

**RED**  
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## New remuneration for electricity transmission



9 January 2014



## New reference framework for the electricity sector

- The new Electricity Sector Law was passed on 26<sup>th</sup> December (Law 24/2013)
- The Royal Decree of Transmission was passed on 27<sup>th</sup> December (RD 1047/2013)
- Mechanisms have been established to minimise differences between income and expenses by means of the automatic review of tolls and charges
- The principles and criteria establishing remuneration for regulated activities have been strengthened and clarified to bring them into line with European peers
- The transmission activity is part of a more stable and predictable backdrop

**Guaranteeing supply, quality and the economic and financial sustainability of the electricity system**



## **New regulation to guarantee the stability of the electricity transmission activity**

**Transparent,  
stable and  
predictable**

**Sustainable**

**Incentives  
for efficiency**



## Key principles

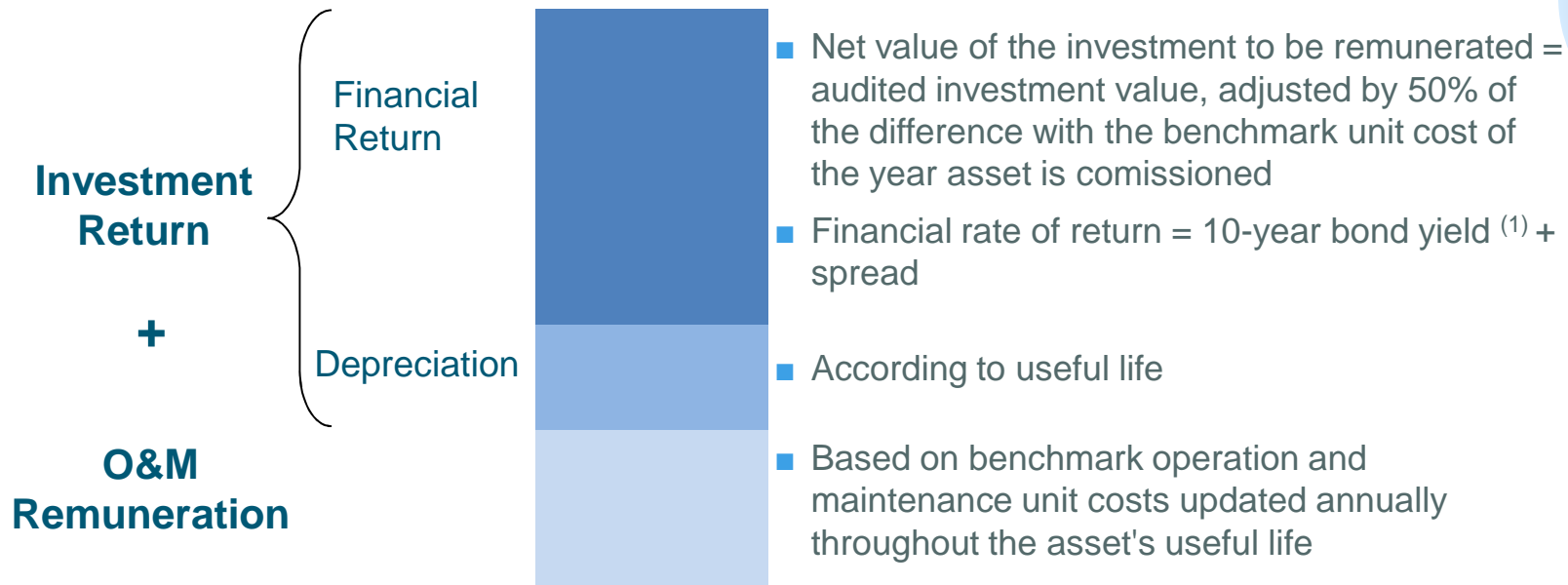
Transparent,  
stable and  
predictable

- A single methodology applicable to all electricity transmission facilities.
- 6-year regulatory periods. First regulatory period ends 31 December 2019.
- Remuneration of investment shall be made for all assets in service according to their net value. All assets currently in operation are assigned a useful life and a return on investment.
- Facilities will be remunerated according to when they were brought into service (eliminating the penalty arising from the n+2 effect and compensation up to “n” for facilities commissioned after 1998).
- Based on reference unit capex costs and operation and maintenance costs.
- The financial return is benchmarked to the Spanish 10-year bond yield. This will increase by a spread to be revised in each regulatory period.
- The useful life of facilities may be extended and remuneration set for when this occurs.
- Incentives for efficiency and availability of the transmission network will be established.



## General remuneration model for transmission facilities

Transparent,  
stable and  
predictable



(1) 10-year Government bond yield in secondary market over 24 months before May of the year prior to the start of the regulatory period.

- Financial expense recognized arising from delays between the commissioning of the facility and the remuneration collection on investment and O&M.
- In the 1<sup>st</sup> regulatory period, the differential will be 200 bp while the rate of return is set at 6.5% before tax.
- Once the useful life ends, the extension of useful life will be remunerated in addition to O&M retribution



Transparent,  
stable and  
predictable

## Remuneration for assets in operation

INVESTMENT RETURN

**Assets  
prior  
to 98**

- Implicit valuation based on retribution on investment associated with these facilities.
- The average residual life set by the Ministry of Industry, Energy and Tourism will be used.
- The residual life may increase depending on renovation and improvements made.
- Assets are valued at replacement cost based on benchmark unit investment costs<sup>(\*)</sup>.
- The useful life will be calculated based on the year each facility was brought into operation.

**Assets  
after  
98**

- The applicable financial rate of return for the first regulatory period is 6.5%

### OPERATION AND MAINTENANCE REMUNERATION

- Based on benchmark operation and maintenance unit costs<sup>(\*)</sup>

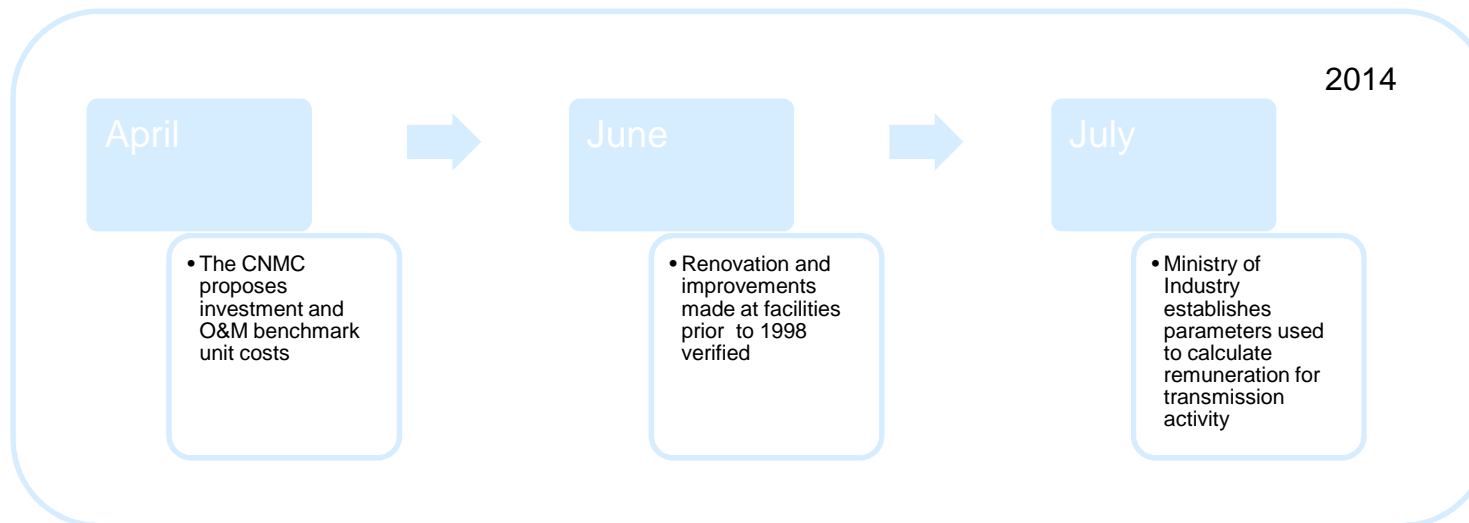
*\* Benchmark unit investment and O&M costs will be defined by the Ministry of Industry, according to proposals from the CNMC.*



## Pending regulatory issues

Transparent,  
stable and  
predictable

- Investment and O&M benchmark unit costs must be established.
- Set average residual life of facilities prior to 1998 by verifying renovation and improvements carried out at assets prior to 98.
- New plan defining investment requirements for new electricity transmission facilities.





## Sustainability

Sustainable

- Tools have been introduced to align investment in the transmission network with the system's financial sustainability.
- Annual volume may not exceed 0.065% of estimated GDP for a certain year, unless economic or technical reasons make it necessary. Maximum investment established is assumed by the electricity system as an annual cost.
- The Ministry of Industry must submit estimates for transmission revenue over a period of six years.

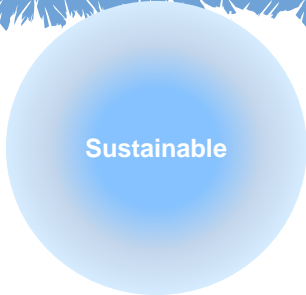
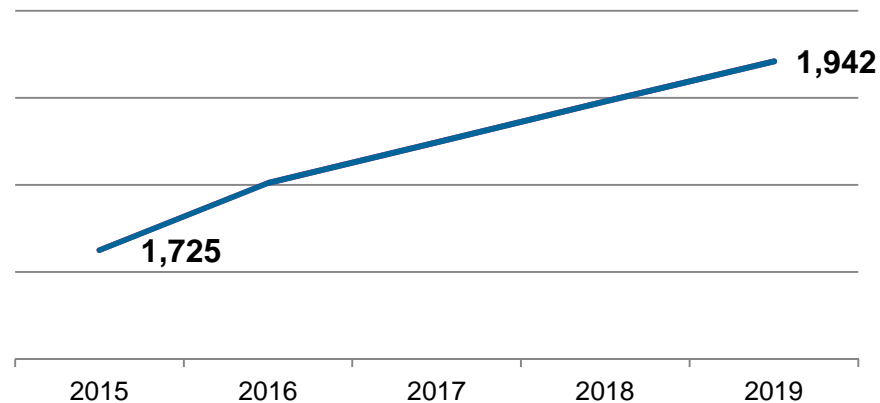




## Sustainable, stable and predictable revenue

Estimated transmission tariff according to RD (\*)

**Transmission remuneration**  
(€mn)

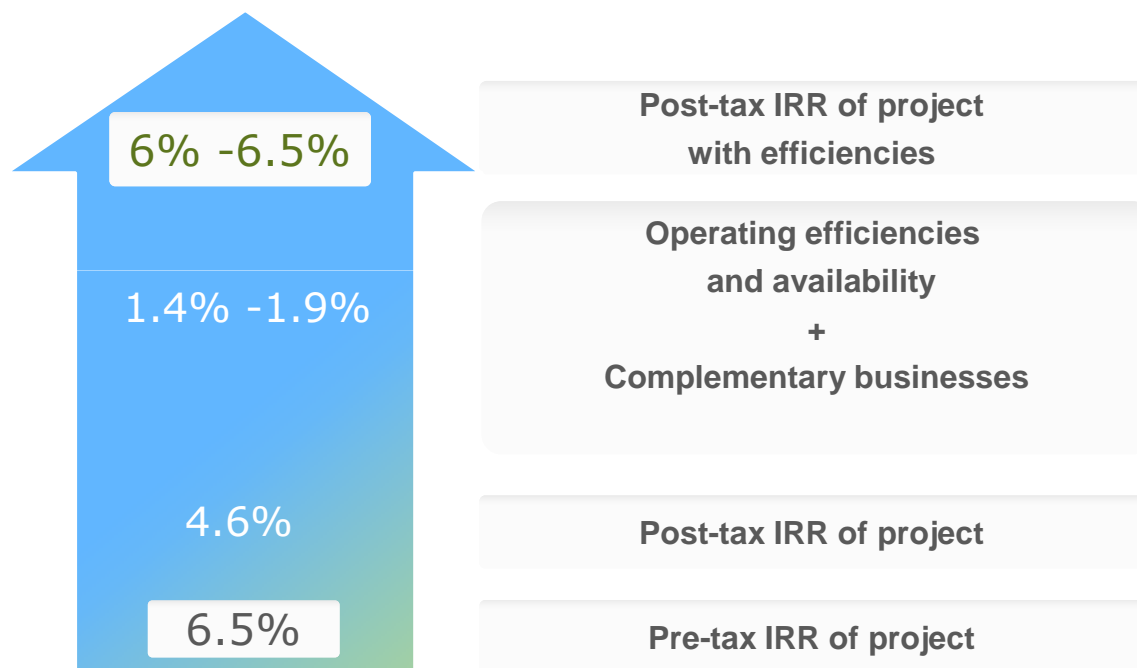


- Forecasts have been calculated using temporary methodology as per RD-I 9/2013, of 12 July.
- Hypothetical annual investment scenario of €600 mn.
- Revenue performance includes availability incentive and remuneration for Gas Natural-Fenosa assets (approx €37 mn in 2013).
- 2015 is the start year of the first regulatory period.
- The 2014 tariff for REE is estimated at over €1,600 million and approx 1,685€mn in 2015.

(\*) Figures taken from analysis report of the regulatory impact of Royal Decree 1047/2013 sent to the State Council establishing the methodology used to calculate electricity transmission remuneration and the regime of payments for access and connection studies for transmission networks.



## Return on new investment



**Additional measures to create value: financial and process management**



## Next steps

- Achieve a reasonable outcome for various pending remuneration and regulatory aspects.
- Analyse treatment of maintenance capex.
- Review main operating processes according to efficiency and adequate quality criteria.
- Develop a suitable remuneration model for system operations.
- Define Strategic Plan for forthcoming years.



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