EXPLANATORY MEMORANDUM TO

THE ELECTRICITY (INDIVIDUAL EXEMPTIONS FROM THE REQUIREMENT FOR A TRANSMISSION LICENCE) (ENGLAND AND WALES) ORDER 2019

2019 No. 106

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Business, Energy & Industrial Strategy and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 To grant exemptions from the requirement to hold an electricity transmission licence to Race Bank Wind Farm Limited in respect of Race Bank offshore wind farm, Galloper Wind Farm Limited in respect of Galloper offshore wind farm, Walney Extension Limited in respect of Walney Extension offshore wind farm and Rampion Offshore Wind Limited in respect of Rampion offshore wind farm.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments.

3.1 None.

Matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business (English Votes for English Laws)

3.2 As the instrument is subject to negative resolution procedure there are no matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business at this stage.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is England and Wales.

4.2 The territorial application of this instrument is England and Wales.

5. European Convention on Human Rights

5.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

6. Legislative Context

6.1 Section 4(1)(b) of the Electricity Act 1989 ("the Act") makes it an offence for a person to participate in the transmission of electricity for the purpose of giving supply to premises without a licence ("a transmission licence"). Section 5(1) of the Act enables the Secretary of State to grant an exemption from (amongst other requirements) the requirement to hold a transmission licence. The exemption can be revoked by the Secretary of State for the reasons set out in section 5(8) of the Act.

6.2 A transmission licence may be granted by the Gas and Electricity Markets Authority ("Ofgem") under section 6(1)(b) of the Act.

6.3 The requirement to hold a transmission licence does not apply where sections 6F and 6G of the Act apply. Those provisions allow offshore generators to transmit electricity without a transmission licence during the "commissioning period" (as defined in section 6G(1) of the Act).

6.4 The commissioning period includes the period before and during the 18 months beginning on the day the National Grid Electricity System Operator issues a completion notice to the developer and notifies Ofgem in respect of the transmission asset. In this context, following the end of the commissioning period, unlicensed transmission by an offshore generator is an offence under section 4(1)(b) of the Act, unless an exemption from the requirement to be licensed is granted. This Order grants exemptions in respect of four offshore generators.

7. Policy background

What is being done and why?

7.1 Government and the Gas and Electricity Markets Authority (more commonly known as Ofgem) established a regulatory regime for offshore transmission networks. Offshore transmission connections to offshore wind farms are licensed through a competitive regime managed by Ofgem to ensure that offshore renewable generation projects are economically and efficiently connected to Great Britain's electricity grid. It underpins the Government's renewable energy targets by placing the requirements of renewable generators and Great Britain's electricity consumers at the forefront.

7.2 Whilst transmission assets can be built and tested by an independent offshore transmission owner ("OFTO"), all projects in the UK to date have been built and tested by generators. EU 'unbundling' rules prevent transmission and generation infrastructure being owned and operated by the same party.[1]

7.3 To select an OFTO to own and operate the transmission asset, after it is transferred by the generator during the commissioning period, Ofgem runs a tender exercise.

7.4 Ofgem also grants a licence and fixed revenue stream for a specified period, which is set at 20 years for all the projects in tender round 5.

7.5 The commissioning period, as set out in paragraph 6.3, is designed to allow the transmission asset to be transferred to an independent OFTO under the OFTO regime, as the Act anticipates on completion of the project (as indicated by the completion notice provided to Ofgem). The commissioning period allows for the technical demonstration of the asset, gives time for Ofgem to run a tender process and select a preferred bidder for the OFTO, and provides time to finalise commercial negotiations ahead of the transfer of assets. It is generally considered that 12 months is required to successfully conclude the commercial negotiations following appointment of the preferred bidder. Beyond the 18-months of the commissioning period, the generator is prevented from continuing to transmit electricity, as doing so would constitute the transmission of electricity without a licence, which is an offence under section 4(1)(b) of the Act.

[1] However, the drivers for unbundling are primarily around non-discriminatory access to the network. If a generator owns a transmission asset, there is a risk that they prioritise access to the asset to their own generation at the expense of competitors (but for a point-to-point cable with a single generator at the end, this risk is significantly reduced).

7.6 Ofgem groups projects together in OFTO tender rounds so that tender rules can be consistently applied across the projects, and bidders have better visibility of the projects coming forward. The process for Ofgem's OFTO tender round 5 projects was significantly delayed for the following reasons: (i) more projects progressing to the tender stage than expected, which stretched the Ofgem resources allocated for tender round 5; (ii) Ofgem's decision to stagger the invitation to tender phases for individual projects so that the preferred bidder for one tender was identified before Ofgem launched the invitation to tender ("ITT") for the next project. This was done to address feedback from bidders that it is challenging to pursue multiple projects in parallel; and (iii) Ofgem consulting on a review of its policy on Income Adjusting Events, which resulted in additional delays to the process as resourcing constraints meant it was not possible to issue further invitations to tender until the policy was finalised.

7.7 These delays mean it is very likely that the offshore generators in tender round 5 (identified in paragraph 2.1 above) will, despite best endeavours to work with Ofgem to progress tenders, find themselves in a position where they have not completed the transfer of transmission assets within the 18-months of the commissioning period. After this, they will be unable to continue to lawfully transmit electricity to the grid.

7.8 The exemptions will come into effect at the end of the 18-months of the commissioning period for each generator and will expire on the relevant date specified in the instrument, or upon transfer of ownership of the transmission asset to an OFTO if that is earlier. For each project, the specified end date for the exemption is 24 months after whichever is the later of the launch of the ITT phase of the tender process or the issue of the completion notice. This accounts for the delays to the tender process and will ensure the projects have sufficient time to conclude commercial negotiations to facilitate the transfer to an OFTO.

7.9 The instrument will effectively extend the period during which these generators can transmit electricity without a licence to 24 months, to account for exceptional delays to the tender process. Without the instrument, the relevant generating stations would be prevented from transmitting lawfully, and hence be prevented from generating electricity. This will be the first time that the powers granted to the Secretary of State under Section 5 of the Act will have been used to grant an exemption from the requirement to hold a transmission licence.

7.10 Race Bank Wind Farm Limited, Galloper Wind Farm Limited, Walney Extension Limited and Rampion Offshore Wind Limited have each requested a temporary exemption from the requirement to hold an electricity transmission licence, in respect of the transmission taking place over the transmission system connected to a specific offshore wind farm (the relevant generating stations are described in the table in article 2 of the instrument).

7.11 Each generator requested an exemption well in advance of the end of its commissioning period based on concerns about the delay, or anticipated delay, to the ITT phase starting and/or delays to the announcement of a preferred bidder.

7.12 Race Bank Wind Farm Limited requested an exemption on 20 April 2018, approximately 11 months before the end of its commissioning period. Race Bank's completion notice had been issued on 12 September 2017. The ITT phase started on 10 November 2017 and a preferred bidder was announced on 20 June 2018. This left

less than 9 months for Race Bank to complete commercial negotiations ahead of the end of their commissioning period on 11 March 2019.

7.13 Galloper Wind Farm Limited requested an exemption on 7 June 2018, approximately 15 months before the end of its commissioning period. Galloper's completion notice was issued on 13 March 2018 and the ITT phase started on 5 March 2018. A preferred bidder was announced on 22 November 2018 leaving less than 10 months for commercial negotiations ahead of the end of their commissioning period on 12 September 2019.

7.14 Walney Extension Limited requested an exemption on 10 May 2018, approximately 16 months before the end of its commissioning period. Walney Extension's completion notice was issued on 21 March 2018 and the ITT process was started on 13 June 2018. A preferred bidder is expected to be appointed in mid-January 2019, leaving 8 months for commercial negotiations ahead of the end of their commissioning period on 20 September 2019.

7.15 Rampion Offshore Wind Limited requested an exemption 8 June 2018, approximately 11 months before the end of its commissioning period. Rampion's completion notice was granted on 21 November 2017 and the ITT phase started on 28 Nov 2018. A preferred bidder is expected to be appointed in June 2019, after the end of their commission period on 20 May 2019.

7.16 In carrying out functions under Part 1 of the Act (including considering granting any exemption from the requirement to hold a transmission licence), the Secretary of State is required under section 3A of the Act to further the principal objective, which is to protect the interests of existing and future consumers in relation to electricity conveyed by distribution systems or transmission systems (including the reduction of emissions of targeted greenhouse gases), wherever appropriate by promoting effective competition between persons engaged in, or in commercial activities connected with, the generation, transmission, distribution or supply of electricity.

7.17 In furthering the principal objective, the Secretary of State should have regard to, among other things, the need to ensure security of supply and the need to contribute to the achievement of sustainable development. In addition, the Secretary of State's regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed. The Secretary of State considers it would further the principal objective of the Act to grant time-limited exemptions to those generators adversely affected by the delays in tender round 5.

7.18 The exemptions promote consumers' interests by protecting these generators from the adverse legal and commercial consequences of tender round 5 delays, which supports the continued investment and competition in the sector. Providing exemptions to these assets also directly supports future reductions in greenhouse gases by ensuring that offshore wind farms can continue to transmit low-carbon power to the grid for the limited time required for the transfer of transmission assets to be completed. The proposed exemptions will allow the affected generators a sufficient window in which to successfully transfer transmission assets so that their generation is not interrupted. This is in line with the overall objective of the Government's Clean Growth Strategy to enable economic growth while cutting greenhouse gas emissions.

7.19 Guidance on the Department's approach to generation, distribution and supply licence exemptions is published on the Government website, including the 'frequently asked

questions' document.[2] This does not explicitly set out circumstances in which transmission licence exemptions would be granted, but does set out general principles, which has informed our approach in considering these exemptions. These principles include that, in determining applications, the Secretary of State should take account of the impact of the exemption on the safe and secure operation of the electricity system, and the interests of consumers. For example, exemptions are routinely granted to generators of less than 100MW capacity due to their low impact on the total electricity system.

7.20 The continued operation of the assets covered by the proposed exemption does not threaten the safe and secure operation of the total electricity system for the following reasons: (i) The offshore transmission assets, operated by the offshore generators to be granted exemptions, do not have the same complexities as onshore transmission - they are point-to-point transmission cables, and are functionally simple connections to one generator rather than part of a complex grid that requires more active management by the Electricity System Operator, and (ii) in that context, the Electricity System Operator already operates the system safely and securely while these generators are generating during the commissioning period.

8. European Union (Withdrawal) Act/Withdrawal of the United Kingdom from the European Union

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act 2018.

9. Consolidation

9.1 None.

10. Consultation outcome

10.1 A notice was published on the Government website setting out the proposal to make the instrument, containing the terms of the instrument, and inviting representations, on 4 December 2018[3].

10.2 The notice period closed on 2 January 2019 and ten representations were received.

10.3 All ten responses supported the general proposal to grant the proposed exemptions. Eight of the responses supported the proposal in its entirety and made no suggestions for changes.

10.4 One response, from an OFTO investor and active bidder in the tender round, expressed a view that the proposed 24-month duration of the exemptions is too long and could reduce the incentive for generators to conclude transfers as quickly as they can, potentially increasing costs for the preferred bidder for the offshore transmission asset. This response offered a view that the exemptions should expire 18 months (rather than the proposed 24 months) after the start of the invitation to tender or 24 months from the issue of the completion notice (whichever is later) because a shorter deadline exerts an incentive on the generator to finalise the transfer, which avoids unnecessary costs for the preferred bidder as a result of extended negotiations. This response commented that the time from the start of the ITT to appointing the preferred bidder is typically 6 months, which in the normal course of business would leave 12

[2] https://www.gov.uk/guidance/electricity-licence-exemptions
[3] https://www.gov.uk/government/consultations/transmission-licence-exemption-order-for-offshore-generators

months for commercial negotiations. The response also commented that Ofgem should have more resource available now it has concluded the policy on Income Adjusting Events, although the Government's view is that this was a contributing factor to the delays thus far, and it would now be very difficult for Ofgem to accelerate the process.

10.5 Overall, the Government still considers the 24-month duration to be appropriate because timelines have generally been much longer in tender round 5 to date. It has taken 2-12 months for the ITT phase to initiate after the issue of completion notice, followed by 7-9 months from the start of the ITT to appointing the preferred bidder. The other nine responses supported the proposed 24-month exemption period, and one offered a view that 24 months would be the minimum required to ensure the objectives of the exemption can be achieved. While we agree that it should be possible to conclude the transfer in less than 24 months, we are concerned that any subsequent, unforeseen delays to the tender round 5 process would undermine the purpose of granting exemptions and fail to deliver the overarching objective as set out in the Notice.

10.6 Several responses also provided additional views that, although providing a fixed end date for each exemption exerted an incentive to finalise the transfer, it puts the generator in a compromised position for the negotiations. However, the Department considers that the way that a generator's transmission charges are calculated provides a commercial incentive to conclude the transfer as soon as possible.

10.7 The majority of views expressed clear support for the exemptions in the terms proposed during the notice period. The Secretary of State has therefore decided that it is appropriate to provide the affected projects with an exemption and to retain the proposed 24-month exemption period to allow sufficient time for commercial negotiations and accounting for the additional delays to the tender process.

11. Guidance

11.1 Several responses highlighted concerns about possible delays in future tender rounds and requested that the Government either publish guidance setting out how transmission licence exemption applications would be considered in the future or amend the OFTO statutory regime to provide more flexibility. Guidance on the Department's approach to generation, distribution and supply licence exemptions is published on the Government website, including the 'frequently asked questions' document.[4] This has informed our approach in considering these transmission licence exemptions. The current situation is considered to arise from exceptional circumstances which are related to delays to the current tender round. Ofgem is in the process of making changes to streamline the tender process for future rounds and we have sought assurances that future tenders will be completed within the 18-month period already provided for in legislation, to the extent that this is within Ofgem's control. We therefore do not intend to publish additional guidance on our approach to transmission licence exemptions.

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 There is no, or no significant, impact on the public sector.

[4] https://www.gov.uk/guidance/electricity-licence-exemptions

12.3 An Impact Assessment has not been prepared for this instrument because it has no significant impact on business, charity or voluntary bodies, satisfying a *de Minimis* limit.

13. Regulating small business

13.1 The legislation does not apply to activities that are undertaken by small businesses.

14. Monitoring & review

14.1 Due to the strictly time-limited nature of the exemptions, there are no formal monitoring or review requirements. There are no conditions attached to the exemptions, but each exempted wind farm must continue to comply with the conditions of its generation licence (including satisfying industry standards).

15. Contact

15.1 Matt Coyne/Amanda Webb and Sophia Cliff at the Department for Business, Energy and Industrial Strategy Telephone: 0300 068 5265/0207 215 6052 and 0207 215 4219 or email: Coyne-Webb.Jobshare@beis.gov.uk and Sophia.Cliff@beis.gov.uk can be contacted with any queries regarding the instrument.

15.2 David Capper, Deputy Director for Electricity Systems, at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.

15.3 Claire Perry, Minister of State for Energy and Clean Growth, at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.