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Update on early model competition

In April 2021 the Electricity System Operator (ESO) published its final Early Competition Plan (ECP)¹. This letter provides a brief update on our plans for early model competition, including our intention to consult on various aspects of the early model this July. It additionally confirms that we have asked the ESO to continue developing various low-regret elements of early model competition over the rest of 2021.

Background

In our May 2019 RIIO-2 Sector Specific Methodology Decision (SSMD)², we requested that the ESO work on an ECP alongside its RIIO-2 Business Plan.

In September 2019, we issued an open letter³ which further detailed our expectations of this work, including timelines and scope.

In December 2020, we issued our RIIO-2 Final Determinations⁴ which outlined our intention to consult on early model competition, following the submission of the ESO final ECP.

Early model competition in RIIO-2

Competition in the design and delivery of energy networks is a central aspect of the RIIO-2 price controls. It has a key role to play in driving innovative solutions and efficient delivery that can help us meet our decarbonisation targets at the lowest possible cost to consumers.

¹ Further information is available here, ESO final Early Competition Plan, April 2021;
<https://www.nationalgrideso.com/document/191251/download>

² See paragraph 2.20, RIIO-2 Sector Specific Methodology Decision and further consultation – Electricity System Operator, Ofgem, 24 May 2019; https://www.ofgem.gov.uk/system/files/docs/2019/05/riio-2_sector_specific_methodology_decision_-_eso.pdf

³ Further information is available here,
https://www.ofgem.gov.uk/system/files/docs/2019/09/electricity_system_operators_early_competition_plan_letter_0.pdf

⁴ See paragraphs 9.38, RIIO-2 Final Determinations for Transmission and Gas Distribution network companies and the Electricity System Operator, Dec 2020;
https://www.ofgem.gov.uk/system/files/docs/2020/12/final_determinations_-_core_document.pdf

We have set specific expectations on the ESO as part of its RIIIO-2 price control to further progress pathfinders which allow for third party engagement within the planning and delivery of specific commercial alternatives to investment on the electricity transmission network. We intend to work with the ESO to explore how these processes can be expanded and improved.

We also intend to ensure that an appropriate range of viable non-network and network options are appropriately considered within wider-network planning arrangements. This includes considering whether and how early model competition could be incorporated into the RIIIO arrangements in a manner that delivers benefits to consumers.

Our views on the ESO's final early competition plan

The ESO final ECP follows c18 months of engagement with relevant stakeholders such as incumbent Transmission Owners (TOs), other potential early competition bidders, and technology providers. This also included input from an independently chaired Energy Networks Stakeholder Group (ENSG), with broad membership from across the sector. Alongside its ongoing stakeholder engagement, the ESO formally consulted on its developing proposals in July 2020⁵ and December 2020⁶.

We are reviewing the ESO's conclusions and recommendations in detail and intend to formally consult on our own views in July. We are, however, broadly satisfied that the update and outputs contained within the ESO's final ECP align with the original project specification set out in the May 2019 SSMD and September 2019 Open Letter.

In our July consultation we intend to set out our views on:

- The overall benefits case for the early competition model
- Early competition criteria and project identification process
- Roles and responsibilities
- Tender process / policy and market offering (high level)
- Key other policy considerations, e.g. TO counterfactual proposal
- Interactions with other workstreams (e.g. Future System Operator considerations⁷).

We then intend to make decisions on key aspects of the above by early 2022.

⁵ Further information is available here, ESO Early Competition Plan – phase 2 Consultation, July 2020; <https://www.nationalgrideso.com/document/177171/download>

⁶ Further information is available here, ESO Early Competition Plan- phase 3 Consultation, Dec 2020; <https://www.nationalgrideso.com/document/181901/download>

⁷Further information on the Review of GB energy system operation can be found here, Jan 2021; <https://www.ofgem.gov.uk/publications-and-updates/review-gb-energy-system-operation>

Our views on ongoing ESO work

Within its recommendations in the final ECP, the ESO considers there are various implementation plan activities which it can start work on⁸, prior to Ofgem taking further formal decisions on early competition.

The areas the ESO proposes to develop further are:

- 1) Finalise process for identifying possible projects for early competition
- 2) Explore the potential for expanding pathfinders as a pre-legislative form of early competition
- 3) Scope out potential Code changes
- 4) Develop a detailed programme plan with Ofgem
- 5) ESO organisational design development

Overall, we agree with the areas proposed by the ESO and that the above are low regret activities to take forward this year, although we have agreed with the ESO to delay area 5) until there is further clarity from the Future System Operator workstream and we have published our July consultation on early model competition. Given the ESO's existing role in network planning and involvement in developing early competition to date, we also agree that it is the party best placed to undertake this work, supported by continued engagement with wider industry stakeholders.

We are particularly interested in the ESO exploring the potential for expanding pathfinders as a pre-legislative form of competition. This aligns with our priority to ensure that the benefits of competition can be delivered, ahead of underpinning legislation⁹.

Further work to explore - Interactions with Electricity Distribution

We also consider that there is further low regrets work that the ESO could do to consider the potential applicability of the Early Competition model to distribution and what adjustments might be required to successfully implement this. This work should focus on developing more detailed proposals for the changes required to transpose the transmission level early competition to distribution, and a consideration on how these changes may be delivered, for example where a change in process or party is identified. This should also include

⁸ See paragraph 7.2, Potential ESO activities prior to an Ofgem decision, ESO final early competition plan <https://www.nationalgrideso.com/document/191251/download>

⁹ Underpinning legislation is required for the "full" early competition model as proposed by the ESO. In December 2020, the Government's Energy White Paper committed to legislate, when Parliamentary time allows, to enable competitive tendering in the building, ownership and operation of the onshore electricity network. The Government intends the legislation to allow the Secretary of State to appoint an appropriate party to run the tender processes. Further information is available here, Energy white paper: Powering our net zero future (see pages 76-77), Dec 2020; <https://www.gov.uk/government/publications/energy-white-paper-powering-our-net-zero-future>

consideration of pre-legislative competition in distribution. This continued work will be used to inform us ahead of any final decision we make on early model competition in the electricity distribution sector. As part of this further work we think there is value in the ESO engaging with relevant stakeholders to test its proposals.

Next Steps

As referenced earlier, we will review the ESO ECP report and recommendations in detail and consult on our views this July. We would encourage all stakeholders to get involved through this consultation. We are additionally happy to engage with parties on early competition through bilateral discussion. Please contact James Norman or Cher-Rae Fairlie at RIIOElectricityTransmission@ofgem.gov.uk to discuss.

Yours sincerely,

James Norman
Head of RIIO Electricity Transmission Development