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for energy consumers

National Grid North Sea Link  
Limited and other interested  
parties

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Date: 23 July 2018

Dear stakeholders,

### **Decision on proposed changes to the electricity interconnector licence held by National Grid North Sea Link Limited**

In January 2018 we conducted a statutory consultation on proposed changes to the electricity interconnector licence held by National Grid North Sea Link Limited (NGNSL).<sup>1</sup> These changes were required in order to implement the cap and floor regime.

Following consideration of the responses to our consultation, we have decided to implement these licence modifications. Notice of licence modifications is published as Appendix 1 alongside this decision. Our decision to make these licence changes will take effect from 28 September 2018.

#### **Consultation responses**

We received four responses to the consultation. The responses were non-confidential and have been published alongside this decision. A summary of the points raised by the respondents, together with our views on the points raised and whether these impact the licence drafting, is set out in Appendix 3 below.

#### **Minor changes to licence drafting since the consultation**

We have made a few changes, primarily for clarification and to correct minor typographical errors, to the licence drafting set out in our January consultation. We have also decided, in response to stakeholder comments, to insert a new paragraph (3) within special licence condition 11<sup>2</sup> to ensure that specific key financial parameters calculated using the NSL Cap and Floor Financial Model (NSLCFFM) are added to the licence once determined by the Authority. These changes are set out in Appendix 2 and are tracked in the updated version of the licence conditions, published as Schedule 1 to this decision.

#### **Licence modification decisions**

Following consideration of the responses received, we are now proceeding to make the licence changes. Modification decision notices together with relevant schedules have been published alongside this letter as follows:

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<sup>1</sup> Our January 2018 statutory consultation is available at: <https://www.ofgem.gov.uk/publications-and-updates/statutory-consultation-proposal-insert-new-conditions-electricity-interconnector-licence-held-national-grid-north-sea-link-limited-ngnsl>

<sup>2</sup> North Sea Link Cap And Floor Financial Model Governance

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| Appendix 1 – Notice of licence modification                          | <ul style="list-style-type: none"> <li>• Schedule 1 – Special conditions for the electricity interconnector licence held by NGNSL</li> </ul> |
| Appendix 2 – Changes made to licence drafting since the consultation |  |
| Appendix 3 – Summary of consultation responses                       |  |
| Appendix 4 – Section G Direction                                     |  |

Alongside this letter, we have also published updated guidance on the cap and floor conditions of NGNSL’s licence.<sup>3</sup> The Authority has also issued a Direction to bring into effect Section G (Cap and Floor Conditions) of the standard licence conditions.<sup>4</sup>

If you have any questions in relation to this letter please contact Okon Enyenihi by email ([okon.enyenihi@ofgem.gov.uk](mailto:okon.enyenihi@ofgem.gov.uk)) or on 0207 901 7017.

Yours sincerely,

**Mark Copley**  
**Deputy Director, Wholesale Markets & Commercial**

<sup>3</sup> We previously published a draft version of the guidance as part of our statutory consultation on the proposed licence changes: [https://www.ofgem.gov.uk/system/files/docs/2018/01/nsl\\_licence\\_guidance\\_jan\\_2018\\_1.pdf](https://www.ofgem.gov.uk/system/files/docs/2018/01/nsl_licence_guidance_jan_2018_1.pdf)

<sup>4</sup> The Section G of the standard licence conditions are switched off by default for all electricity interconnector licensees until the Authority issues a Section G (Cap and Floor Conditions) Direction to switch them on.

## Appendix 2: Changes made to licence drafting since the consultation

We have made the following changes to the licence drafting for clarification and to correct minor typographical and formatting errors. We have also added a new paragraph 3 to special licence condition 11.

All changes made to each of the NSL special conditions have been tracked throughout the licence (published as Schedule 1 alongside this decision).

| Condition   | Reference                       | Change made   |
|---|---------------------------------|---|
| Special Condition 1: Definitions and Interpretation | "Allowed Outage"                | Definition on "Allowed Outage" moved to special condition 1 from Part G of special condition 4  |
| Special Condition 1                                 | "Preliminary Cap Level" (PCL)   | Reference to paragraph '11' amended to '12'   |
| Special Condition 1                                 | "Preliminary Floor Level" (PFL) | Reference to paragraph '11' amended to '12'   |
| Special Condition 1                                 | 'First Year of Operation'       | The wording is amended to make it clearer from <i>'means the period starting from the Full Commissioning Date and ending a full calendar year later'</i> to <i>'means a full calendar year starting on the Full Commissioning Date'</i>   |
| Special Condition 2: Cap Level and Floor Level      | Paragraph 4                     | Amendment to paragraph reference. Paragraph: <ul style="list-style-type: none"> <li>- '16' amended to '17' within the definition of AICt term</li> <li>- '17' amended to '18' within the definition of AIFt term</li> <li>- '11' amended to '12' within the definition of PCL term</li> <li>- '11' amended to '12' within the definition of PFL term</li> </ul> |
| Special Condition 2                                 | Paragraph 7(a)                  | Reference to <i>'such an interconnector'</i> changed to <i>'the licensee's interconnector'</i>  |
| Special Condition 2                                 | Paragraph 7(b)                  | Reference to paragraph '10' amended to '11'   |
| Special Condition 2                                 | Paragraph 8(b)                  | Reference to 'Exceptional Events' amended to 'Trial Operation Exceptional Event or Allowed Outage'  |
| Special Condition 2                                 | Paragraph 9                     | New paragraph 9 inserted to provide the meaning of 'Trial Operation Exceptional Event'  |
| Special Condition 2                                 | Paragraphs 10 to 22             | Paragraph numbers updated from '9 to 21' to '10 to 22'  |
| Special Condition 2                                 | Paragraph 12(b)                 | Reference to paragraph '13' amended to '14'   |
| Special Condition 2                                 | Paragraph 12(e)                 | Reference to paragraph '12' amended to '13'   |
| Special Condition 2                                 | Paragraph 13                    | Reference to paragraph '12' amended to '13'   |

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| Special Condition 2  | Paragraph 14(b)                                      | Reference to paragraph '15' amended to '16'   |
| Special Condition 2  | Paragraph 14(e)                                      | Reference to paragraph '14(a) to 14(d)' amended to '15(a) to 15(d)'   |
| Special Condition 2  | Paragraph 15   | Reference to paragraph '14(a) to 14(d)' amended to '15(a) to 15(d)'   |
| Special Condition 2  | Paragraph 18   | Amendment to paragraph reference. Paragraph: <ul style="list-style-type: none"> <li>- '19(a)' amended to '20(a)' within the definition of UK RPI index term</li> <li>- '19(b)' amended to '20(b)' within the definition of UK RPI index term</li> </ul> |
| Special Condition 2  | Paragraph 21(b)                                      | Amendment to paragraph reference. Paragraph: <ul style="list-style-type: none"> <li>- '20' amended to '21' within the definition of PYCt term</li> <li>- '21' amended to '22' within the definition of PYFt term</li> </ul>                             |
| Special Condition 3: Cap and Floor Assessment              | Paragraph 17   | In the calculation of NODRt term, 'RPIt' term amended to 'CRPIt' term   |
| Special Condition 3  | Paragraph 17   | 'part F' amended to 'Part F' in the definition of 'RPIt' term   |
| Special Condition 3  | Paragraph 18   | New paragraph 18 inserted setting out the formula for calculating CRPIt term  |
| Special Condition 3  | Paragraph 18   | The reference to 'part F' within the definition of RPIt amended to 'Part F'   |
| Special Condition 3  | Paragraphs 18 to 24                                  | Paragraph numbers updated from '18 to 24' to '19 to 25'   |
| Special Condition 4: Interconnector Availability Incentive | Paragraph 21   | The wording 'the additional requirement that' deleted   |
| Special Condition 4  | Paragraph 21   | The wording 'be treated as if the Minimum Availability Target has been met' replaced with 'set to 1'  |
| Special Condition 4  | Paragraph 29(a)                                      | The reference to paragraph '20' amended to '21'   |
| Special Condition 4  | Paragraph 29(b)                                      | The reference to paragraph '20' amended to '21'   |
| Special Condition 4  | Paragraph 31(b)                                      | The reference to paragraph '21' amended to '22'   |
| Special Condition 4  | Paragraph 32(a)                                      | The meaning of 'Allowed Outage' amended to include ' <i>or reductions in capacity'.....'or any other entity as may be determined by the Authority'</i> . The definition of "Allowed Outage" moved to special condition 1.                               |
| Special Condition 4  | Paragraph 32 (definition of 'Interconnector Outage') | The wording 'in either direction' deleted   |

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| Special Condition 7: Non-Controllable Costs  | Paragraph 12    | The word 'cost' amended to 'Cost' in the definition of Non-Controllable Operational Cost Items (ONCOct)   |
| Special Condition 7  | Paragraph 13    | A new term 'PYAFt' added to the formula for calculating BNCOct term   |
| Special Condition 7  | Paragraph 13    | Meaning of PYAFt added  |
| Special Condition 7  | Paragraph 17(b) | The wording 'the additional requirement that' deleted   |
| Special Condition 7  | Paragraph 17(b) | The wording 'be treated as if the Minimum Availability Target has been met' replaced with 'set to 1'  |
| Special Condition 7  | Paragraph 36    | Amendment to paragraph reference. Paragraph: <ul style="list-style-type: none"> <li>- '16' amended to '17' within the definition of AICt term</li> <li>- '17' amended to '18' within the definition of AIFt term</li> <li>- '11' amended to '12' within the definition of PCL term</li> <li>- '11' amended to '12' within the definition of PFL term</li> </ul> |
| Special Condition 8: Process for determining the value of the Post Construction Adjustment terms | Paragraph 9(b)  | The word 'specify' amended to 'specifies'   |
| Special Condition 8  | Paragraph 16    | The wording ' <i>through a public consultation</i> ' inserted within paragraph 16   |
| Special Condition 11: North Sea Link Cap And Floor Financial Model Governance                    | Paragraph 2     | The wording ' <i>is a stand-alone document and</i> ' deleted.   |
| Special Condition 11   | Paragraph 3     | A new paragraph 3(a)-(d) has been added.  |
| Special Condition 11   | Paragraph 14    | Definitions for the terms (PCAC, PCAF, ORAC and ORAF) added.  |

### Appendix 3: Summary of consultation responses

| Respondent                                      | Condition Ref  | Comments   | Our views   | Changes to licence drafting   |
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| NSL / National Grid NSL                         | Special condition 1: Definitions and Interpretations (page 2, paragraph 4) | <p>1) For the availability incentive at the cap to be fully effective, actual availability at all times should be amended for exceptional events, not just at the floor.</p> <p>2) During the period of 60 days of continuous operation which is required to meet the Full Commissioning Date, exceptional events should be discounted irrespective of the effect on the annual Actual Availability.</p> | <p>1) We reject the view that the availability incentive will not function as intended. We have previously made clear in Nemo Link's licence consultation that the mechanism allowing the licensee to be 'deemed' available for outages caused by an exceptional event will only be considered at the floor.</p> <p>2) We recognise that the definition of Exceptional Event is impossible to be met in the trial period and have added a new defined term 'Trial Operation Exceptional Event' as paragraph (9) of special condition 2.</p> | No change to the definition of 'Exceptional Event' rather, we have added a new defined term: 'Trial Operation Exceptional Event' as paragraph (9) of special condition 2. |
| NSL / National Grid NSL / FAB Link / Neuconnect | Special condition 1: Definitions and Interpretations (page 3, paragraph 2) | <p>1) Propose to add 'strike, lockout or other industrial disturbance and other legislation' etc to the definition of force majeure.</p> <p>2) The current Force Majeure definition is inconsistent with the System Operator – Transmission Owner Code (STC).</p>  | <p>1) We do not consider it appropriate for risks from the events described here to be borne by consumers. We consider such risks largely to be normal business risks that should be managed by developers. This is consistent with our cap and floor policy decisions, such as our 2014 decision on Nemo Link.</p>   | No change   |

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|                         |  |   | 2) We consider that the STC and our cap and floor regime are different frameworks. The cap and floor regime is designed to encourage efficient investment in interconnectors - the regime provides specified and limited protection from downside risk.  |                            |
| NSL / National Grid NSL | Special condition 1: Definitions and Interpretations (page 3, paragraph 5) | 1) Proposes to change the definition of Interconnector Revenue to reflect the actual revenue earned by the licensee not 50% of the total revenue of the interconnector. | 1) We consider the current definition to be appropriate. In addition, the Initial Project Assessment for the interconnector and the granting of a cap and floor regime is based on revenues being shared equally between the licensee and its partner Statnett.  | No change.                 |
| Neuconnect              | Special condition 2: Cap and Floor levels                                  | 1) The Authority should be more flexible and provide more clarity on Exceptional Events and Force Majeure that may affect the regime start date.                        | 1) We do understand that sometimes delays are caused by external factors and have therefore excluded the duration of any delays caused by force majeure events. More detail is provided under 'Proposed relief for delays to regime start date for force majeure' within our June 2017 update to cap and floor regime for Window 1 interconnector projects. <sup>5</sup> | No change.                 |
| FAB Link                | Special condition 2: Cap and Floor   | 1) Periods in which the interconnector is in an   | 1) We will maintain the approach of discounting such periods. This is  | No change to proposal (1). |

<sup>5</sup> <https://www.ofgem.gov.uk/ofgem-publications/117512>

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|   | Levels (Page 8, Paragraph 7 and 8)   | <p>operational situation however no power is flowing because of insufficient price differential should be considered as contributing to the 60 day period.</p> <p>2) Suggest adding a separate and new defined term to cover Exceptional Events and Allowed Outage that may happen during the Trial Operations period.</p>  | <p>because the proving period is designed to demonstrate the ability of the interconnector to flow power.</p> <p>2) We agree with this proposal and have inserted a new defined item. We have also added Allowed Outage to paragraph 8(b).</p>  | <p>In response to proposal (2), we have inserted a new defined item "Trial Operation Exceptional Events" within special licence condition 2 and added 'Allowed Outage' to paragraph 8(b).</p> |
| FAB Link, NeuConnect, NSL / National Grid NSL | Special condition 4: Interconnector Availability Incentive (Pages 24, 27 and 28) | <p>1) Maximum Possible Availability is calculated in a single direction however; outages can be in either direction.</p> <p>2) Consider Interconnector Outages only if flows/capacity sales are impacted or more simply by considering Maximum Possible Availability in both directions simultaneously.</p> <p>3) The definition of "Allowed Outage" only considers disconnection or curtailment by the GB or Norwegian SO's. It needs expanding to take account of the</p> | <p>1) Outages in one direction are measured against the Maximum Possible Availability in that direction. This approach considers availability in each direction in turn reflecting the fact that flows will occur in one direction at any point in time and not simultaneously in both directions.</p> <p>2) The interconnector availability incentive aims to encourage licensees to maintain technical availability of the interconnector in both directions throughout the regime duration.</p> <p>3) We have modified the definition of 'Allowed Outage' to include other entities and reduction in</p> | <p>No change based on (1), (2), (4), (5) and (7).</p> <p>Definition of 'Interconnector Outage' and 'Allowed Outage' modified to address comments (3) and (6).</p>                             |



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|  |  | <p>provisions of the Network Codes.</p> <p>4) The Authority should provide further guidance and specific circumstance of situations in which a notice given by the licensee that an Exceptional Event has occurred may be denied by the Authority.</p> <p>5) The Floor is subject to large risk of removal if licensee misses the MAT. The requirement that IAT must exceed 5% of the Floor level should be relaxed.</p> <p>6) The current definition of Interconnector Outage as <i>"any reduction in MWh of Maximum Possible Availability of the licensee's Interconnector in either direction"</i> effectively double counts reductions.</p> <p>7) Amend the formula that calculates Actual Availability</p> | <p>capacity as may be determined by the Authority.</p> <p>4) We note that Part A of special licence condition 4 sets out the relevant principle that will guide the Authority's consideration of any Exceptional Event notice given by the licensee.</p> <p>5) We note that the regime already considers exceptional events when assessing whether the MAT is met. We consider the 5% threshold as appropriate.</p> <p>6) The definition of Interconnector Outage has been modified and is now consistent with the wording in Nemo Link's licence.</p> <p>7) The Actual Availability formula includes 'Allowed Outage', which discounts outages that are caused as a result of curtailment by the System Operator and any other entity as may be determined by the Authority. Exceptional Events (which must be Force Majeure events) are only considered at the floor and when such an event causes the licensee to miss the</p> |  |
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|                         |  | to include adjustments to the calculation of availability at the cap for force majeure related outages.  | Minimum Availability Target. We believe that current drafting allows the availability incentive to function as intended.   |           |
| NSL / National Grid NSL | Special condition 5: Assessed Revenue (Part B: page 30, paragraph 6) | 1) Provide further clarity for the terms: ASRN <sub>t</sub> , CAR <sub>t</sub> , CMR <sub>t</sub> to ensure it refers only to the licensee's revenue, not the total revenue, which is shared with Statnett i.e. similar to the terms: CPN <sub>t</sub> , CPGB <sub>t</sub> , RIt which all refer to the income "receivable by the licensee". | 1) We do not think a modification is necessary. We note that special licence condition 1 defines Interconnector Revenues as ' <i>50% share of all sources of revenue derived by the licensee's Interconnector, for Relevant Year t, from participating in the operation of the licensee's Interconnector</i> '. This definition covers all forms of revenues generated by the licensee's interconnector. | No change |
| NSL / National Grid NSL | Special condition 5: Assessed Revenue (Part C: page 31, paragraph 8) | 1) Only the costs and revenues borne by the licensee should form part of the assessment. This is because costs and revenues will not always be shared equally between NSL and its joint venture partner Statnett.  | 1) We expect the costs incurred by the licensee to be broadly 50% of the total cost, with some specific deviation as set out in our FPA decision. Revenues should always be 50% of the total revenue derived by the interconnector (ie the joint venture between the licensee and Statnett).   | No change |
| NSL / National Grid NSL | Special condition 5: Assessed Revenue (Part                          | 1) The current approach to the assessment of Additional Revenue does not allow enough innovation to occur. Prefers that  | 2) Our view is that the current drafting provides sufficient scope for the licensee to explore additional revenue streams as necessary. No up-front  | No change |

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|            | D: page 32 - 33)   | all costs for developing additional revenue streams will be recovered to the extent to which they are covered by revenues.   | approval is required from Ofgem before the licensee can develop additional revenue streams. However, the Authority must approve a revenue source (and all related development and associated costs) as being an additional revenue source either before or after the fact.  |   |
| FAB Link   | Special condition 6: Within Period Adjustment, page 41, paragraph 17 (b) | <p>1) Income Adjusting Event (IAE) is only triggered if a single event results in an impact of at least 5% of the floor. Proposes this should instead consider the cumulative effect of multiple potential events.</p> <p>2) Propose the following amendment: <i>'...with the additional requirement that the Availability Incentive at Floor (AIFt) term set to 1.00. be treated as if the Minimum Availability Target has been met.'</i></p> | <p>1) The regime sets a threshold of 5% of the Floor Level for a single IAE. It is our view that the Floor already provides adequate protection ensuring that licensees can continue to operate and service debt in the event of multiple IAEs.</p> <p>2) We welcome the proposal and believe that the drafting is clearer.</p> | <p>(1) The proposal to allow multiple events to count towards the threshold of 5% of the Floor Level is not accepted.</p> <p>(2) We accept the second proposal and have amended the text as proposed.</p> |
| Neuconnect | Special condition 7: Non-Controllable Costs                              | 1) UK consumers stand to benefit from half of all revenues under the cap and floor regime. But the definition of Non-controllable cost does not include similar changes to costs in the connecting jurisdiction.   | 1) In the NSL FPA decision, GB specific non-controllable costs are covered by the regime (100%) and non-GB specific (Norway) non-controllable costs are not covered by the regime (0%). We expect the non-controllable costs specific to the connecting   | No change   |

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|                         |  |  | market to broadly equate to the GB specific non-controllable costs.  |  |
| NSL / National Grid NSL | Special condition 7: Non-Controllable Costs, Part C: page 40, paragraph 13)                                    | 1) Baseline Non-Controllable costs (BNCOA term) should be revised to capture first and last relevant years as partial years.                     | 1) This proposal is accepted. The BNCOA term, in the first and last relevant years, has been adjusted by a partial year adjustment factor.   | PYC <sub>t</sub> term added to the formula to account for partial years.<br><br>$BNCOA_t = BNCOA \times RPI_t \times PYAF_t$   |
| NSL / National Grid NSL | Special condition 7: Non-Controllable Costs, Part D: page 40 - 43)   | 1) Costs associated with IAE should be fully passed through to consumers.  | 1) We do not think it is appropriate for GB consumers to bear this cost when revenue is between the cap and the floor. The regime permits IAE cost recovery when revenue is either above the cap (reflecting benefit sharing between consumers and licensees) or below the floor (where IAE cost is fully passed on to consumers). When revenue is between the cap and the floor developers should bear this cost. | No change  |
| NSL / National Grid NSL | Special condition 8: Process for determining the value of the Post Construction Adjustment terms: page 48 - 49 | 1) Ofgem has considerable discretion in deriving cap and floor values, without the licensee having the right of appeal on the merits to the CMA. | 1) We disagree with this view. The regime and the process of setting the Cap and Floor Levels have gone through extensive non-statutory and statutory consultations. The licence itself provides a governance framework for the NSL Cap and Floor Financial Model. We note that we have made further modifications to special condition 11.  | We have modified special condition 11. This ensures that licensees can provide views on changes to key financial parameters once determined by the Authority and written into the licence. |

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| FAB Link  | Special condition 8: Process for determining the value of the Post Construction Adjustment terms: page 49, paragraph 17 | 1) Propose the following amendment to the licence: " <i>If the PCR is not completed within the First Year of Operation, we reserve the right to disallow NSL any Within Period Adjustments will be subject to a reconciliation until once the Post Construction Review is completed and final Cap Level and Floor Level are established</i> " | 1) We believe that the current licence drafting allows for a Within Period Adjustments in the first four years of each regime period (5-years) when certain conditions are met. Our view is that these conditions protect consumers by ensuring the licensee submits complete documentation on time for the PCR process to be completed and the final Cap and Floor Levels determined. | No change                      |
| NSL / National Grid NSL / Neuconnect / FAB Link | Special condition 11: NSLCFFM Governance: pages 55 – 57   | 1) Ofgem has considerable discretion in deriving cap and floor values, without the licensee having the right of appeal to the CMA.  | 1) We have modified special condition 11 to allow key financial parameters to be included in the licence once determined by the Authority.   | Special condition 11 modified. |
| <b>General comments</b>                         |   |   |  |                                |
| <b>1</b>  | Cap and Floor Framework   | 1) Need for clear regulatory principles setting out a consistent and transparent end-to-end process.<br><br>2) Need for appropriate consultation and appeal rights.   | 1) We believe that the cap and floor framework as well as the licence implementation for Nemo Link and, now, NSL both provide reasonable regulatory clarity and will continue to work with stakeholders on this issue.<br><br>2) Please refer to our response under special condition 11.  |                                |