



Making a positive difference  
for energy consumers

Interconnector Operators,  
Nominated Electricity Market  
Operators and other interested  
parties

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Date: 6<sup>th</sup> March 2017

Dear colleague,

**Consultation on proposed approach to cost recovery in relation to Capacity Allocation and Congestion Management mechanisms for electricity interconnectors**

**1. Overview and purpose**

The Commission Regulation (EU) 2015/1222 establishing a guideline on Capacity Allocation and Congestion Management (CACM) is a central component of the internal electricity market, as set out in the EU Third Energy Package<sup>1</sup>. CACM, which came into force on 14 August 2015, aims to maximise the efficient use of interconnection and facilitate greater cross-border electricity trade, through market coupling in the day-ahead and intraday timeframes. Market coupling should make sure power is produced where it is most efficient and transported to areas of consumption where it is most valued. This should lower prices for consumers and support secure and sustainable supply.

Article 9 of CACM, **Adoption of terms and conditions or methodologies**, sets out a range of items requiring approval of the relevant National Regulatory Authority (NRA) as follows:-

*"8. The following terms and conditions or methodologies shall be subject to individual approval by each regulatory authority or other competent authority of the Member States concerned:*

*(e) capacity allocation and congestion management costs in accordance with Articles 75 to 79;"*

Article 75 of CACM, **General provisions on cost recovery**, provides that:-

*"Costs assessed as reasonable, efficient and proportionate shall be recovered in a timely manner through network tariffs or other appropriate mechanisms as determined by the competent regulatory authorities."*

This consultation sets out Ofgem's national proposals as to how GB interconnectors involved in the NWE Price Coupling Project and Cross Border Intraday (XBID) Project, referred to as the "CACM Pilot Projects", will recover their costs associated with these Pilot Projects and the enduring arrangements that are to apply retrospectively from 14 August 2015 and 14 February 2017, respectively. We invite comments on the proposals set out in this letter from all interested parties.

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<sup>1</sup> Directive 2009/72/EC and Regulation (EC) 714/2009

## **2. Timing issues: cost recovery arrangements for the pilot projects and the enduring arrangements from the entry into force of CACM**

To inform the drafting of CACM prior to its adoption by Member States and to assist Member States' compliance with legal deadlines established under the Regulation, the CACM Pilot Projects were the early implementation projects set up to develop market coupling solutions for day-ahead and intraday on a regional basis known as the NWE (North West Europe) Price Coupling and the Cross Border Intraday (XBID) Project respectively.

When CACM came into force on 14<sup>th</sup> August 2015 it provided a legal underpinning to what was previously a voluntary project and placed obligations on entities designated as Nominated Electricity Market Operators (NEMOs) – for example "Article 7: NEMO tasks, and on Transmission System Operators (TSOs)" – for example "Article 8: TSO's tasks related to single day-ahead and intraday trading".

From this date onwards CACM requires a number of tasks to be completed within fixed legal deadlines to deliver single day ahead and intraday coupling. Both NEMOs and TSOs have responsibility for undertaking those tasks.

### ***NWE (North West Europe) Price Coupling project***

We propose that enduring arrangements for cost recovery should apply to the NWE (North West Europe) Price Coupling project. Before that date special arrangements will be made as set out below.

### ***Cross Border Intraday (XBID) Project***

The National Energy Regulators of North West Europe and associated countries (the NWE + Regulators) wrote to the relevant TSOs on 16<sup>th</sup> January 2014 establishing cost recovery rules for the XBID pilot project and which stated that these would cover the final Development Contract and would last until the adoption of the XBID solution under CACM. However, an explicit limitation has been placed on this commitment by all NRAs to prevent it being entirely open ended and unreasonably exploited. This is discussed further in section 3 below in dealing with special arrangements for pilot projects.

## **3. Proposed cost recovery arrangements**

### ***Application of the matching convention***

We consider that the payment of costs must match the basis on which they were incurred. The key distinction is between costs relating to the creation and provision of infrastructure to provide the CACM capability on the one hand (development costs), and the operational costs associated with making use of that capability to make power trades, including clearing and settlement costs, (operational costs) on the other.

### ***Responsibility for development costs***

We propose that Interconnector TSOs bear GB's share of the development costs associated with establishing the Cross Border Intraday (XBID) Project and any amendments to XBID and the NWE Price Coupling Project, including providing continued access to the trading platform and necessary updates. As providing the capability for market coupling is a fundamental part of the product Interconnector TSOs offer to the market, we propose that the enduring arrangement for this capability should be paid for through the Interconnector TSO' congestion revenues. All these costs should be divided between the relevant TSOs on a basis to be proposed by the interconnectors and approved by Ofgem.

### **Responsibility for operating costs**

The cost of making use of that capability is the responsibility of those availing of the facilities, and we propose that the enduring arrangement for availing of this capability should therefore be borne by NEMOs that are designated or have passported into GB.

### **Special arrangements for the pilot projects**

We propose recovery of efficiently incurred development costs in relation to the CACM Pilot Projects by the Power Exchanges' (designated as NEMOs under CACM) through reimbursement by interconnector TSOs. For GB, the development costs relating to the CACM Pilot Projects will be recoverable from transmission network use of system (TNUoS) charges. To implement this proposal, modifications to the transmission licence of the National System Operator, NGET, and BritNed's interconnector licence will be necessary (note that for IFA this mechanism already exists within their interconnector licence).

We consider that these proposals are consistent with the NEW + Regulators letters to TSOs on 22 June 2102 addressing the price coupling (day ahead) project and that of 16 January 2014 addressing XBID (intraday).

The intention of the first letter was that that:-

- 100% of design costs, &
- 75% of implementation costs

would be covered by TSOs. The letter anticipates go live by end 2012 by which time design and implementation costs should largely have been incurred.

Similar cost issues related to XBID are addressed by the 16 January 2014 comfort letter and a letter from ACER on 31 March 2015 letter. These agree that:-

- 100% of the Final Development Contract for the XBID Solution will be covered by TSOs.
- Local implementation and operational costs are not covered but are to be addressed at national level

In the "REQUEST FOR AMENDMENT BY ALL NRAs AGREED AT THE ENERGY REGULATORS' FORUM ON ALL NEMOs' PROPOSAL FOR THE PLAN ON JOINT PERFORMANCE OF MCO FUNCTIONS (MCO Plan), 26.09.2016"<sup>2</sup> all Regulatory Authorities stipulated that as soon as the MCO Plan is approved, and from 14 February 2017 at the latest, XBID is acknowledged as the pan-European solution for single intraday coupling.

In line with this agreement, and given that the MCO plan has not yet been approved, Ofgem proposes 14 February 2017 as the point at which the enduring cost recovery arrangements for GB's share of XBID costs shall apply for GB NEMOs and TSOs.

These cost recovery proposals are summarised in Tables 1 & 2 below.

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<sup>2</sup> [https://www.ofgem.gov.uk/system/files/docs/2017/02/all\\_nra\\_position\\_paper\\_mco\\_plan.pdf](https://www.ofgem.gov.uk/system/files/docs/2017/02/all_nra_position_paper_mco_plan.pdf)

**Table 1: NWE (North West Europe) Price Coupling project: analysis of interconnector TSO and NEMO CACM costs by type and time**

<b>Cost type</b>	<b>Date incurred</b>	<b>Recovery from</b>
The CACM Pilot Project development costs	Before 14 August 2015	To be allowable against TNUoS
Development cost	After 14 August 2015	To be recovered from congestion revenues
Operational and clearing and settlement costs	Before 14 August 2015	Transaction costs, to be borne by Power Exchanges (designated as NEMOs under CACM) and not to be paid by Interconnector TSOs
Operational and clearing and settlement costs	After 14 August 2015	Transaction costs, to be borne by NEMOs and not to be paid by Interconnector TSOs

**Table 2: Cross Border Intraday (XBID) Project: analysis of interconnector TSO and NEMO CACM costs by type and time**

<b>Cost type</b>	<b>Date incurred</b>	<b>Recovery from</b>
The CACM Pilot Project development costs	Before 14 February 2017	To be allowable against TNUoS
Development cost	After 14 February 2017	To be recovered from congestion revenues
Operational and clearing and settlement costs	Before 14 February 2017	Transaction costs, to be borne by Power Exchanges (designated as NEMOs under CACM) and not to be paid by Interconnector TSOs
Operational and clearing and settlement costs	After 14 February 2017	Transaction costs, to be borne by NEMOs and not to be paid by Interconnector TSOs

All costs to be recovered in line with our proposals must be reasonable, efficient and proportionate. When assessing whether this criteria has been met we will consider whether the project milestones have been implemented on a timely basis and in the event of a delay, whether it is in consumers interests. We will work with the parties involved to ensure that this is and has been the case and to establish the correct categorisation of costs wherever there is an element of ambiguity.

#### **4. Responding and Next Steps**

We welcome the views of interested parties in relation to the proposals set out in this document. Please also send us supporting evidence to substantiate your views by 31 March 2017. Following consideration of responses, we will issue its decision on the matter.

Unless marked confidential, all responses will be published by placing them in Ofgem's library and on its website [www.ofgem.gov.uk](http://www.ofgem.gov.uk).

Respondents may request that their response is kept confidential. Ofgem shall respect this request, subject to any obligations to disclose information, for example, under the Freedom of Information Act 2000. Respondents who wish to have their responses remain confidential should clearly mark the document/s to that effect and include the reasons for confidentiality. Respondents are asked to put any confidential material in the appendices to their responses.

Responses should be sent to:

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Yours faithfully,

**Min Zhu**  
Associate Partner, Networks