



MEMORANDUM

TO Authority for Consumers & Markets

DATE

July 7, 2017

REFERENCE

REC-N 17-034

FROM

SUBJECT Report auction receipts TenneT TSO B.V. for the period January 2016 - June 2017

REPORT DECISION

1. Introduction

TenneT TSO B.V. ("TenneT") provides this report in order to enable the Authority for Consumers & Markets ("ACM") to comply with the requirements as defined in article 6.5 of annex 1 of 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 1228/2003 ("Regulation").

This report contains the following information:

- Realised auction receipts and withdrawals for the period January 1, 2016 – June 30, 2017.
- Intended withdrawals from the auction receipts for the period July 1, 2017 – June 30, 2018.
- Annex 1: realised auction receipts and withdrawals for the period January 1, 2016 – December 31, 2016, accompanied by an unqualified auditor's report.

The withdrawals from the auction proceeds comply with the purposes mentioned in the Regulation.

2. Realised auction receipts and withdrawals for the period January 1, 2016 – June 30, 2017

2.1 General information

TenneT is certified as transmission system operator ("TSO") for the Dutch national (extra) high voltage grid and as the interconnector operator for the southern part of the NorNed Cable. TenneT is exclusively charged with the management of cross-border interconnections with alternating current on the Belgian and German borders. The management includes applying non-discriminatory and transparent transfer capacity allocation mechanisms as prescribed by the EC Electricity Regulations (EC Regulations no. 96/92, 2003/54, 2009/72), 2009/714 the Electricity Act and implementing regulations. These mechanisms include the auctions performed by Joint Allocation Office S.A. ("JAO"). JAO is a joint service company of twenty Transmission System Operators in seventeen countries. JAO's principle activity is facilitating the yearly, monthly and daily auctions of transmission rights between 27 countries in Europe. Furthermore TenneT operates the so-called NorNed Cable, an interconnector with direct current between Norway and the Netherlands.

The Foundation for the Management of Allocated Funds from the National High-Voltage Grid (Stichting Beheer Doelgelden Landelijk Hoogspanningsnet) ("The Foundation") is a foundation established under Dutch law for the management of the "allocated funds" received from TenneT in its capacity as administrator of the National EHV Grid. These allocated funds comprise proceeds of imbalance settlements (not within scope of this report) and proceeds from market-based allocation of cross-border electricity transfer capacity (including proceeds from explicit or implicit auctions of interconnector capacity). TenneT is not allowed to use the allocated funds for other objectives than set forth in the Regulation. According to the relevant competence agreement (bevoegdhedenovereenkomst) with ACM the surplus funds of The Foundation will be used for (future) tariff reductions.

In accordance with article 16.6 of the Regulation the auction receipts shall be used for the following purposes:

6. Any revenues resulting from the allocation of interconnection shall be used for the following purposes:

(a) guaranteeing the actual availability of the allocated capacity; and/or

(b) maintaining or increasing interconnection capacities through network investments, in particular in new interconnectors.

If the revenues cannot be efficiently used for the purposes set out in points (a) and/or (b) of the first subparagraph, they may be used, subject to approval by the regulatory authorities of the Member States concerned, up to a maximum amount to be decided by those regulatory authorities, as income to be taken into account by the regulatory authorities when approving the methodology for calculating network tariffs and/or fixing network tariffs.

The rest of revenues shall be placed on a separate internal account line until such time as it can be spent on the purposes set out in points (a) and/or (b) of the first subparagraph. The regulatory authority shall inform the Agency of the approval referred to in the second subparagraph.

The allocated funds are invested within the boundaries of the treasury statute of The Foundation when they are temporarily placed on a separate internal account as prescribed in the Regulation. The treasury statute of TenneT Holding B.V. also applies to the Foundation. The statute contains principles which cover specific areas such as interest rate risk, liquidity risk, the use of derivatives, and the investment of excess liquidity. The return on these investments is added to the auction receipts.

In 2016 the management of the allocated funds was executed by The Foundation. The overview of auction receipts provided in this report reconciles with the financial administration of TenneT. The figures for the auction receipts 2016 have been used for the preparation of the statutory annual accounts of TenneT for the year 2016. The figures for the auction receipts during the first half of 2017 will be used for the preparation of the half-year report 2017 of TenneT Holding B.V.

2.2 Overview realised auction receipts and withdrawals

The movement schedule for the auction receipts during the period January 1, 2016 – June 30, 2017 is included in the overview below:

| Table 2 - Auction receipts TenneT TSO B.V. | | | | | |
|---|--|------------------------|-------------------------|-------------------------|------------------------|
| 714/2009 reference | Book year (numbers in EUR X 1.000) | 2016 (1-1 t/m 30/6) | 2016 (1-7 t/m 31/12) | 2016 (1-1 t/m 31/12) | 2017 (1-1 t/m 30/6) |
| | Opening balance auction receipts | -830.520 | -808.188 | -830.520 | -768.244 |
| | Norred | | | | |
| | Plus: transmission right revenues NorNed auction | -7.714 | -8.968 | -16.682 | -11.152 |
| 16.6a | Minus: contribution TenneT towards auction costs | 254 | 194 | 448 | 200 |
| 16.6a | Minus: costs grid losses | 163 | 148 | 311 | 155 |
| 16.6a | Minus: costs for balancing and reserve power | 316 | 1.152 | 1.468 | 796 |
| | Net revenue NorNed | -6.981 | -7.474 | -14.455 | -10.001 |
| 16.6a | Minus: outcome NorNed bonus-penalty scheme relative availability | | 1.450 | 1.450 | 11 |
| | Plus: credit note 2013-11 cable outage 30-10/20-12-2013 | -23 | | -23 | |
| | Net addition NorNed | -7.004 | -6.024 | -13.028 | -9.990 |
| | Auctions other interconnectors | | | | |
| | Plus: transmission right revenues interconnectors: NL-DE and NL-BE | -23.368 | -29.699 | -53.067 | -25.473 |
| 16.6a | Minus: contribution TenneT towards auction costs | 1.760 | 1.091 | 2.851 | 1.621 |
| | Net addition other interconnectors | -21.608 | -28.608 | -50.216 | -23.852 |
| | Plus: net income from participation TenneT GmbH & Co. KG | -13.852 | 2.992 | -10.860 | -13.856 |
| | Plus: net addition interest revenues | -247 | -65 | -312 | - |
| | Net other revenues | -35.707 | -25.681 | -61.388 | -37.708 |
| | Other additions / withdrawals | | | | |
| 16.6a | Minus: overhead costs (according to Netcode art. 5.6.15) | 114 | 30 | 144 | - |
| 16.6 | Minus: auction receipts used for reduction of transmission tariffs | 64.929 | 64.928 | 129.857 | 86.808 |
| 16.6a | Minus: redispatch critical branches | - | 6.691 | 6.691 | 17.949 |
| | Total other additions / withdrawals | 65.043 | 71.649 | 136.692 | 104.757 |
| | Movement auction receipts | 22.332 | 39.944 | 62.276 | 57.059 |
| | Closing balance congestion revenues | -808.188 | -768.244 | -768.244 | -711.185 |

Please note that the report for the period 2016 accompanied by an unqualified auditor's report is attached in annex 1 to this report.

2.3 Disclosures to overview realised auction receipts and withdrawals

2.3.1 Receipts and withdrawals NorNed

In accordance with the ACM decision dated November 14, 2007 (reference: 102746) the capacity of the NorNed cable becomes available for the market through an auction. The auction receipts are equally divided between TenneT and its counterpart Statnett SF. The TenneT part of these receipts has been added to the auction receipts since the start of NorNed.

In accordance with article 16.6 of the Regulation TenneT has withdrawn an amount of EUR 0.3 million regarding grid losses for the NorNed cable in 2016 and an amount of EUR 0.2 million for the first half of 2017.

In accordance with article 16.6 of the Regulation TenneT has withdrawn an amount of EUR 1.5 million regarding balancing and reserve power for the NorNed cable in 2016 and an amount of EUR 0.8 million for the first half of 2017.

In accordance with article 16.6 of the Regulation TenneT has withdrawn an amount of EUR 0.4 million regarding operational costs for the execution of the auctions for the NorNed cable in 2016 and an amount of EUR 0.2 million for the first half of 2017.

In accordance with ACM decision 101783_2-76 TenneT is entitled to an incentive in the situation that the availability of the NorNed cable exceeds predefined limits. Based on the decision of ACM dated April 5, 2017 (reference: ACM/DE/0217/202057) TenneT is entitled to withdraw an amount of EUR 1.5 million from the auction receipts with regard to the availability of the NorNed cable during 2016.

2.3.2 Receipts and withdrawals other interconnectors

The yearly, monthly and daily auctions of transmission rights for the other interconnectors are performed by JAO. The annual and monthly capacity is allocated by means of explicit auctions. At such auctions, the market party acquires long term transmission rights. The European system operators have created shared rules governing the explicit auctions for allocating annual and monthly capacity. TenneT receives 50% of the auction receipts on the Belgian and German borders.

The daily capacity is allocated to market parties through an implicit allocation mechanism. The power exchanges and the involved TSO's organise this by means of day-ahead market coupling. Per May 21, 2015 flow based market coupling was introduced in the CWE region. As a result the distribution of the auction proceeds between the involved TSO's has also been changed.

In accordance with article 16.6 of the Regulation TenneT has withdrawn an amount of EUR 2.9 million regarding operational costs for the execution of the auctions for the other interconnectors in 2016 and an amount of EUR 1.6 million for the first half of 2017.

2.3.3 Participation in TenneT Germany

In 2010 The Foundation participated in the acquisition of transpower stromübertragungs GmbH (subsequently renamed TenneT TSO GmbH). The Foundation contributed EUR 375 million and obtained 2,000 Class B shares in TenneT TSO Duitsland B.V. in return. Based on the requirements set by the Dutch government The Foundation financed EUR 300 million of this transaction through the auction receipts and obtained a loan of EUR 75 million from TenneT Orange B.V. for the remaining amount.

In order to protect the allocated funds and to ensure their immediate availability upon request from ACM a put- and a call option have been emitted at 25 February 2010. The call option with an exercise price of EUR 375 million and a maturity period of ten years entitles TenneT Holding B.V. to acquire the investment from The Foundation. The put option has an exercise price of EUR 375 million and a maturity period of ten years and requires TenneT Orange B.V. to buy the investment for The Foundation upon offer. TenneT Orange B.V.'s obligation is substantially covered by a guarantee issued by the Dutch State for an amount of EUR 300 million expiring in 2020.

All proceeds and costs related to the abovementioned structure have been added / withdrawn from the auction receipts. In 2016 the total proceeds that are added to the auction receipts amount to EUR 10.9 million.

2.4 Other additions / withdrawals

2.4.1 Tariff reduction

In accordance with article 16.6 of the Regulation and the competence agreement (bevoegdhedenovereenkomst) with ACM of December 15, 2015 (reference: ACM/DE/2015/206388_OV) TenneT will use the auction receipts for (future) tariff reductions. The calculation method for the annual withdrawal from the auction receipts for this purpose is included in this agreement. Based on this calculation method TenneT used an amount of EUR 129.9 million to reduce its tariffs for 2016 and TenneT will withdraw an amount of EUR 173.6 million to reduce its tariffs for 2017 (refer to tariff decision 2017 with reference: ACM/DE/2016/207614).

2.4.2 Operational costs of The Foundation

An amount of EUR 0.1 million has been withdrawn in 2016 for operational costs of The Foundation for the management of the allocated funds. This withdrawal is in accordance with article 16.6 of the Regulation.

2.4.3 Redispatch costs related to critical branches

The Regulation requires TSOs to optimise cross-border capacity of the interconnections and the transmission networks affecting cross-border flows, while complying with safety standards of secure network operation.

As a result guaranteeing the actual availability of allocated capacity and maintaining or expanding capacity of the interconnections and of the transmission networks affecting cross-border flows contributes to the purposes laid down in the EU legislation. In accordance with article 16.6 of the Regulation these activities can be funded from the revenues resulting from the allocation of interconnection (hereinafter cross-border congestion income). TenneT has withdrawn an amount of EUR 6.7 million regarding redispatch costs related to critical branches in 2016 and an amount of EUR 17.9 million for the first half of 2017.

The interconnectors and relevant parts of the transmission network that are affected by cross-border flows are identified as 'critical branches' in accordance with the implemented Flow Based Allocation Methodology.

In the following situations TenneT is using cross-border congestion income to fund the costs of solving congestions on critical branches (both upward and downward adjustment of transported volumes by means of redispatch and/or countertrade):

- I. If planned non-availability of a critical branch is required to enable the increase of capacity of the critical branch.
- II. If the critical branch is temporarily not available.
- III. If there is an unplanned outage of a critical branch.
- IV. If the scheduled transport on the critical branch exceeds security limits.

These situations are further explained in the following sections:

- I. Expansion of capacity of critical branches

TenneT is planning to increase the capacity of a significant number of critical branches. It is expected that these capacity increases require certain periods of planned non-availability (planned outage) for these critical branches as the expansion work needs to be conducted with these branches disconnected from the operating network.

Naturally TenneT plans to perform these activities when the market does not require this capacity, however TenneT expects that this will not be possible in all situations. Increasing the capacity of existing branches is a complex process which requires relatively long periods in which the relevant assets are disconnected from the operating network.

Any costs arising from the application of costly measures such as redispatch and/or countertrade to allow investments in the increase of capacity of critical branches are funded through the cross-

border congestion income, as they contribute to the primary goals of the regulation to increase and maintain the cross-border capacity.

II. Temporary non-availability of a critical branch (planned outage)

In case a critical branch is temporarily not available due to planned work, for instance maintenance, it will be disconnected from the operating network. As the work contributes to maintain the cross border and/or critical branch capacity the associated redispatch and/or countertrade costs will be funded from the cross-border congestion rents.

III. Temporary not foreseen non-availability (unplanned outage)

In case there is unforeseen non-availability of a critical branch, TenneT needs to take action to ensure that the network returns to a normal state which is characterised by operational security limits. These measures contribute to maintaining the planned use of the critical branch and thus to guaranteeing the already allocated cross-border capacity. Any costs arising from these measures can thus be funded from the cross-border congestion income.

IV. Scheduled transport on the critical branch exceeds operational security limits

It is the intention of the Flow Based Methodology to maximise cross-border capacity provided to the market, while respecting a secure operation of the transmission grid. The flow based market coupling algorithm respects actual limitations in the transmission grid and takes them into account while calculating the cross-border capacity. This is a complex process which applies amongst other things Flow Reliability Margins (FRM) and takes into account the already allocated long term transmission capacity (LTA inclusion).

The FRM for instance is determined based on statistical methods. The method does not consider the 10% of most extreme deviations when setting the margin. This could result in overloads on specific critical branches in the operational time frame even when the methodology aims not to provide more capacity than is physically secure. The allocated capacity could also breach the operational security limits for a number of other reasons for instance due to the LTA inclusion.

These examples demonstrate that even with the application of the Flow Based Methodology it is still possible to have overloads on critical branches in the operational time frame.

As TenneT should comply with the operational security limits these overloads may result in redispatch or other actions in the day-ahead, intra-day or real timeframe. The costs of the associated actions will be funded with cross-border congestion income, as they contribute to guaranteeing already allocated cross-border capacity.

3. Intended withdrawals from the auction receipts for the period July 1, 2017 – June 30, 2018.

In accordance with article 16.6 of the Regulation TenneT intends to use the auction proceeds in the period July 1, 2017 – June 30, 2018 for the following purposes:

I. Energy & capacity expenses for the NorNed cable.

The estimated withdrawal is based on historical costs and amounts approximately EUR 2.0 million. These withdrawals are in accordance with article 16.6 of the Regulation.

II. Operational costs for the execution of the auctions for interconnection capacity on the borders with Belgium, Germany and Norway.

The estimated withdrawal is based on historical costs and amounts approximately EUR 3.5 million. These withdrawals are in accordance with article 16.6 of the Regulation.

III. Availability incentive NorNed

In accordance with ACM decision 101783_2-76 TenneT is entitled to an incentive in the situation that the availability of the NorNed cable exceeds predefined limits. If a higher availability is realised TenneT will withdraw an amount with a maximum of approximately EUR 1.5 million from the auction receipts. If a lower availability is realised TenneT will add an amount to the auction receipt with a maximum of approximately EUR 1.5 million.

IV. Operational costs of The Foundation

The estimated withdrawal for operational costs of The Foundation amounts to approximately EUR 0.1 million. This withdrawal is in accordance with article 16.6 of the Regulation.

V. Redispatch, countertrade and curtailment costs related to critical branches

As already disclosed in paragraph 2.4.2 of this document TenneT will withdraw the costs for redispatch, countertrade and curtailment related to critical branches from the auction receipts. Given the unpredictable nature of these costs TenneT is not able to provide an estimated withdrawal for this period. This withdrawal is in accordance with article 16.6 of the Regulation.

- VI. In accordance with article 16.6 of the Regulation and the competence agreement (Bevoegdhedenovereenkomst) with ACM of December 15, 2015 (reference: ACM/DE/2015/206388_OV) TenneT will use the auction receipts for (future) tariff reductions. The calculation method for the annual withdrawal from the auction receipts for this purpose is included in this agreement. Based on this calculation method TenneT will withdraw an amount of EUR 173.615.855 to reduce its tariffs for 2017 (refer to tariff decision 2017 with reference: ACM/DE/2016/207614).

The withdrawal from the auction receipts for the reduction of the tariffs 2018 will be calculated as part of the tariff proposal 2018.