COMMISSION OPINION

of 10.11.2020

pursuant to Article 51(1) of Regulation (EU) 2019/943 and Articles 52(6) and 53(6) of Directive (EU) 2019/944 – United Kingdom – Certification of Diamond Transmission Partners Hornsea One Limited as transmission system operator for electricity

(ONLY THE ENGLISH VERSION IS AUTHENTIC)
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I. PROCEDURE

On 11 September 2020, the Commission received an initial notification from the regulatory authority in the United Kingdom (UK) responsible for Great Britain (GB), the Office of Gas and Electricity Markets (hereafter “Ofgem”), of a preliminary decision concerning the certification of Diamond Transmission Partners Hornsea One Limited (hereafter “Hornsea One OFTO”) as transmission system operator for electricity (hereafter “TSO”).

The UK withdrew from the European Union as of 1 February 2020. During the transition period, which ends on 31 December 2020, Union law, with a few limited exceptions, continues to be applicable to and in the UK and any reference to Member States in Union law shall be understood as including the UK.

Pursuant to Article 51 of Regulation (EU) 2019/943\(^1\) (hereafter "Electricity Regulation") and Articles 52 and 53 of Directive (EU) 2019/944\(^2\) (hereafter "Electricity Directive"), the Commission is required to examine the notified draft decision and to deliver an opinion within two months to the relevant national regulatory authority as to its compatibility with Articles 43, 52(2) and 53(7) of the Electricity Directive.

II. DESCRIPTION OF THE NOTIFIED DRAFT DECISION

Hornsea One OFTO is a special purpose vehicle established to own and operate the offshore transmission system which will connect the Hornsea One Offshore Wind Farm (with an installed capacity of 1218 MW, located in the North Sea off the coast of Yorkshire, England) with National Grid Electricity Transmission’s (hereafter “NGET”) onshore network at the connection point at North Killingholme in North Lincolnshire (England). The Hornsea One Offshore Wind Farm is not owned or operated by Hornsea One OFTO. It is the first of a series of offshore wind farms developed by Ørsted: Hornsea Two (with a planned capacity of 1386 MW) is under construction, Hornsea Three (with a planned capacity of 2400 MW) is in planning and Hornsea Four (with a planned capacity of 1200 MW) is in the pre-planning stage\(^3\).

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\(^3\) [https://www.thecrownestate.co.uk/en-gb/what-we-do/on-the-seabed/energy/#osw](https://www.thecrownestate.co.uk/en-gb/what-we-do/on-the-seabed/energy/#osw)
Hornsea One OFTO would be a licensed offshore transmission system owner (hereafter “OFTO”) under the specific national regime for such projects (hereafter “OFTO regime”).

Ofgem has analysed whether Hornsea One OFTO complies with the requirements of the ownership unbundling model, as laid down in the UK legislation transposing the Electricity Directive⁴.

As special purpose vehicle, Hornsea One OFTO itself does not own or otherwise exercise control over an undertaking performing any of the functions of generation or supply. Its appointed (or to be appointed) four Directors do not hold such or equivalent positions in an undertaking performing any of the functions of generation or supply.

The situation is different as regards the entities identified by Ofgem as Hornsea One OFTO’s ultimate controllers: Mitsubishi Corporation (hereafter “MC”) and Chubu Electric Power Co., Inc. (hereafter “Chubu”).

Hornsea One OFTO is a 100% subsidiary of Diamond Transmission Partners Hornsea One (Holdings) Limited (hereafter “HoldCo”).

51% of the shares of HoldCo are held by Diamond Transmission Corporation Limited (hereafter “DTC”) which is a 100% subsidiary of MC. The purpose of DTC is to act as holding company for offshore transmission investments of MC in Europe, including the four Blue Transmission OFTOs (Walney 1 and 2, Sheringham Shoal and London Array) which were the subject of Commission opinion C(2016)27 final, Diamond Transmission Partners BBE Limited (see Commission opinion C(2018) 2266 final of 12 April 2018), RB OFTO (see Commission opinion C(2019) 699 final of 24 January 2019), Galloper OFTO (see Commission opinion C(2019) 699 final of 24 January 2019), Galloper OFTO (see

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⁴ Directive 2009/72/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in electricity and repealing Directive 2003/54/EC has in the meantime been replaced by Directive (EU) 2019/944, which needs to be transposed by Member States until 31 December 2020. However, the provisions relevant for this case have not been changed.
Commission opinion C(2019) 5994 final of 7 August 2019) and Walney Extension OFTO (see Commission opinion C(2019) 8845 final of 5 December 2019). Following the financial close of Hornsea One OFTO, DTC will transfer its shares in HoldCo to Diamond Transmission UK Limited, a 100% subsidiary of DTC.

49% of HoldCo’s shares are indirectly held by Chubu through its 100% subsidiary Chubu Electric Power Company Netherlands B.V. (hereafter “CEPCON”).

According to the draft certification decision by Ofgem, MC and Chubu hold the following participations in the EEA which qualify as “relevant producers or suppliers” under UK legislation:

**Participations of Chubu**

- The Gunfleet Sands and Gunfleet Sands II offshore wind farms: Chubu has an interest in this 173 MW wind farm of the coast of South East England through its interest in CEPCO and its subsidiaries.

- Zenobe Energy Storage: Chubu has an indirect, controlling interest in nine battery storage sites in GB with a total capacity of 73 MW.

**Participations of MC in offshore wind farms in BENELUX countries**

- The Norther Offshore Wind Farm Project: MC has 25% interest in this 379 MW wind farm, located off the cost of Belgium. MC may exercise indirect control over this wind farm as a result of voting and veto rights.

- SeaMade Offshore Wind Farm Project: MC will have an indirect share in this offshore wind farm with a capacity of 487 MW located off the coast of Belgium. The wind farm is expected to be operational in the fourth quarter of 2020. Ofgem considers this project as relevant for its assessment.

- The Luchterduinen Offshore Wind Farm Project: MC has a 50% share in this 129 MW wind farm, located off the coast of the Netherlands.

- The Prinses Amalia Offshore Wind Farm Project: MC has a 80% share in this 120 MW wind farm, located off the coast of the Netherlands.

- The Delfzijl-Noord Wind Farm Project: MC has a share in this 62.7 MW wind farm, located off the coast of the Netherlands.

- Borssele 3 and Borssele 4 Offshore Wind Farm Projects: MC will have a 23% indirect share in these wind farms with a capacity of 350 MW each, located off the

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5 JERA is a 50:50 joint venture of CEPCO with TEPCO Fuel & Power, which has a 50% interest in a company which via several 100% subsidiaries has a 49.9% interest in the holding company owning both offshore wind farms.

6 A 100% subsidiary of JERA has a 95% interest in a company which has a 10.19% interest in Zenobe Energy Limited.

The wind farm is expected to be operational in the first quarter of 2021. Ofgem considers this project as relevant for its assessment.

**Participations of MC in other electricity generation (including storage) projects**

- **BESS Project**: MC has a 50% equity interest in a 48 MW battery energy storage system project in Germany. The BESS Project connects to the TenneT transmission system in Germany.
- **The Enecogen CCGT Project**: MC has a 40% indirect share in this 870 MW CCGT plant in the Netherlands.
- **The CHP MK12 Project**: MC has a [redacted] share in this 227 MW [redacted] plant in the Netherlands.
- **The CHP LW06 combined heat and power project**: MC has a 80% share in this 247 MW [redacted] plant in the Netherlands.

**Participations of MC in energy suppliers**

- **OVO Energy**: MC has a 20% minority interest in OVO Energy, based in GB. With the recent acquisition of the retail section of SSE, OVO Energy now has [redacted] customers in GB

- **Eneco Energy Supply Netherlands**: a group of energy suppliers operating under the Eneco brand with circa 3.6 million electricity and gas customers in the Netherlands.
- **Eneco Energy Supply Belgium**: an energy supplier with circa one million electricity and gas customers in Belgium.
- **Eneco Energy Trade B.V.**: an energy trading company holding an electricity supply licence in GB.
- **LichtBlick**: an energy supplier with circa 600,000 electricity and gas customers in Germany.
- **ElectroRoute Holdings Limited**: MC holds a 57.7% share in this Irish energy trading company that trades in electricity markets located in the EEA, including GB markets.

Ofgem furthermore mentions interests of MC in “other generation” installations which are not “relevant producers or suppliers” in the meaning of UK unbundling legislation, since they are exempt from the requirement to hold a license. This concerns the Moy (60 MW) and Lochluichart (69 MW) wind farms located in Scotland.

Additionally, Ofgem’s assessment of the application for certification lists multiple interests in “small-scale” producers or suppliers, mainly renewable energy projects, in the EEA, amounting to a total of 4375 MW installed generation capacity.

Ofgem states that it has considered these interests in “small-scale” producers or suppliers as well as the interest in “other generation” for the purpose of assessing whether there is any risk of discrimination.

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10. [https://www.ovoenergy.com/about](https://www.ovoenergy.com/about)
Ofgem also notes that MC intends to purchase an indirect interest in the Moray East Offshore Wind Farm Project to be located off the coast of Scotland and expected to be operational by April 2022. Ofgem explains that this project is not covered by the assessment on which the draft decision is based, since it will not be operational at the time Hornsea One OFTO is expected to be certified and the transactions details are not yet sufficiently certain.

Ofgem notes that MC and Chubu also hold interests in a number of “relevant producers or suppliers” that are located outside the EEA: in North and South America, in Asia and in the Middle East.

In its preliminary decision, Ofgem concludes that, despite the considerable, above listed interests of its controllers, Hornsea One OFTO complies with the requirements of the ownership unbundling model, as laid down in the UK legislation transposing the Electricity Directive. Ofgem considers that there is no realistic prospect or incentive for Hornsea One OFTO to discriminate in favour of the generation or supply interests of its controllers, or vice versa for several reasons:

1. Ofgem considers that Hornsea One OFTO’s controllers currently do not have sufficient market power to discriminate in favour of generation, transmission or supply interests: Ofgem estimates that their aggregate share of the GB generation market is under 0.3%, and under 0.1% of the total EU market. Furthermore, Ofgem considers that only flexible generation can be used to exert market power. The majority of generation controlled by Hornsea One OFTO’s controllers is wind generation, which Ofgem considers to be inflexible.

2. Ofgem considers that Hornsea One OFTO or other OFTOs controlled by MC or Chubu would not have the ability to distort the generation market by reducing transmission capacity or that this ability is merely theoretic since the risk of doing so would far outweigh the potential benefits. MC and Chubu share control of one other transmission system: Diamond Transmission Partners Walney Extension Limited with a connected generation capacity of 659 MW. Including Hornsea One OFTO, MC will control, with partners, 9 OFTOs with a total connected generation capacity of around 4.5 GW, below demand margins of between 7.5 and 9 GW.

Furthermore, managing electricity flows over the onshore and offshore network is the role and obligation of National Grid Electricity System Operator, which is certified as ownership unbundled (see Commission opinion C(2018) 6306 final of 25 September 2018) and is the National Electricity System Operator (hereafter “NETSO”). Therefore Hornsea One OFTO’s controllers would not be able to create a shortage in the GB transmission system and, if they would be able, since NETSO manages flows in the system it would be impossible for them to know whether it would be their generation interests that would be despatched.

Ofgem also refers to the rules of the OFTO regime and the OFTO license for Hornsea One OFTO, to incentives for wind farm operators for monitoring the reasons for reduction in transmission services and to national and EU rules on energy market integrity and transparency. Due to the rules in place for OFTOs and the obligations of the OFTO licence, Ofgem considers the risk (including penalties) of any discriminatory behaviour to far outweigh the potential benefits. In this context, Ofgem stresses that each controller of Hornsea One OFTO has no interest to let the other controller to incur such risks for decisions which would only be to the benefit of one of the controllers.

3. Ofgem sees no possibility for a physical connection between the transmission system owned by Hornsea One OFTO and the “relevant producers or suppliers” controlled by MC or
Chubu: the TSO is a radial link only between the Hornsea One wind farm and the onshore connection point. Existing interconnectors between GB and the Netherlands or Belgium are not routed through the Luchterduinen or the Norther offshore wind farms. Ofgem also considers the “relevant producers or suppliers” controlled by MC or Chubu of not being in physical proximity to Hornsea One OFTO’s transmission system. Ofgem acknowledges the potential development of a North Sea offshore grid, but does not expect relevant changes happening in the foreseeable future that would increase the risk that MC influences Hornsea One OFTO’s decision making to the benefit of MC’s electricity generation projects in North Sea coastal countries. Therefore, Ofgem’s assessment excludes the potential development of a North Sea offshore grid, while keeping such developments under review.

Finally, given that MC and Chubu are registered in Japan, hence in a third country, Ofgem is also required to ascertain that granting the certification would not put at risk the security of energy supply of the UK and the Union, in accordance with the requirements set out in Article 53 of the Electricity Directive. Ofgem asked the UK Department for Business, Energy & Industrial Strategy (hereafter “BEIS”) for its opinion. BEIS concluded in its letter to Ofgem of 4 June 2020 that this is not the case due to the limited scope of Hornsea One OFTO as a TSO licensed to transmit electricity generated from a designated offshore area and its capacity compared to the UK’s peak demand. The offshore wind farm is connected with the national transmission system on a point-to-point basis only and Hornsea One OFTO is thus not part of a meshed network. Generally, from the perspective of BEIS’ wider work on potential risks of foreign investment in the UK energy system, companies from Japan do not, in and of itself, trigger particular concerns.

On this basis, Ofgem submitted its draft decision to the Commission requesting an opinion.

III. COMMENTS

On the basis of the present notification the Commission has the following comments on the draft decision.

1. Generation and supply interests linked to Hornsea One OFTO’s controllers

Background to the Commission assessment

Article 43(1)(b)(i) of the Electricity Directive prohibits the same person(s) from directly or indirectly exercising control over an undertaking performing any of the functions of generation or supply, and directly or indirectly exercising control or exercising any right over a TSO or over a transmission system. Article 43(1)(b)(ii) of the Electricity Directive prohibits the same person(s) from directly or indirectly exercising control over a TSO or over a transmission system, and directly or indirectly exercising control or exercising any right over an undertaking performing any of the functions of generation or supply. The objective which the unbundling rules of the Electricity and Gas Directives pursue is the removal of any conflict of interest between, on the one hand, generators/producers and suppliers and, on the other hand, TSOs.

The Commission considers that the means with which the legislator intended to pursue the objective of removing any conflict of interest between, on the one hand, generators/producers

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and suppliers and, on the other hand, TSOs is to provide for a structural solution to the problem that owners of electricity or gas infrastructure may use their control over this infrastructure (constituting a natural monopoly or an “essential facility”) to favour their own generation or supply business. The unbundling regime pursuant to EU legislation is meant to prevent such practices and replaces the previous regime of relying exclusively on behavioural measures (reporting, ex post control including fines) by a structural separation between generation/supply and transport infrastructure which excludes the possibility to use the infrastructure to influence competition.

Nevertheless, the objective and purpose of the EU unbundling rules should be kept in mind in the certification of TSOs. As explained in the Staff Working Paper ‘Ownership Unbundling: The Commission’s practice in assessing a conflict of interest including in the case of financial investors’ (SWP (2013) 177), a certification of a TSO should not be refused in cases where it can be clearly demonstrated that there is no incentive and ability for a shareholder in a TSO to influence the TSO's decision making in order to favour its generation, production and/or supply interests to the detriment of other network users and therefore prohibiting person(s) from investing in a TSO would be disproportionate. The Staff Working Paper assumed that such cases would mainly relate to globally active holding companies owning, *inter alia*, a TSO or to financial investors whose investment strategy typically involves investments in both renewable energy generation assets and grid transmission infrastructure with a view to benefiting from regulated income.

One example mentioned in the Staff Working Paper is a case were the holding company of an electricity TSOs also controls generation interests on another continent. Other examples concern electricity TSOs which also own smaller generation assets in other countries, e.g. a waste incinerator or a combined heat and power plant mainly providing heat to a district heating system which also produce electricity and which operate in a regulated system.

*Assessment of a possible conflict of interest*

The Commission agrees with Ofgem that the generation and supply interests controlled by Hornsea One OFTO’s ultimate controllers which are located on other continents do not pose a risk as regards a possible conflict of interests: Due to the geographical distance there exists neither a direct link nor is it likely that at any time in the future such a physical connection of the markets in question will be established. Therefore, it is obvious that there is no incentive and ability for a shareholder in a TSO located in the UK to influence the TSO's decision making in order to favour such generation or supply interests to the detriment of other network users.

However, Hornsea One OFTO’s ultimate controllers also hold substantial participations in generation and supply interests located in the UK or neighbouring countries. Whereas the Staff Working Paper refers to cases where the amount of energy produced by shareholders of a TSO was considered insignificant, the same cannot be said in the present case where the shareholders hold generation assets in the EEA with an installed capacity of in total around [redacted] in the case of MC and [redacted] in the case of Chubu. As regards MC, this is a considerable increase compared to the situation in 2019 reflected in the Commission Opinion of 5 December 2019 on the certification of Walney Extension Limited\(^{12}\), when MC’s generation assets amounted to [redacted] in total.

Furthermore, MC considerably increased its interests in electricity suppliers: OVO Energy is now the second largest electricity supplier in GB with around 3.5 million customers and hence

\(^{12}\) C(2019) 8845 final
a market share of more than 15%, compared to less than 5% in 2019. With Eneco Energy Supply Netherlands and Belgium, MC has interests in energy suppliers with an aggregate total of approximately 4.6 million customers in adjacent and interconnected supply markets and, with Lichtblick, an interest in an energy supplier with around 0.6 million customers in Germany.

In relation to the generation and supply interests of Hornsea One OFTO’s shareholders located in the GB, Ofgem relies on behavioural safeguards enshrined in the regulatory regime for the required demonstration that there clearly is no incentive and ability for a shareholder to influence the TSO’s decision making in order to favour these generation or supply interests.

Notably, Ofgem argues that a conflict of interest can still be excluded due to the limited responsibility of OFTOs, the behavioural safeguards in place (e.g. fines for interruptions) and due to the allegedly insignificant market share of a) their generation interests and b) the generation capacity linked by OFTOs controlled by the parties, by comparison to the aggregate GB market/capacity.

As regards the ability and incentive to abuse control over Hornsea One OFTO, the Commission acknowledges that the OFTO Regime as well as the rules according to which NETSO manages the electricity system provides for a range of behavioural safeguards. However, there are limits to the extent such regulatory safeguards can be considered as suitable replacements for the above mentioned structural separation imposed by the Union legislator. In the present case, the Commission is of the opinion that, at least as far as MC is concerned, the required unambiguous absence of an incentive and ability for a shareholder in a TSO to influence the TSO’s decision-making in order to favour its generation and/or supply interests to the detriment of other network users has not been sufficiently established in the preliminary decision. In view of the considerable generation and supply interests held by Hornsea One OFTO’s controllers, the present case can therefore not be considered as supported by the doctrine on financial investors developed in the Commission’s Staff Working Paper.

MC is among the shareholders also for other OFTOs previously certified by Ofgem. In its opinion on the draft certification of Galloper OFTO, the Commission had already expressed certain reservations as to the compatibility of the envisaged certification with the requirements of the Electricity Directive. In its opinion on the draft certification of Walney Extension OFTO, the Commission had expressed its severe concerns and had invited Ofgem to reconsider its assessment. The added generation and supply interests acquired by MC as described above further corroborate the Commission’s concerns.

Thus, in the view of the Commission, the certification of Hornsea One OFTO as an ownership unbundled TSO cannot be considered compatible with the unbundling provisions of the Electricity Directive requiring a structural separation of generation and supply interests on the one hand and transmission assets on the other hand, at least as long as MC has “any rights” in Hornsea One OFTO going beyond a purely passive minority participation.

Based on the above, the Commission invites Ofgem to reconsider its assessment that, despite the considerable generation and supply interests of its controllers, Hornsea One OFTO meets the requirements for certification as ownership unbundled TSO.

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14 Commission opinion C(2019) 5994 final of 7 August 2019
15 Commission opinion C(2020) 8845 final of 5 December 2019
2. Application of Article 53 – Certification in relation to third countries

Pursuant to Article 53 of the Electricity Directive, Ofgem is to refuse certification unless it is demonstrated, on the basis of an assessment, that granting certification does not put at risk the security of supply of the UK or the EU. In the present case, the application of Article 53 is triggered due to the fact that MC and Chubu are registered in Japan.

Commission assessment

Japan is an OECD member and – as also most EU Member States – a member of the International Energy Agency (IEA), an organisation which has among its main tasks to increase the security of the energy supply of its members. Both the EU and Japan are cooperating on energy issues in the G7 context and are partners through the multilateral ITER Project. An Economic Partnership Agreement between the EU and Japan was finalised in 2017 and entered into force on 1 February 2019\(^16\). Furthermore, at the EU and Japan Summit on 6 July 2017 a political agreement was achieved on the main elements of a Strategic Partnership Agreement to increase cooperation including on energy\(^17\) and negotiations on this agreement were concluded on 25 April 2018\(^18\). On 11 July 2017 a ‘Memorandum of Cooperation between the EU and Japan on promoting and establishing a liquid, flexible and transparent global Liquefied Natural Gas (LNG) market’ was signed, further showing how closely the EU and Japan are cooperating in addressing issues of security of supply. The EU and Japan continue to closely cooperate also against the background of the COVID-19 pandemic\(^19\).

In view of the above, and given the limited amount of generation capacity connected via the Hornsea One OFTO system in terms of the UK’s security of supply, the Commission shares the view of BEIS that the granting of certification to Hornsea One OFTO would not put at risk the security of supply of the UK or the EU.

3. Ongoing monitoring

The Commission recalls the obligation set out in Article 52(4) of the Electricity Directive for national regulatory authorities to monitor the continued compliance of TSOs with the unbundling requirements of Article 43 of the Electricity Directive.

Should Ofgem decide to certify Hornsea One OFTO, the Commission invites Ofgem to continue monitoring the case also after the adoption of the final certification decision in order to satisfy itself that no new facts emerge which would justify a change of its assessment.

IV. CONCLUSION

Pursuant to Article 51 of the Electricity Regulation, Ofgem shall take utmost account of the above comments of the Commission when taking its final decision regarding the certification of Hornsea One OFTO, and when it does so, shall communicate its decision to the Commission.

The Commission's position on this particular notification is without prejudice to any position it may take vis-à-vis Member State regulatory authorities on any other notified draft measures concerning certification, or vis-à-vis Member State authorities responsible for the

transposition of EU legislation, on the compatibility of any national implementing measure with EU law.

The Commission will publish this document on its website. The Commission does not consider the information contained therein to be confidential. Ofgem is invited to inform the Commission within five working days following receipt whether and why they consider that, in accordance with EU and national rules on business confidentiality, this document contains confidential information which they wish to have deleted prior to such publication.

Done at Brussels, 10.11.2020

For the Commission
Kadri SIMSON
Member of the Commission