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**OPINION OF THE AGENCY FOR THE COOPERATION OF ENERGY
REGULATORS No 07/2013**

of 25 March 2013

**ON THE SUITABILITY OF LONG RUN AVERAGE INCREMENTAL
COSTS FOR THE ASSESSMENT OF INTER-TRANSMISSION
SYSTEM OPERATOR COMPENSATION FOR INFRASTRUCTURE**

THE AGENCY FOR THE COOPERATION OF ENERGY REGULATORS,

HAVING REGARD to Regulation (EC) No 713/2009 of the European Parliament and of the Council of 13 July 2009 establishing an Agency for the Cooperation of Energy Regulators (hereinafter referred to as the “Agency”)¹,

HAVING REGARD to Commission Regulation (EU) No 838/2010 of 23 September 2010 on laying down guidelines relating to the inter-transmission system operator compensation mechanism and a common regulatory approach to transmission charging², and, in particular, point 5(5) of Part A of the Annex thereto,

WHEREAS:

- (1) Regulation (EC) No 714/2009 of the European Parliament and of the Council of 13 July 2009 on conditions for access to the network for cross-border exchanges in electricity and repealing Regulation (EC) No 1228/2003³ defines an inter-transmission system operator compensation (ITC) mechanism. Under this ITC mechanism, transmission system operators (TSOs) shall receive compensation for costs incurred as a result of hosting cross-border flows of electricity on their networks. The basis for establishing those costs are forward-looking long-run average incremental costs (LRAIC), while taking into account losses, investment in new infrastructure, and an appropriate proportion of the cost of existing infrastructure.
- (2) On this basis, Regulation (EU) No 838/2010 refines the framework for the operation of the ITC mechanism. Though it still relies on a LRAIC-based cost assessment for the compensation of costs of making infrastructure available to

¹ OJ L 211, 14.8.2009, p.1.

² OJ L 250, 24.9.2010, p. 5.

³ OJ L 211, 14.8.2009. p. 15.

host cross-border flows of electricity, it provides that the suitability of the LRAIC approach is reviewed by the Agency.

- (3) Similarly, the Florence Forum, in its 22nd meeting⁴, requested the Agency to identify whether the current ITC scheme needs enhancement.
- (4) In the course of its review of the ITC mechanism, the Agency has taken into account the results of an independent study commissioned to an external consultant and held a public consultation. The stakeholders' responses to the consultation were highly diverse regarding the desirable development of the ITC mechanism. There was no consensus on any determination method or even size of the ITC infrastructure fund. Besides, many responses either partly or completely suggested modifications to the ITC mechanism that are beyond the limits of the current legal framework. Moreover, many expressed concerns about the appropriateness of using the LRAIC approach,

HAS ADOPTED THIS OPINION:

The ITC mechanism proved to be an important instrument to facilitate the market integration process as it allowed the removal of transit fees on commercial cross-border flows, which represented, with the administrative mechanisms to allocate cross-border capacities and the priority access granted to historical contracts, the main obstacles to the development of an Internal Electricity Market.

A cost assessment based on LRAIC is forward-looking in terms of its costs and aims at mimicking the conditions of a competitive market.

This implies that the LRAIC methodology is appropriate for industries where the objective is to facilitate the entry of new participants in the market.

However, the purpose of the ITC mechanism is not to promote new entry, but rather to fix compensation rules between TSOs, which are local monopolies, for the efficient costs incurred as a result of hosting cross-border flows. Thus, applying the LRAIC approach might result in an undue over- or under-compensation, depending on the trend of unit costs.

⁴ Conclusions of the 22th meeting of the European Electricity Regulatory Forum, Florence 22 and 23 May 2012
http://ec.europa.eu/energy/gas_electricity/doc/forum_florence_electricity/2012_meeting_conclusions.pdf

Further, it is to be noted that in practice the LRAIC approach has not established itself as a relevant cost assessment methodology in the electricity sector. It is rarely applied in EU Member States for calculation of electricity transmission network tariffs. Several ITC-related studies and consultations, conducted during the period 2006-2012⁵, found a LRAIC assessment not acceptable as a compromise for compensating costs of transmission network infrastructure.

Therefore, the Agency has come to the conclusion that the LRAIC methodology is only of limited suitability in the context of the current ITC mechanism and that a new regulatory framework should be developed for the ITC.

Done at Ljubljana on 25 March 2013.

For the Agency:


Alberto Pototschnig
Director

⁵ Assessment of the annual cross-border infrastructure compensation sum, Consentec Report October 2012, http://www.acer.europa.eu/Official_documents/Public_consultations/PC_2012_E_15/Consentec_ACER_ITC-Fund_FinalReport_Draft.pdf ; Study on the further issues relating to the inter-TSO compensation mechanism, Consentec and Frontier Economics, Study commissioned by the European Commission, DG TREN, Final report, February 2006, ; http://ec.europa.eu/energy/gas_electricity/studies/doc/electricity/2006_03_tso_compensation_mechanism.pdf ; Study on further issues relating to the inter-TSO compensation mechanism –assessment of cost level data, Consentec and Frontier Economics A report prepared for the European Commission, July 2007, http://ec.europa.eu/energy/gas_electricity/studies/doc/electricity/2007_09_inter_tco.pdf



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