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Consultation on proposed changes to the standard licence conditions of the electricity interconnector licence, the electricity interconnector licences held by Nemo Link and NGIL and the electricity transmission licence held by NGET to implement the cap and floor regime and use of revenues compliance: RWE Response

Dear Laura,

RWE welcomes the opportunity to respond to the Ofgem consultation on proposed changes to the standard licence conditions of the electricity interconnector licence, the electricity interconnector licences held by Nemo Link and NGIL and the electricity transmission licence held by NGET to implement the cap and floor regime and use of revenues compliance. We are responding on behalf of RWE companies operating in the UK.

RWE remains supportive of efforts to improve market liquidity, competition and security of supply. We expect interconnectors to play an important role in the integrated European electricity market by facilitating balancing of supply and demand. We also recognise that interconnectors form part of the transmission system in line with Directive 2009/72/EC and as such interconnectors must comply with all EU Regulations, guidelines and network codes.

In considering the cap and floor regime, it is important to assess the impact of interconnectors on the energy market and customer welfare. A recent report by Aurora Energy Research¹ highlighted three key drawbacks associated with increased interconnection that has received inadequate attention, namely that “*customer’s incur significant costs*”, “*total CO2 emissions increase*” and “*more interconnection does not deliver increased security of supply*”². Aurora concludes that “*excessive interconnection build out can in fact detract from affordability, decarbonisation and energy security*”³. We expect Ofgem to assess and evaluate these findings in relation to the current consultation.

¹ A copy of the report can be found at <http://auroraer.com/files/reports/Dash%20for%20interconnection%20-%20Aurora%20Energy%20Research%20-%20February%202016.pdf> (the Aurora Report)

² Aurora Report Page 2

³ Aurora Report, Page 2

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The cap and floor approach may have a role to play in ensuring provision of interconnector investment only if such an approach can be properly justified. However, GB customers should not underwrite inefficient interconnection by creating a regulatory regime that insulates interconnector investors from the downside risks of the investment.

As we stated in our response to previous Ofgem consultations on the cap and floor regime it is our view that collectively the GB carbon floor price, the GB capacity market and the EU target model are capable of creating the conditions for merchant investment in interconnection without the need for regulatory safeguards. The merchant approach should remain the default arrangements for interconnector investment with the merits of the cap and floor approach considered as a last resort and on a case by case basis. Therefore we do not see the need to modify the enduring electricity interconnector licence standard conditions to incorporate the cap and floor regime.

We recognise that the cap and floor regime requires that that any costs associated with the floor or the benefits associated with the cap are reflected in the cost pass-through arrangements that apply to NGET. However, we are concerned that the impact of the proposed licence changes on the TNUoS charging regime has not been considered in the consultation document. We note that Ofgem are proposing that the costs/benefits of the cap and floor regime form part of the allowed pass through items for the system operator under amendments to Special Condition 3B resulting in “a corresponding increase or decrease in TNUoS charges” (Consultation Document page 9). It is unclear as to the extent of the potential impact of these changes on generation and demand TNUoS tariffs and whether they result in transmission tariffs that are more or less cost reflective (as required under the Electricity Directive (2009/72)). We believe that further consideration is required in relation to impact the proposed arrangements on market participants and customer welfare.

Our responses to the specific questions are included in Annex 1 to this document.

If you have any comments or wish to discuss the contents of this letter then please do not hesitate to contact me.

Yours faithfully

By email

Bill Reed
Market Development Manager

Annex 1: RWE Response to the Consultation Questions

(1) the proposed insertion of new cap and floor standard conditions into the standard conditions of the electricity interconnector licence;

We do not support the proposed insertion of new cap and floor conditions into the standard conditions of the electricity interconnector licence. We believe that the cap and floor regime should not be established as the default enduring arrangements for interconnectors. The introduction of the relevant licence conditions for the cap and floor regime should be considered on a case by case basis.

(2) the proposed insertion of new special conditions into the electricity interconnector licences held by Nemo Link and NGIL;

We do not have any specific comments on the proposed new special conditions to be inserted into the electricity interconnector licences held by NEMO Link and NGIL. However, we note that it is important that the special conditions reflect the policy intent that underlies the cap and floor regime.

(3) the proposed amendments to NGET's electricity transmission licence;

We recognise that the cap and floor regime requires NGET as system operator to recover the funds required to make the relevant payments to interconnectors or to return surplus funds to customers. The proposed amendments to NGET's electricity transmission licence appear to be the minimum required to facilitate the establishment of the appropriate cash flows.

Further work is required to understand the potential impact of the proposed changes on the TNUoS charging regime. In particular we note that Directive 2009/72/EC⁴ states in the preamble that

"(36) National regulatory authorities should be able to fix or approve tariffs, or the methodologies underlying the calculation of the tariffs, on the basis of a proposal by the transmission system operator or distribution system operator(s), or on the basis of a proposal agreed between those operator(s) and the users of the network. In carrying out those tasks, national regulatory authorities should ensure that transmission and distribution tariffs are non-discriminatory and cost-reflective, and should take account of the long-term, marginal, avoided network costs from distributed generation and demand-side management measures".

The proposed pass-through arrangements which impact TNUoS tariffs and market signals, particularly in relation to demand side peak charges, require further detailed consideration.

(4) the draft Cap and Floor RIGs published alongside this letter; and

We do not have any specific comments on the draft Cap and Floor RIGs.

(5) the draft guidance on the cap and floor conditions in Nemo Link's electricity interconnector licence published alongside this letter.

We do not have any specific comments on the draft guidance on the cap and floor conditions in Nemo Link's electricity interconnector licence.

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