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OFGEM
9 Millbank
LONDON SW1P EGE

Email to: TransmissionCompetition@ofgem.gov.uk

11th January 2016

Subj: **Extending competition in electricity transmission. Arrangements to introduce onshore tenders**

Dear Sirs

We would like to thank OFGEM for the opportunity given to participate in the public consultation process for establishing the criteria and procedures for the introduction of onshore tenders for transmission projects.

ELECNOR is one of the major Spanish electrical contractors with a vast international experience in electrical transmission concession contracts, through a process of public tendering, mainly in Chile and Brazil where we have participated, since 2002, as investors and EPC contractors in 23 *Build, Operate and Own* (BOO) concessions (21 in Brazil and 2 in Chile) involving the following installations:

	kM of Lines			
Country	**500 kV**	**230 kV**	**138 kV**	**TOTAL**
Brazil	5228,50	2343,95	234,95	7807,40
Chile	454,00			454,00
Total	5682,50	2343,95	234,95	**8261,40**

	Number of Substations				**MVA**
Country	**500 kV**	**500/230 kV**	**230 kV**	**230/138 kV**	**Involved**
Brazil	33	3	17	8	9375
Chile	4				
Total	37	3	17	**57**	**9375**

At present, ELECNOR retains, in Brazil, through our affiliate CELEO Redes the 100% ownership of 6 concessions and 51% or 50% of another 6 concessions, and in Chile the 100% of the 2 concessions, performing its operation and maintenance.

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We believe that the successful experience developed in countries like Brazil, were there are at present many Transmission Operators through Concession Contracts gained in public tendering, should reinforce the path undertaken by Ofgem of opening the onshore transmission market in the UK to new operators with the aim of achieving the target of bringing value to consumers.

In the document attached, we will try to provide you with our point of view, based in our experience, for the questions included in your publication dated 19th October and we confirm that we are ready to provide any additional clarification or information that you may require.

In this respect you can contact any of the following persons: Antonio Vila (avila@elecnor.es), Almudena Sotos (asotos@elecnor.es) or myself (apinon@elecnor.es)

Yours sincerely

Antonio Piñon

Antonio Piñon
Business Development Area Director

Attachment: OFGEM Questionnaire

2. What will be subject to competition and how will we identify those projects?

Chapter Summary

We propose that brand new or complete replacement transmission infrastructure projects worth £100m or more should be subject to competitive tenders. These will be identified and developed by TOs or the SO before a tender. Appendix 2 has further detail

Question 1: *What are your views on the proposed detailed interpretations of new, separable and high value (the 'criteria')?*

With reference to establishing a threshold value for projects to be tendered, we consider that there should be flexibility on that value of 100 M£ and agree that should be the expected capex value of the project. As you advance in the definition of projects, you may be able to detect the market interest in lower sizes of projects.

With reference to the new and separable concepts, we clearly support the idea of new projects and not the idea of partial replacement of elements in an existing project that it is owned by an existing TO (i.e. an existing Transmission Line that will replace the conductors). The Transmission project should also be clearly separable from existing TO assets from the point of view of ownership and also from the operational point of view.

Certainly there will probably many projects where connection to existing incumbent TO's assets will be required (connection of the CATO Transmission Line to an existing TO Substation). In this case electrical separability through Disconector and Circuit Breaker arrangements, may be convenient to minimize or eliminate the risks of interference to the operation of the incumbent TO system and clearly define responsibilities.

In the Transmission Concessionary market in Brazil, the collaboration through an specific contract "*sharing contract*" defining eventual sharing of installations and responsibilities, between the owner of the Substation and the new Transmission concessionaire (CATO) has been working very well, being known the structure of said contract at the time of the tender.

Previous to the tender process, the definition of any associated costs or criteria of the incumbent TOs for implementation of the extension of their substation should be clearly specified with some of such costs (i.e: rental of the land if owned by the TO or others) established by negotiations between Ofgem and the incumbent TO and specified in the tender

In our opinion the sharing of installations should be the minimum possible and certainly the incumbent TO should receive market compensations from the CATO, or consumers if set up during the tender process, for accepting such commercial arrangement.

Operation of the extension of the substation is handled by the CATO following instructions of the SO.

Question 2: *Under what circumstances do you think asset transfer from an existing asset owner to a CATO would be required, recognising the principle that projects identified for tendering should be new?*

We are of the opinion that transfer of assets of the TOs to the CATOs should be avoided as much as possible since this would transfer also uncertainties and risks on the real asset situation to the CATOs maybe even reducing the interest of investors.

In case some assets seem convenient to be transferred, it should be limited to some assets in substations that could be considered physically and electrically independent and that the guarantees for the asset and future availability could be clearly separated between the former owner and the new one.

Question 3: *What are your views on our proposal that electrical separability should not be required at each interface, but that the SO can propose it to us if it thinks there is a cost-benefit justification based on system operability?*

In most cases electrical separability is convenient in order to clearly establish responsibilities and avoid operation interferences between the CATO and incumbent TO. Certainly, the SO can propose for each particular case the most convenient approach, always allowing the clear separation of responsibilities in case of any failure.

Question 4: *What are your views on the suggested process and roles for identifying projects for tendering? We have proposed specific roles for the SO – do you think there are any additional roles the SO could take on to support competition? What's the most appropriate way to ensure that the network options assessment (NOA) considers the widest range of network options, including those that would be tendered?*

It would be preferable that SO became completely independent of TOs and CATOs. It would eliminate any future conflict of interest, coming its remuneration from consumers or a fee invoiced to the TOs and CATOs.

It should be penalized the identification of solutions not to be tendered to assure that in a short term the maximum number of assets are assigned to CATOs and that only the options not valid to be tender avoid this path.

Question 5: *What incentives and obligations should the SO and TOs have for undertaking preliminary works for tendered projects, and is there any value in considering a success fee incentive?*

We are in the opinion that the direct costs of the preliminary works developed by the SO and TOs for the projects to be tendered should be directly negotiated by Ofgem with the full detailed information of such development and costs to be provided in the tender.

The possibility of considering a success fee clearly defined in the tender could be a good approach.

Only in the early CATO bidding process one option to incentivize the participation in tenders could be the reimbursement of the partial or total of development cost from non-winners with a minimum defined technical level of innovation in the solution

Question 6: *Should CATOs pay for the preliminary works at the point of transfer?*

Yes, as far as those costs are clearly defined with the tender.

3. How will the tender work and what will CATOs get?

Chapter Summary

We propose to continue to develop both early and late CATO build tender models, although in the short term we intend to prioritize late CATO build. We also propose that CATOs should receive an annual revenue stream fixed over a 25-year period without periodic reviews

Question 1: *What are your views on our proposed late CATO build tender model? Do you have any views on the basis of bids, use of cost-sharing factors or what risks, if any, it would not be efficient for a CATO to manage during construction?*

A preliminary environmental and social route assessment should be guaranteed before the tender, so the implementation of the selected solution be feasible and, any negative impact of the assumptions of the preliminary route not achieved could be recovered by adjustments in tariff.

Question 2: *What are your views on our proposed early CATO build tender model? Do you have any views on what tender specification would best facilitate innovative but deliverable bids, and how we can best manage cost uncertainty after the tender?*

Preliminary assessment should include a high level environmental and social red flag clearance to a first route with a with of 10 km. The basic electrical requirements should be established and let the CATOs define the technical solution in order to try to minimize the costs during the life of the asset.

Question 3: *Do you have any views on the best way to tender projects that use high voltage direct current (HVDC) technology?*

From the point of view of an Investor-EPC Contractor group, if SO procures the Converter Station, this would reduce the interest in participating in that specific tender and may pose some risks for the group when accepting the transfer of that procurement contract

It may be not so economical to the consumer that the HVDC conversion substation is preselected because reduces the optimization possibilities of the CATOs and the assumptions of risks from the transfers could reduce competition in tender.

Question 4: *Do you have any views on our proposal to prioritise late CATO build? Do you have any views on specific circumstances where early CATO build might lead to better outcomes than late CATO build?*

If no advanced works exists at this moment it could be not necessarily more beneficial to wait for the SO to develop preliminary works. Early CATO build could eliminate most of the conflicts of interest that arise in late CATO build.

Question 5: *Do you have any views on how we could mitigate the risk of a CATO not being in place?*

Our company has experience in two different schemes, a) In Brazil the CATO has a fixed revenue term of 30 years with a contractual revenue per year (including the construction period) with transfer at the end of the period at adjusted book value, so, in case that CATO does not timely deliver the project, will suffer a lost of revenue; b) in Chile with 25 years of assured income and after that, regulatory calculated ones. In this case the CATO is penalized with a pre-established penalty for each day or week of delay in delivering the project

Question 6: *What are your views on our proposed revenue package for CATOs? Do you have any views on the proposed* *duration of the revenue term, including how it links to the asset cost recovery period, and whether operations and maintenance costs can be fixed over this period? Do you have any views on our proposed approach to indexation, refinancing and enabling new asset investment?*

The bid may be more competitive if CATO could consider that after the 25 years of fixed tariffs will be remunerated as other TOs up to 45 or more years for the remaining non-depreciated assets. This will allow the assumption of lower returns associated to the first 25 years.

If eventual refinancing gains have to be shared with the customers, the inclusion of such eventual improvement may not be considered by the CATO at the tender phase if future benefits of such refinancing are very reduced compared with the risks assumed.

Partial Indexation could be OK offering the percentage to be indexed, but will complicate the comparison of offers because should be defined a LCO Tariff calculation

Question 7: *What are your views on our proposed package of financial incentives for CATOs? Do you have any views on how we could structure an availability-based incentive to ensure CATOs operate their assets with a 'whole network' view? Do you have any views on whether there are circumstances under which 'payment on completion' would not be appropriate to incentivize timely asset delivery?*

To facilitate financing, we suggest that the penalty for non availability should be caped monthly and yearly.

Question 8: *Are there other types of incentives not covered in this chapter that you think should apply to CATOs?*

The income from assets could be recognized permitting partial beginning of operation.

Also early beginning of operation should be encouraged allowing it and giving a bonus to the CATOs, let say double its monthly income in case of advance in COD.

4. Managing conflicts of interest

Chapter Summary

The roles of incumbent TOs and the SO could lead to conflicts of interest or opportunities to give one party an advantage in the competitive process. We think there should be transparent measures to ensure that there is a level playing field for all participants and no one is able to unduly benefit from the competitive tender process. Further details are set out in Appendix 6.

***Question 1**: Are there any risks or conflicts of interest arising from the SO's role that we haven't identified?*

During implementation phase before operation phase, the SO maybe should act to decide between CATOs and or other CATO and TOs in the interferences and existing assets access that could benefit one or another if it is not a completely independent entity.

***Question 2**: Are there any risks or conflicts of interest arising from the participation of incumbent onshore TOs that we haven't identified?*

In order to minimize the interference between existing TOs and CATOs and clearly establish responsibilities, using of existing TOs assets should be minimized or at least the new CATO assets should be physically separated with independent operation. The access to existing TOs installation should be allowed and full information to the bidding CATO of the existing TO asset, during preparation of the offer, the design, construction and commissioning should be provided.

***Question 3**: Are there any additional conflicts of interest that we haven't identified?*

There may be unidentified interferences in the construction phase that will require access to existing assets, approval of designs, supervision, share of information, commissioning of SO, TOs and CATOs

***Question 4**: What measures do you think would be appropriate to mitigate the risks and conflicts of interest? What additional conflict mitigation measures would be needed if the SO takes on a broader role in supporting competition?*

One way to minimize the advantage that the SO or TOs have gained having undertaken the preliminary works is that the scope, disclosure and costs of the recognized works should be agreed by Ofgem and to be sure that the disclosure of the designs/ routes /licenses /permits/ terrains that will be necessary to develop the project are acquired and validated previously so the price and quality of that assets are previously recognized.

In other countries existing TOs have been restricted to participate in tenders during the first stages of the privatization processes or at least having a majority position in Consortiums, so their participation would be allowed in consortiums controlled by new entrants in the market.

Also limitations in owning more than a fixed market percentage has been used in some countries to limit the participation of exiting TOs until the market is well developed.