

Review of the Energy Market Investigation (Electricity Transmission Losses) Order 2016

Provisional decision

23 July 2024

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The Competition and Markets Authority has excluded from this published version of the Provisional Decision information which it considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂].

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1. Summary

- 1.1 In line with its statutory duty under sections 92 and 162 of the Enterprise Act 2002 (the Act), the CMA keeps the portfolio of undertakings and orders arising from its markets and mergers work under review, including through considering those undertakings and orders that should be reviewed where there are reasons to suspect that one or more changes in circumstance have taken place.
- 1.2 In March 2024, the CMA was contacted by the Department for Energy Security and Net Zero (DESNZ) regarding the impact of the coming into force of certain provisions in Part 5 of the Energy Act 2023 (EA23)¹ on the [Energy Market Investigation \(Electricity Transmission Losses\) Order 2016](#) (the Order). DESNZ informed the CMA that amendments made to the Electricity Act 1989 (EA89) by Part 5 of EA23, and the proposed establishment of a new Electricity System Operator (ESO), by virtue of Part 5 of EA23, could amount to a change of circumstances that required the Order to be varied. DESNZ requested that the CMA undertake a formal review of the Order on the basis if the Order were not varied, the full implementation of Part 5 of EA23 and establishment of the ESO could unintentionally deprive the Order of continued effect.
- 1.3 The purpose of this review is to determine whether there has been a change of circumstance and if so, to amend the Order to take account of the amendments made to the Electricity Act 1989 by Part 5 of EA23 and the establishment of the ESO.
- 1.4 Given that, in this instance, the CMA considers that the change of circumstances and the outcome that would be required to resolve the resulting regulatory inconsistency would both be clear, the CMA has exercised its discretion to proceed directly to publication of, and consultation on, a Provisional Decision and Notice of Intention to Vary the Order.
- 1.5 This document sets out and gives notice of the CMA's Provisional Decision that relevant changes of circumstances have taken place which means that Part 1 (Article 2.1) and Part 4 of the Order (the Relevant Parts of the Order) are no longer appropriate as currently drafted and should be varied by means of a variation order. The substance of the proposed changes to be made to the Order is set out in the Annex, which covers:

¹ Some provisions in Part 5 of EA23 came into force on Royal Assent (EA23, s.334(2)(h)). Most of its other provisions were brought into force by the Energy Act 2023 (Commencement No. 1) Regulations 2024 (S.I. 2024/32). DESNZ intends that the remaining provisions (s.166(2) and s.168(2)) will be brought into force when the ISOP is designated (see further paragraph 3.7 below).

- (a) In Part 1: Addition in Article 2.1 of new definitions relating to ‘ESO Licence’ and ‘Relevant Direction’ and amendment of the definition of ‘Transmission Company’.
- (b) In Part 4: Addition of a new Article 6A on ‘Effect of Relevant Direction’.
- (c) Equivalent amendments to the Explanatory Note to the Order.

1.6 The CMA is now consulting on the Provisional Decision and proposed changes set out in the Annexes before it makes its Final Decision. Respondents should provide their views, supported with relevant evidence where possible, in writing to the CMA at:

Email: remedies.reviews@cma.gov.uk (Subject line: ‘Energy (ETL) Order’)

Responses should be provided to the CMA by **5pm on Friday 23 August 2024**. The CMA requests that all submissions be accompanied by a non-confidential version which the respondent would be willing to have published on the CMA website at the time that the CMA’s final decision is published.

2. Legal Framework

- 2.1 The CMA has a statutory duty under section 162 of the Act to keep under review undertakings and orders accepted or made under the Act.² From time to time, the CMA must consider whether, by reason of any change of circumstances:
- (a) undertakings are no longer appropriate and need to be varied, superseded or released; or
 - (b) an order is no longer appropriate and needs to be varied or revoked.
- 2.2 The nature of the CMA's consideration of any change of circumstances will depend on the individual circumstances affecting a particular undertaking or order. However, the change of circumstances must be such that the undertaking or order is no longer appropriate in dealing with the competition problem and/or adverse effects which it was designed to remedy, if it is to lead to either variation or termination.³
- 2.3 The process the CMA follows when conducting reviews of undertakings and orders is set out in CMA11, *Remedies: Guidance on the CMA's approach to the variation and termination of merger, monopoly and market undertakings and orders*.

² In addition, Schedule 24 of the Enterprise Act 2002 requires the CMA to keep under review undertakings originally agreed under the Fair Trading Act 1973.

³ CMA11, paragraph 2.5.

3. Provisional Decision

Background

The market investigation and the Order

- 3.1 The CMA's market investigation into the energy market found, among other things, an adverse effect on competition (AEC) resulting from the absence of locational pricing in the wholesale electricity market. The CMA found that the problem was likely to distort competition between generators, with likely short- and long-run effects on electricity generation and demand.
- 3.2 To address its concerns, the CMA made the Order, which imposes a set of obligations on the Transmission Company (defined below) about Transmission Losses⁴. The definition of Transmission Company is therefore key to the Order.
- 3.3 Article 2 of the Order defines 'Transmission Company' as National Grid Electricity Transmission plc (NGET), or any successor body, as the holder of a transmission licence in relation to which the Gas and Electricity Markets Authority (GEMA) or the Secretary of State has issued a 'Section C Direction' (as defined in the transmission licence) and where Section C of the transmission licence remains in effect.
- 3.4 Article 2 of the Order defines 'Transmission Licence' as a licence granted or treated as granted under section 6(1)(b) of the Electricity Act 1989.
- 3.5 In 2019, the system operator functions of NGET, including those relating to Transmission Losses, passed to National Grid ESO (NG ESO). However, the licence under which NG ESO carries out the functions previously carried out by NGET is a licence of the same kind as NGET's licence.

Reasons for undertaking a review

- 3.6 In March 2024, DESNZ notified the CMA that the coming into force of Part 5 of EA23 and the establishment of a new ESO would have an impact on certain definitions in the Order. The CMA decided to undertake a formal review of the Order to determine whether this represents a relevant change of

⁴ The units of electricity unaccounted for on the Transmission System as allocated in accordance with the BSC and the Order.

circumstances which would result in the Order being no longer appropriate as currently drafted.

Change of circumstances

- 3.7 Part 5 of the EA23 will introduce an ESO licence. The ESO licence will be held by a single entity (the Independent System Operator and Planner (ISOP)) which will carry out the transmission system operator functions relevant to the Order.
- 3.8 Under Part 5 of EA23, NG ESO (ie the company currently subject to the Order) will (a) be extracted from the National Grid group; (b) be given a new corporate identity as the National Energy System Operator (NESO); and (c) become the holder of an ESO licence and be designated as the ISOP by the Secretary of State under section 162 of EA23.
- 3.9 Although most of Part 5 of EA23 is already in force, some provisions, notably section 166(2) of EA23 will only come into force when NESO is designated as ISOP and granted the ESO licence. Similarly, although some of the consequential amendments to existing legislation reflecting these changes set out in the Energy Act 2023 (Consequential Amendments) Regulations 2024 (S.I. 2024/706) are already in force, others will only come into force immediately after the coming into force of section 166(2).
- 3.10 In relation to the Order, the current definitions of ‘Transmission Licence’ and ‘Transmission Company’ are no longer appropriate because they do not include an ESO licence or the holder of an ESO licence, and so do not cover the situation where a successor body to what were originally NGET's functions in relation to Transmission Losses holds an ESO licence, as will be the case for the ISOP/NESO. Therefore, unless the Order is varied, it would not apply to ISOP/NESO. Moreover, the specific provisions in the Order regarding obligations under the Transmission Licence (as defined in the Order) will no longer be appropriate because the ESO licence, which will contain such obligations, will not be a Transmission Licence as defined under the Order.

Proposed changes to the Order

- 3.11 In order for the Order to become consistent with the changes introduced by Part 5 of EA23, the CMA's provisional view is that it would be appropriate to make the following variations to the Order:
- (a) The defined terms relating to the Transmission Company should be broadened to include the ISOP / NESO within the scope of those terms.

- (b) The Order should be varied to reflect the fact that the functions and obligations of the Transmission Company will be governed by an ESO licence rather than a Transmission Licence.

3.12 The Annex sets out the proposed changes, which would be executed by means of a variation order.

Provisional conclusions on change of circumstances and appropriate outcome

3.13 The CMA provisionally concludes that:

- (a) The coming into force of Part 5 of EA23 and the Secretary of State's proposal to establish the ESO amount to a relevant change in circumstances.
- (b) As a result, the provisions of the Order described in paragraph 3.11 and 3.12 above are no longer appropriate as currently drafted as they will no longer apply to NESO once it holds an ESO licence.
- (c) The most appropriate outcome is to vary these provisions by means of a variation order.

3.14 The proposed changes to the Order are set out in the Annex.

4. Consultation

Notice of Intention to Vary

- 4.1 As envisaged in paragraph 3.29 of [CMA11](#), and required under Schedule 10 of the Act, the CMA hereby gives notice of its intention to vary the Order to update the Relevant Parts of the Order and make minor amendments to the remainder of the Order to ensure the Order remains coherent.

Stakeholder's views sought

- 4.2 The CMA is now seeking views from interested parties on its Provisional Decision, Notice of Intention to Vary, and the content of the proposed changes to the Order which are set out in the Annexe.
- 4.3 Respondents should provide their views, supported with relevant evidence where possible, in writing to the CMA at:
- Email: remedies.reviews@cma.gov.uk (Subject line: 'Energy (ETL) Order')
- 4.4 The CMA intends to publish all submissions received. Please ensure any submission provided to the CMA that contains any confidential material is accompanied by a non-confidential version which the CMA will publish on its website at the time that its Final Decision is published.
- 4.5 Responses should be submitted to the CMA by **5pm on Friday 23 August 2024**.

Annexe: Proposed changes to the Order and to the Explanatory Note

Part 1, Article 2.1 (Definitions)

1. **Addition** of: “**ESO Licence** means an electricity system operator licence within the meaning of section 6(1)(da) of the Electricity Act 1989.”
2. **Addition** of: “**Relevant Direction** means a direction given by the Secretary of State under section 167 of the Energy Act 2023.”⁵
3. **Amendment** to the definition of Transmission Company:

“means ~~National Grid Electricity Transmission plc, or any successor body, as the holder of a transmission licence in relation to which licence GEMA or the Secretary of State, where appropriate, has issued a Section C (system operator standard conditions) Direction (as defined in the Transmission Licence) and where Section C of the Transmission Licence remains in effect (whether or not subject to any terms included in a Section C (system operator standard conditions) Direction or to any subsequent variation of its terms to which the licensee may be a~~ the holder of a Transmission Licence which is a system operator as defined in the standard conditions published under section 88 of the Utilities Act 2000 and incorporated into Transmission Licences under section 8A of the Electricity Act 1989; or b) if the Secretary of State gives a Relevant Direction, from the time when the Relevant Direction takes effect, the holder or an ESO licence.”

Part 4

4. **Addition** of: “**6A. Effect of Relevant Direction ...** 6A.1 If the Secretary of State gives a Relevant Direction, from the date on which it takes effect, Article 6 is complied with if the ESO Licence contains provisions that, having regard to the effect of the Relevant Direction, are of equivalent effect to those set out in Schedule 3.”

⁵ The Relevant Direction is the instrument that would effectively convert NG ESO's transmission licence into an ESO Licence, with some new terms and some terms inherited from the transmission licence (including the provisions that were inserted into it by the Order), whilst ensuring continuity of rights and obligations.

The Explanatory Note to the Order

5. **Amendment** to paragraph 16: “Article 1 provides that the Order applies to ~~National Grid Electricity Transmission plc the Transmission Company~~, as system operator...”
6. **Amendment** to paragraph 17: “Article 2 includes definitions of various terms used in the Order. To the extent possible, the terms used in the Order have been defined to have the same meaning as in the Transmission Licence **or ESO Licence as applicable** and in the BSC...”
7. **Addition** to paragraph 32: “**Article 6A.1 provides for the application of ESO Licence provisions of equivalent effect to those set out in Schedule 3 to the Order in the event that the Secretary of State gives a Relevant Direction**”.