# Request for Exemption: AQUIND Interconnector

PRIVATE AND CONFIDENTIAL

# 5 Exemption request and rationale

## 5.1 Introduction

This section of the exemption application includes:

- A description of the grounds for exemption.
- A summary of AQUIND's exemption request.

## 5.2 The grounds for exemption

The decision to award an exemption is based on the specific nature of the project.  An exemption may only be granted where the project meets the conditions set out in Article 63 of Regulation 2019/943:

> *(a) the investment enhances competition in electricity supply;*
>
> *(b) the level of risk attached to the investment is such that the investment would not take place unless the exemption is granted;*
>
> *(c) the interconnector is owned by a natural or legal person which is separate, at least in terms of its legal form, from the system operators in whose systems that interconnector will be built;*
>
> *(d) charges are levied on users of that interconnector;*
>
> *(e) since the partial market opening referred to in Article 19 of Directive 96/92/EC of the European Parliament and of the Council*[1]*, no part of the capital or operating costs of the interconnector has been recovered from any component of charges made for the use of transmission or distribution systems linked by the interconnector; and*
>
> *(f) an exemption would not be to the detriment of competition or the effective functioning of the internal market for electricity, or the efficient functioning of the regulated systems to which the interconnector is linked.*

Article 63 states in relation to a request for an exemption for a new direct-current interconnector that:

- such exemption is "for a limited period of time" – 63(1)
- the decision "shall be taken on a case-by-case basis by the regulatory authority" – 63(4)
- the "exemption may cover all or part of the new interconnector" – 63(4).

This section of the Request for Exemption explains the unique nature of AQUIND Interconnector, the risks faced by the project developers, and the rationale for the exemption.

## 5.3 AQUIND's exemption request

Pursuant to Article 63 of Regulation 2019/943, AQUIND seeks a partial exemption for AQUIND Interconnector in France from Articles 19(2) and 19(3) of Regulation 2019/943 (regarding the Use of Revenues) for a period of 25 years from the start of commercial operations.  The partial exemption

[1] Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity (OJ L 27, 30.1.1997, p. 20)

would apply to a fixed share of AQUIND's revenues that corresponds to the proportion of AQUIND Interconnector capital and operational costs related to French territory (onshore and French territorial waters).

In accordance with French national law, an exemption granted under Article 63 of Regulation 2019/943 would also have the effect of permitting AQUIND to operate AQUIND Interconnector in France. Despite the limited duration of the exemption requested, AQUIND will seek to maintain this permission to operate AQUIND Interconnector in France for its full operational life.

AQUIND does not seek an exemption for Unbundling (Article 43, Directive 2019/944), Third Party Access (Article 6, Directive 2019/944) or the approval of charging and access rules (Article 59(7) and 60(1) of Directive 2019/944). While AQUIND's existing structure and investors do not require an exemption from unbundling requirements, AQUIND does not rule out the possibility of reconsidering unbundling requirements if necessitated by the business's arrangements of potential future investors.

### 5.3.1 Articles 19(2) and 19(3) of Regulation 2019/943: Use of Revenues

AQUIND is applying for a partial exemption from Articles 19(2) and 19(3) of Regulation 2019/943. The exemption will apply to a fixed share of the revenues[2] generated by AQUIND Interconnector that corresponds to the proportion of the project that will be situated in French territory (including onshore and in French territorial waters) (the "**Exempt Portion**"). This share is estimated to be 32%, based on AQUIND's cost analysis presented in Section 6.4 below. The remaining share of the revenues generated by the project will not be exempt from the requirements of Articles 19(2) and 19(3).

The revenues covered by the scope of the Exemption will include the fixed share of the sum of the following components:

- Congestion revenues generated by AQUIND Interconnector
- Capacity Mechanism revenues, insofar as these revenues accrue to the interconnector owner
- Ancillary services revenues, insofar as these revenues accrue to the interconnector owner
- Netting-off component, which may include, for example, any costs that may apply to the project, such as trading tariffs, or penalties associated with non-performance of Capacity Mechanism and/or Ancillary services contracts that AQUIND Interconnector may, from time to time, enter into
- Such other revenues arising from AQUIND Interconnector performing its role as electricity interconnector within the period of duration of the requested exemption.

AQUIND's Request for Exemption on the Use of Revenues in France follows extensive regulatory engagement with CRE, as well as Ofgem and ACER to consider and test the viability of different investment and regulatory routes for AQUIND Interconnector. The conclusion of these regulatory tests, extensive analysis and formal regulatory decisions is that the only investment route available to AQUIND in France is through an exemption under Article 63. Without an exemption, the project cannot, and will not, progress and the significant benefits to France, GB and Europe, as demonstrated in the AQUIND revenue and social welfare analysis (Exhibit 1) will not be realised.[3]

[2] We envisage that the share of revenues subject to the Exemption will be fixed ex-ante for the duration of the Exemption (i.e. 25 years), based on the territorial principle.

[3] The project benefits include social welfare benefits, benefits to security of supply, competition benefits, environmental benefits, benefits in the provision of ancillary services and taxation benefits to French society.

We summarise here the project history and the regulatory decisions that led to this exemption request and provide the core rationale for AQUNID's Request for Exemption:

- **AQUIND's 2017 Request for Exemption**: On 15 May 2017, AQUIND applied to CRE and Ofgem (as the NRAs for GB and France) under Article 17 of Regulation 714/2009[4] (the "Electricity Regulation") for certain exemptions from the relevant regulations (the "2017 Exemption Request"). Following the provision of further information by AQUIND, the 2017 Exemption Request was accepted as complete by Ofgem on 4 September 2017. Pursuant to Article 17(5) of the Electricity Regulation, on 19 December 2017, AQUIND's exemption application was then referred by Ofgem and CRE to ACER for a decision.
- **ACER's decision not to grant AQUIND's Request for Exemption**: By decision on 19 June 2018, ACER refused to grant the 2017 Exemption Request on the basis that the condition set out in Article 17(1)(b) of the Electricity Regulation was not met, finding that AQUIND had not sufficiently demonstrated that the level of risk attached to the investment was such that the investment would not take place unless an exemption was granted. This decision by ACER was primarily based on the fact that, in ACER's view, AQUIND should have tested whether a regulated regime was available to the Project. This in turn was based on AQUIND Interconnector's PCI status (granted during the course of ACER's review of the 2017 Exemption Request), which could allow the development of the project under a regulated regime pursuant to the Cross-Border Cost Allocation (CBCA) arrangements of Article 12 of Regulation 347/2013 (the "TEN-E Regulation").[5]
- [redacted]
- **AQUIND's PCI status**: On 31 October 2019 the European Commission (the "Commission") adopted a delegated regulation (the "Delegated Regulation") that amends the union list of projects of common interest ("PCIs") inter alia by removing AQUIND Interconnector from the list and accordingly AQUIND Interconnector is set to lose PCI status when the Delegated Regulation comes into force. [redacted]

The conclusions of the steps and decisions summarised above is that the only investment route that will permit AQUIND to continue to develop to project is through an exemption in France. There is no other regulated regime for non-RTE interconnection in France.[6] [redacted]

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[4] Article 63 of Regulation 2019/943 essentially restates the conditions for an exemption set out in Article 17 of Regulation 714/2009.

[5] AQUIND Limited appealed to the Board of Appeal of ACER against ACER's decision to reject the Exemption Request, but this appeal was rejected on 17 October 2018. An appeal to the General Court of the European Union against the decision of the Board of Appeal was submitted in January 2019, which is ongoing as of the date of this Request for Exemption.

[6] In GB, the regulatory arrangements set out under the Cap and Floor regime allow for third party interconnector developers and as such AQUIND does not require any exemptions in GB.

[redacted] The steps taken by AQUIND demonstrate fully that the project risk is such that the investment will not take place unless an exemption is granted.

AQUIND therefore seeks a partial exemption sufficient to allow the project to progress in France. The scope of the exemption is proportionate and limited such that the exemption is only sought for elements of the legislation that would otherwise prevent the project's development in France, i.e. the use of revenues. The interconnector will operate in the same way as any other regulated interconnector, with capacity products made available to third parties in regulated timeframes.

AQUIND recognises that there is a degree of revenue uncertainty for a GB-France interconnector, as is the case for any infrastructure project of this scale, which could also result in additional returns for the project. Should the AQUIND Interconnector be more profitable than expected, AQUIND proposes to introduce additional conditions on the portion of the revenues generated by the interconnector in France to re-distribute some of the profits to French network users in scenarios where revenues exceed expectations. Specifically, we propose a "profit-sharing mechanism" as follows: if the present value of profits related to the Exempt Portion of the Project, discounted at a nominal rate of [redacted]%, is positive, then [redacted]% of these profits would be transferred from AQUIND to RTE (and hence to French network users).

In calculating the profits related to the Exempt Portion of the Project, for the purposes of the "profit-sharing mechanism" described above, we propose that:

- The profits are calculated based on the actual costs and actual revenues associated with the Exempt Portion of the Project; and
- The revenues will be split and ring-fenced into two separate "pots", corresponding to the Exempt and Non-Exempt Portion of the Project. The ring-fencing arrangements put in place will be such that there is no interaction between the two "pots". For the avoidance of doubt, regulatory arrangements (if any) related to the treatment of AQUIND's revenues on the GB side will be entirely independent of the calculations performed for the purposes of the "profit-sharing mechanism" for the Exempt Portion of the Project described above.

We consider that this profit-sharing mechanism is appropriate, proportionate and in the interest of French socio-economic welfare because it aligns AQUIND's and French network users' incentives to maximise operational availability of the interconnector at times when the Project generates the highest value. In addition, the "profit-sharing mechanism" will deliver additional benefits of revenue upside to French network users, and critically it will do so without transferring additional risk to French network users. The specific details of the proposed "profit-sharing mechanism" would be fixed ex-ante by CRE, for the duration of the Exemption.

The exemption from Article 19 is sought for a period of 25 years.

### 5.3.2 Exemption required to operate AQUIND Interconnector in France

An exemption is required in order for AQUIND to be permitted to operate AQUIND Interconnector in France. Under French law, the TSO is responsible for the development, construction and operation of regulated interconnectors. RTE is currently the only eligible entity to undertake these operations. AQUIND is therefore prohibited from operating a regulated interconnector in France under Articles L. 121-4 and L. 321-6 of the French Energy Code[7].

[7] Adopted by Ordonnance 2011-504 of 9 May 2010.

Based on the above, CRE adopted a decision on 29 March 2012[8] which provides that the only possibility for a private party to operate an interconnector in France is within the framework of an exemption. As such, AQUIND requires an exemption under Regulation 2019/943 in order to construct and operate AQUIND Interconnector in France.

AQUIND will seek to maintain this permission to operate AQUIND Interconnector in France for its full operational life, beyond the 25 year period of this Request for Exemption.

## 5.4 Exempt Portion of AQUIND Interconnector

AQUIND has undertaken a detailed cost analysis, focusing on the development, capital and operating expenditure. On this basis, AQUIND estimates that the proportion of the Project that will be situated in French territory (including onshore and in French territorial waters), i.e. the Exempt Portion, is 32%.

A summary of this analysis is presented in Table 5-1 below.

**Table 5-1: Allocation of AQUIND Interconnector costs[9]**

| Cost category | Total | ...of which the Exempt Portion |
|---|---|---|
| Capex – Converters | [redacted] | [redacted] |
| Capex – Cables + Connections | [redacted] | [redacted] |
| Capex – (CAR, Project mgmt) | [redacted] | [redacted] |
| Devex | [redacted] | [redacted] |
| **Subtotal Capex + Devex** | [redacted] | [redacted] |
| **Opex (Present value)** | [redacted] | [redacted] |
| **Repex (Present value)** | [redacted] | [redacted] |
| **Total Capex + Devex + Opex + Repex** | €1,537m | €488m |
| **Cost split** | 100% | 32% |

*Source: AQUIND analysis.*

[8] CRE deliberation dated 29 March 2012 communicating on the application of Article 17 of the EC Regulation No. 714/2009 dated 13 July 2009

[9] Presented here in PV terms taking into account the profile of costs