Regulations'), amended the definition of Relevant Producer or Supplier ('RPOS') by removing the EEA geographical limitation on production, generation and supply activities, so that a person undertaking those activities anywhere in the world may now fall within the definition of RPOS. As a result, production, generation and supply activities both within and outside the EEA had to be considered as part of the five certification tests. Previously, only production, generation and supply activities carried out within the EEA were considered as part of the five certification tests.²³

3. An overview of the GB legal framework

The five certification tests and our approach to exercising the discretionary power have not changed. The five tests, as set out in the legislation, are:

- **First test:** the applicant
 - a) does not control an RPOS;
 - b) does not have a majority shareholding in an RPOS; and
 - c) will not, on or after the relevant date,²⁴ exercise shareholder rights in relation to an RPOS.
- **Second test:** if the applicant is a company, partnership or other business, none of its senior officers has been, or may be, appointed by a person who—
 - a) controls an undertaking²⁵ which is an RPOS; or
 - b) has a majority shareholding in an undertaking which is an RPOS.
- **Third test:** if the applicant is a company, partnership or other business, none of its senior officers is also a senior officer of an undertaking which is an RPOS.
- **Fourth test:** the applicant is not controlled by a person who controls an RPOS.
- **Fifth test:** the applicant is not controlled by a person who has a majority shareholding in an RPOS.

¹⁹ As amended by the Electricity and Gas (Internal Markets) Regulations 2011.

²⁰ Section 10A of the Electricity Act and 8C of the Gas Act.

²¹ http://www.legislation.gov.uk/ukxi/2014/3333/pdfs/ukxi_20143333_en.pdf

²² <https://www.ofgem.gov.uk/publications-and-updates/certification-arrangements-great-britain-following-amendments-ownership-unbundling-requirements-gas-act-1986-and-electricity-act-1989>

²³ <https://www.ofgem.gov.uk/publications-and-updates/certification-arrangements-great-britain-following-amendments-ownership-unbundling-requirements-gas-act-1986-and-electricity-act-1989-0>

²⁴ Section 10A of the Electricity Act and 8C of the Gas Act.

²⁵ The definition of "electricity undertaking" is set out in Section 100 of the Electricity Act. The definition of "gas undertaking" is set out in Section 8Q of the Gas Act.

Who is an applicant?

In this document we refer to persons applying for certification (under section 10B(1) of the Electricity Act or section 8D(1) of the Gas Act) and those whose certification is being reviewed (under section 10I(5) of the Electricity Act or section 8K(3) of the Gas Act) collectively as the 'applicant'. To date, all applicants for certification have been either current or prospective electricity transmission licensees (onshore and offshore), electricity interconnector licensees, gas transporter licensees (who carry out the activity of transmission) and gas interconnector licensees.

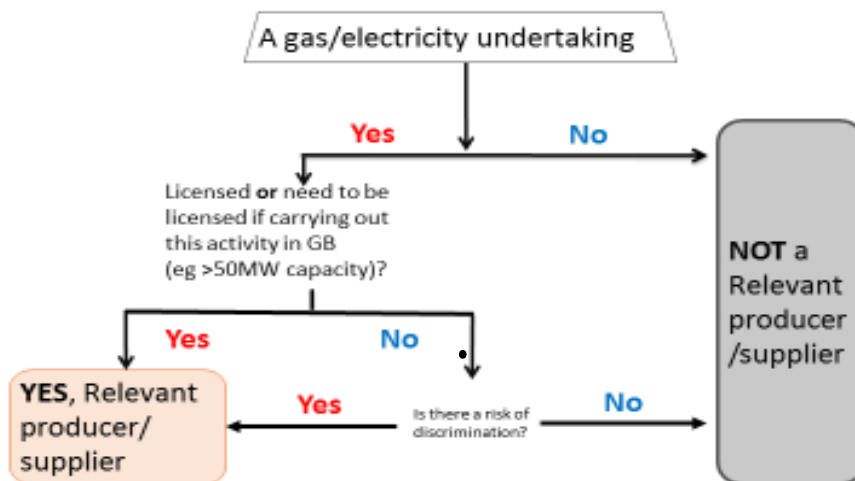
Who is a relevant producer or supplier ('RPOS')?

The relationship between the applicant and the RPOS is at the heart of each of the five certification tests. An RPOS is anyone who participates in one or more of the activities of electricity generation, gas production and/or energy supply, and

- Requires or, in the Authority's opinion, would require a licence to carry out that activity or activities in GB; or
- does not require a licence, or is operating under an exemption granted by the Secretary of State, but has a relationship with the applicant which we think might lead the applicant to discriminate in favour of that person.

This definition is set out in Section 100(3)-(5) of the Electricity Act and sections 8Q(3)-(5) of the Gas Act. There is an illustration of the term RPOS in Figure 1 below.

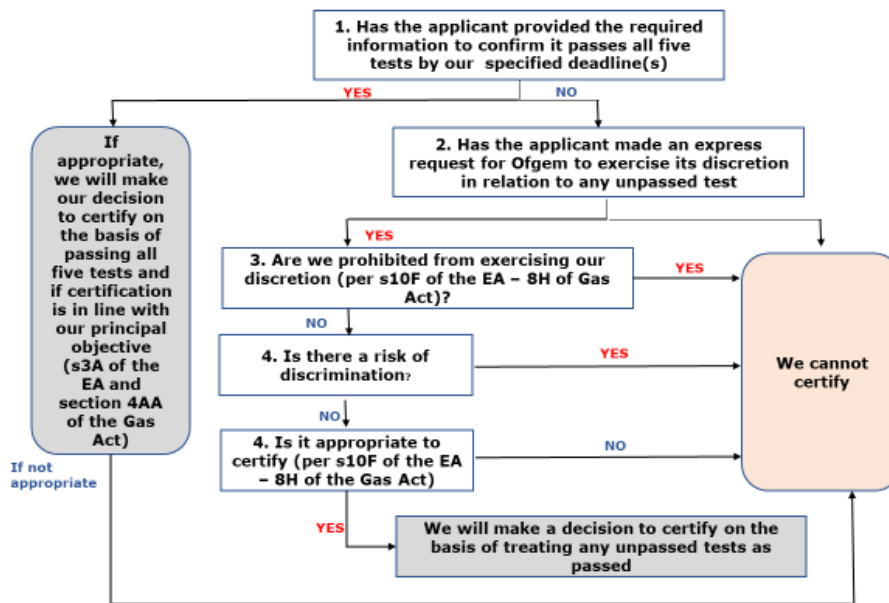
Figure 1: Illustration of the term "Relevant producer or supplier" within the meaning of section 100 of the Electricity Act and section 8Q of the Gas Act



What is risk of discrimination?

Our assessment of risk of discrimination refers to whether an applicant has a relationship with an RPoS which might lead the applicant to discriminate in favour of the RPoS.

Figure 2 – Overview of certification assessment



4. What has changed?

This section sets out the changes introduced by the Amending Regulations.

Removes the requirement for the Authority to send a preliminary decision to the EC and changes the timescales in which the Authority has to make its decision

From the end of the transition period, the Authority will no longer send a preliminary decision to the EC. Instead the Authority will make its decision whether to certify an applicant within four months of receipt of the application.²⁶

Any final decision must be notified to the applicant and the Secretary of State – the requirement for the Authority to notify the EC has been removed.²⁷

We recommend that applicants discuss their applications with us in advance of their submission. Where time allows, we recommend that applicants send us a draft application for consideration, and before the final application is submitted.

²⁶ Section 8F and 8N of the Gas Act and section 10D and 10L of the Electricity Act refer.

²⁷ Section 8F of the Gas Act and section 10D of the Electricity Act refers.

Report where applicant is controlled by a person from a country outside the United Kingdom

Section 8D and 8K of the Gas Act and section 10B and 10I of the Electricity Act places an obligation on the Authority to notify the Secretary of State ('SoS') where an applicant is controlled by a person from a country outside the United Kingdom. Prior to the end of the transition period the Authority was required to notify the SoS where an applicant is controlled by a person from a country outside the European Economic Area ('EEA').

For clarity, TSOs that were certified prior to the end of the transition period need only notify us of a change where the person that controls the TSO has changed. We do not require to be notified where a TSO was controlled by a person from outside the United Kingdom at the end of the transition period and that control has not changed.

Removes the requirement on the Authority to notify the EC when a TSO is designated.²⁸

Section 8J(4) of the Gas Act and section 10H(4) of the Electricity Act requires the Authority to notify the applicant and the SoS where an applicant is designated as a TSO. The requirement to notify the EC has been removed.

5. Review process

Ofgem can review certification where we consider that a TSO's current certification basis may no longer apply. We will open a review where there is evidence that a change in circumstance may cause a TSO to fail any of the tests or there may be a risk of discrimination.

Certified TSOs have an obligation in their licence to advise the Authority of any changes that may affect their eligibility for certification. Certified TSOs can also trigger a review by notifying us of changes under section 10I(5)(a) of the Electricity Act or Section 8K(5)(a) of the Gas Act.

6. The discretion to treat one or more of the five tests as passed

Section 10F(9A) of the Electricity Act sets out how the discretion applies to applicants under that Act, unless the exception in subsection (9B) applies.²⁹ Subsection (9B) relates to circumstances where the Authority is prohibited from exercising its discretion. This is discussed in more detail later in this section.

Section 10F9(A) states:

- “(9A) Except where subsection (9B) applies, the Authority may treat one or more of the five tests in this section as passed if—
- (a) the test or tests are not passed in relation to a relevant producer or supplier,
 - (b) the applicant has demonstrated to the Authority's satisfaction that the applicant does not have a relationship with the relevant producer or supplier which might lead the applicant to discriminate in favour of the relevant producer or supplier, and
 - (c) the Authority thinks it appropriate to treat the test or tests as passed.”

Section 8H(9A) of the Gas Act sets out how the discretion applies to applicants under that Act, shown below.

²⁸ Section 8J of the Gas Act and/or section 10H of the Electricity Act refers.

²⁹ To note, we are still able to treat the fourth and fifth tests as passed in specific circumstances and for a specified period of time under subsections 10F of the Electricity Act and 8H of the Gas Act.

- if—
- “(9A) The Authority may treat one or more of the five tests in this section as passed
- (a) the test or tests are not passed in relation to a relevant producer or supplier,
 - (b) the applicant has demonstrated to the Authority’s satisfaction that the applicant does not have a relationship with the relevant producer or supplier which might lead the applicant to discriminate in favour of the relevant producer or supplier, and
 - (c) the Authority thinks it appropriate to treat the test or tests as passed.”

General approach

Below we describe our general approach to exercising the discretion according to the above provisions. Unless otherwise stated, this approach applies equally to all applicants for certification under the ownership unbundling ground.

- a) For applicants under the Electricity Act only, we are prohibited from exercising the discretion to treat one or more of the five tests as passed where the circumstances discussed in section 10F(9B) apply. This is discussed further below.
- b) Where the circumstances in (a) do not apply, the starting point remains that an applicant who does not meet all five tests will not be certified. The onus is on the applicant to ask us to consider exercising the discretion. We expect the applicant to:
 - i. expressly request that we consider exercising our discretion, and reference the particular test or tests which are not passed.
 - ii. detail the reasons why it believes that there is no risk of discrimination in the particular circumstances.
 - iii. provide information to support its explanation. The nature of such information will depend on the particular test or tests that the applicant is asking us to treat as passed and the circumstances of each individual case, but the following may be relevant:
 - Corporate governance arrangements between the applicant and the RPoS, such as details of shareholder agreements and corporate charts.
 - Information to confirm the size and physical location of the relevant assets such as maps or grid references and copies of connection agreements.
 - Other evidence such as copies of licence documents, export capacity agreements and exporting market details.

Unless we are satisfied, on the basis of the information received, that the applicant does not have a relationship with the RPoS which might lead the applicant to discriminate in favour of that RPoS, the applicant will not be certified.

- c) To decide whether it is appropriate to treat the tests as passed, we will need to consider the wider circumstances of the application by having regard to our principal objective and general duties.

Risk of discrimination

This section lists the factors that we consider may be particularly relevant to assessing the risk of discrimination and our ability to exercise discretion.

Each case will be assessed on its merits, taking into account the context and conditions likely to affect the competitiveness of the energy markets in which the applicant and the RPoS operate. No factor alone will be decisive and further factors may be relevant.

- **Geographical proximity of the assets under the ownership or operational control of the applicant and the RPoS' assets.** The closer the two are, the stronger the indication that a risk of discrimination may exist and the stronger the evidence we will require to rebut it. The risk of discrimination is likely to be greater when the applicant's and RPoS's assets are both located in GB. Conversely, the risk is likely to be lower when the assets are not in the same or a neighbouring market.
- **Role carried out by the applicant.** Each type of licensee has a different role in the GB energy market. Some have an extensive range of responsibilities in operating a large integrated network and establishing the commercial terms for access to a network, and have some influence over investment planning decisions. Others have a more limited range of activities relating to a point-to-point system, which connects to the larger integrated network. The more activities performed by the licensee, the greater the risk of discrimination and the stronger the evidence we will need to rebut it. We consider the risk of discrimination greater if the applicant carries out significant system operation functions or is responsible for investment planning in the geographical area in which the RPoS connects.
- **Market share of electricity generation, gas production and energy supply activities concerned.** We will be particularly concerned about the risk of discrimination if an applicant, or a controller of the applicant, has a relationship which amounts to control over an RPoS, or some RPoS' collectively, who has a large share of the market that both the applicant and the RPoS are active in. The greater the market share, the easier it is to create an opportunity for discrimination, and the stronger the evidence we will require to rebut it. The information gathered as part of this assessment may also be used as part of a broader assessment of potential market power, if necessary. For example, our concerns about the risk of discrimination may be moderated by evidence of the extent to which the RPoS is a price-taker in the relevant market or is insensitive to wholesale market fluctuations.
- **Type of energy assets operated.** We consider that the likelihood of discrimination would be greater when the applicant and the RPoS operate assets in the same sector (i.e. electricity or gas) than otherwise. We may also consider whether the gas production, electricity generation or energy supply activity is the result of a by-product of another primary operation, and whether this affects the risk of discrimination.
- **Arrangements governing the relationship between the applicant, or its controller, and the RPoS.** For example, we are likely to have particular concerns about the risk of discrimination where an applicant, or its controller, has access to confidential information on the activities of an RPoS which has the potential to weaken the scope for investment across the sectors where both the applicant and the RPoS(s) are active.

Appropriateness

As noted above, the Authority will also consider whether it is appropriate to treat the relevant tests as passed by having regard to our principal objective and general duties.

Circumstances where the Authority is prohibited from exercising its discretion

Subsection 10F(9B) contains the following exception for applicants under the Electricity Act:

“This subsection applies where the applicant, or a person who controls or has a majority shareholding in the applicant, controls or has a majority shareholding in a person (“A”) who operates a generating station and—

- (a) A is a relevant producer or supplier; and
- (b) the generating station is directly physically connected to anything that forms part of the applicant’s transmission system or electricity interconnector.”

In the September 2014 call for comments, DECC (now BEIS) explained that this exception is appropriate as certification cannot be granted in these specific circumstances because: *“there would always and necessarily be an unacceptable risk of discrimination in such a situation, i.e. if an electricity TSO were not ownership unbundled from a generator to which it is directly physically connected.”*

An example of a scenario where we would be prohibited from exercising the discretion is where the same person controls, or has a majority shareholding in, an offshore transmission asset and a generating station connected to it.

7. Other relevant legislation and regulation

We remind applicants and certified persons that, notwithstanding their certification status, they must continue to comply with all legal requirements applicable to them, including licence conditions.

If you have any queries please contact unbundlingcertification@ofgem.gov.uk

Annex 2 – Questions for Electricity Transmission System Operators (TSOs) – Applicants under section 10B of the Electricity Act 1989 only: see separate document

Annex 3 - Questions for Gas Transmission System Operators (TSOs) – Applicants under section 8D of the Gas Act 198 only: see separate document