RED ELÉCTRICA DE ESPAÑA

Grupo Red Eléctrica

Draft Circular CIR/DE/008/19 of the CNMC establishing the remuneration methodology for electricity transmission.

Executive Summary.

Scope of Comments and Arguments

8 August 2019

Table of contents

1. Background

The CNMC, in accordance with the duties set out in article 7.1.i) of Law 3/2013, of 4 June, regarding the creation of the Spanish National Markets and Competition Commission ('CNMC'), has publicly disclosed Draft Circular CIR/DE/008/19, which establishes the methodology for the calculation of the remuneration of the electrical energy transmission activity (hereinafter, the 'Draft Circular'), together with its Justification Report, and has initiated the public consultation procedure.

On 5 July 2019, Red Eléctrica de España, S.A.U. ('Red Eléctrica') received the communication from the CNMC giving official notice of the Draft Circular, indicating that the final date for the period allotted for the public information & consultation procedure was August 9.

Prior to the official notice of the Draft Circular being sent, the BOE (the Official State Gazette) had published, on 9 April, Order TEC/406/2019 of 5 April, of the Ministry for the Ecological Transition ('MITECO'), establishing the energy policy guidelines for the CNMC. In said Order, section four sets out *the guidelines related to the 'Circular on the Remuneration Methodology for Electricity Transmission'*.

The present document contains an executive summary of the main observations of Red Eléctrica, as transmission agent, regarding the new remuneration methodology for electricity transmission contained in the Draft Circular.

2. Executive summary

The following is a summary of the main proposals and observations that Red Eléctrica makes to the Draft Circular.

2.1. Main impacts of the Draft Circular on the electricity transmission activity

On January 11, 2019, Royal Decree-Law 1/2019 on urgent measures was approved to bring the competencies of the Spanish National Markets and Competition Commission ('CNMC') in line with the requirements of EU law in relation to Directives 2009/72/EC and 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in electricity and natural gas, hereinafter 'RDL 1/2019'.

RDL 1/2019-Law modifies article 7.1 of Law 3/2013, of June 4, regarding the creation of the CNMC, and assigns to the Commission the duty, among other responsibilities, of establishing, by Circular, prior public consultation procedure and with economic efficiency, transparency, objectivity and non-discrimination criteria, the methodology for the remuneration of transmission facilities as well as the methodology for calculating the financial rate of return.

In relation to the electrical energy transmission activity, the powers conferred on the CNMC in the mentioned RDL 1/2019 are those of approving the methodology, the remuneration parameters, the regulated asset base and the annual remuneration of the activity.

As mentioned, the new methodology contemplated in the Draft Circular should also consider the energy policy guidelines set by MITECO, among which are the following in relation to the Circular on electricity transmission:

- The new methodology should ensure that changes in methodologies that, where appropriate, are introduced, are accompanied by mechanisms for their gradual adoption and implementation.
- The methodology should adequately remunerate the new investment needs that will be derived from the 2021-2026 Planning, both in terms of volume and nature (assets for smart transmission grid management based on IT and communications technologies, that have lower return on investment periods and greater uncertainty), appropriately distributing the risks between the grid owner, users and consumers, in order to guarantee a supply at the lowest cost possible.
- The remuneration methodology should require that owners of grid assets incorporate a principle of financial prudence.
- The remuneration methodology should incentivise extending the continued operation of assets that have exceeded their remunerated life-cycle, in order to contribute to the optimal management of national resources and under the principle of optimizing the return on investment for consumers and maintaining assets already built and depreciated under appropriate operating conditions, avoiding the need to replace them at a higher cost.

The previous regulatory framework for electricity transmission activity (reform of regulated activities carried out in 2012 and 2013, and specifically Royal Decrees 1047/2013 and 1073/2015), was established in an exceptional context derived from the financial crisis and the deficit of the electricity sector. These measures brought about a significant adjustment to revenues and therefore to the profitability of regulated activities, and in particular to electricity transmission.

The Draft Circular to establish the methodology for the calculation of the remuneration of the electricity transmission activity remains in line with the methodology of the aforementioned Royal Decrees, however, new adjustments are introduced for the next regulatory period that in the current situation, once the deficit is eliminated and within the context of the challenges posed by the energy transition, should not be necessary. Moreover, some adjustment measures of an extraordinary nature that were adopted at that time and that only affected the electricity transmission and distribution activities are not reversed.

Detailed on the following pages, are the most strategic and relevant aspects for the transmission activity and how they will be impacted during the next 2020-2025 regulatory period by the remuneration model methodology proposed by the CNMC. A summary of the main proposals made by Red Eléctrica regarding the Draft Circular has also been prepared.

2.1.1. Investment

The Draft Circular introduces a series of measures that, in the first instance, limit the realisation of investments and introduce uncertainty, as well as an administrative burden, which will reduce agility in the context of the Energy Transition that in turn will require the commitment and flexibility of all the agents involved so that it may come to fruition.

The Draft Circular modifies the reference indicator used to establish the annual investment limit, replacing the current reference indicator (based on GDP and the annual limit on it of 0.065%), with an index weighted by 70% of the increase in demand and 30% of the increase in the penetration level of renewable energy over the investment limit established in the previous year.

The Report itself that accompanies the Draft Circular already mentions that investments will be reduced in the future as a result of the new way of calculating the limit: "*the sectoral limits that would be obtained by applying the new methodology, would be lower than those resulting from the application of Royal Decree 1047/2013* ."

In short, there is a reduction in the annual investment limits for the upcoming regulatory period, and there is also great uncertainty about the parameters used by the CNMC to estimate the investment limits. In addition, elements that are at their discretion are incorporated, such as the 'scale factor' that will be used to calculate the investment limit, without the methodology for its calculation being detailed.

2.1.2. Remuneration and Profitability of Investments

The Draft Circular introduces a series of additional measures to those already introduced by Royal Decree 1047/2013, all of them tending towards reducing the profitability of future investments.

Firstly, noteworthy of mention is the incorporation of a measure consisting of limiting the recognised investment value in the event the real investment value exceeds the unit value.

The current remuneration model, and the one proposed by the new Draft Circular, bases investment on unit construction costs. This means that investment is based on average costs for the whole of Spain and therefore the execution of the different projects, depending on where they are carried out (on the plateau, in the mountains, on the coast, ...), may be below and above the established unit values.

Furthermore, this measure implies a differentiated and unjustified approach with respect to other regulated activities, where such limits do not exist or apply.

In relation to EU subsidies, the previous model allowed the transmission agent to retain 10% of such subsidies, as an economic incentive to obtain them. The Draft Circular maintains this percentage, although it limits the amount to be retained by the transmission agent to €5 million (per project).

This measure again reduces the profitability of investments with respect to the previous model and discourages the transmission agent from dedicating resources and making the effort to obtain the aforementioned subsidies. Far from increasing the efficiency of the Spanish transmission agent, this measure will increase the efficiency of the European transmission agents that will be able to benefit from the funding that Red Eléctrica will no longer receive and consequently will increase the cost that Spanish consumers will have to bear.

Additionally, the remuneration model of the transmission activity maintains the criteria for the beginning of the accrual and collection of the remuneration of transmission facilities commissioned in year 'n', from 1 January of year 'n + 2'. That is to say, a mechanism has been consolidated that was implemented at a time of extreme financial difficulty, which is not applied by the various regulators to the transmission agents of the countries around us (some of which begin to receive the remuneration during the construction period itself, as they begin to receive the remuneration for works that are underway). This measure represents a deficit that the transmission agent must assume and finance as the consumer 'enjoys' facilities that begin to be remunerated 2 years later.

The elimination of the 'n + 2' criteria would additionally contribute to reducing the indebtedness of the transmission activity and facilitate compliance with the CNMC ratios established in its draft '*communication regarding the definition of ratios to assess the level of indebtedness and the economic-financial capacity of the companies that carry out regulated activities, and of their recommended value ranges*'. This would also enable compliance with the orientation

of the energy policy consisting of the principle of financial prudence that should govern the remuneration methodology.

In the current context, it is considered that the application of this remuneration criteria has ceased to make sense as, in addition to having been established at a time of financial stress in the entire electricity system that is no longer the case today, it already lacks regulatory support as it has disappeared from the LSE (Spanish Power Sector Law).

In the activities for the transmission and distribution of gas this deferral of the beginning of the collection and accrual of the remuneration is not contemplated, so a discriminatory situation would arise.

All these measures that impact on the profitability of the investment are now coupled with the reduction in profitability caused by the new financial rate of return set forth in the Draft Circular published by the CNMC that establishes the methodology for calculating the financial remuneration rate. The new rate entails that the profitability of investments (both past and future) would be reduced from 6.503% to 5.58% as of 2021, although, exceptionally, the rate in 2020 would be 6.003% as a result of Royal Decrees 1047/2013 and 1048/2013 (remuneration models for electricity transmission and distribution, respectively) which established that "in no case may the proposed variation of the Financial Rate of Return ('FRR') used between two consecutive years be greater than 50 basis points in terms of absolute value"

Not surprisingly, though the reduction was a contemplated (since the Draft Circular is aligned with the proposal that the CNMC published in October 2018), should the impact it will have on revenues of all regulated activities in the field of electricity, and especially in transmission, be ignored.

In addition, the Draft Circular does not maintain the mechanism of a gradual adoption and implementation process in the future that was set out in the previous remuneration methodology (Royal Decrees 1047/2013 and 1048/2013, remuneration models for electricity transmission and distribution, respectively, which established that "in no case may the proposed variation of the financial rate of return used between two consecutive years be greater than 50 basis points in terms of absolute value"), as the Draft Circular establishes that the methodology for calculating the FRR, should the variation between 2 years not exceed 50 basis points, is limited to only the year 2020, as it is considered as an 'exceptional' measure.

In this regard, the Draft Circular has only applied a gradual implementation mechanism for the adoption of the FRR (although it is of an 'exceptional' nature). However, as will be argued throughout this document, the Circular that is finally approved should establish mechanisms for a gradual implementation process of other parameters, as previously indicated, in order to comply with the principle of financial prudence and consequently not jeopardise compliance with the ratios proposed by the CNMC.

2.1.3. Extending the useful life of assets that reach the end of their regulatory life

The previous remuneration model considered all facilities prior to 1998, which represent a significant percentage of the transmission grid, as a single facility with a single residual life, instead of considering them individually with different residual lives based on the date each of them was brought into service. This model assumes that all these facilities reach the end of their regulatory life at the same time, meaning that in 2023 there would be an exceptional drop in revenue, which would have been gradual had the residual life been individualised.

This exceptional situation generated by the previous remuneration model, requires measures that avoid the serious problem of economic and financial stability that will occur as of that year. Therefore, it is necessary that extraordinary measures be applied, such as a mechanism that allows the gradual management of the fall in revenue, so that its impact can be spaced out over several years in line with that established in the energy policy guidelines.

In addition, the previous remuneration model did not give have a mechanism to deal with the investments to be made regarding these facilities, beyond the transitory solution for the investments made between 2015-2018 included in Royal Decree 1073/2015, which temporarily extended the problem but did not provide a solution for it.

The non-consideration of this mechanism would also cause the principle of financial prudence contained in the energy policy guidelines to not be fulfilled, as the transmission activity would suffer a worsening of its economic-financial capacity and, consequently, of the ratios established by the CNMC.

Additionally, the Draft Circular does not adequately incentivise or clarify the criteria for extending the operation of those facilities that have exceeded their useful life. For investments in renovation and improvement work carried out on facilities that have exceeded, or are close to exceeding their useful life, it is established that they should be planned. Notwithstanding the foregoing, the Draft Circular additionally requires that the CNMC be requested to take into consideration investments in renovation and improvement, providing a detailed economic analysis thereof that justifies the annual investment and remuneration savings for the system that such actions entail compared to the construction of a new facility, as a prerequisite for them to be authorised. That is, new requirements for the authorisation of facilities are introduced, beyond the approval of the Planning document by the Government, after being submitted to the House of Commons (*Congreso de los Diputados*) and the analysis and justification that the Planning already contains for each of the actions included.

This mechanism, confusing in its wording and apparently not very agile, introduces uncertainty, as the transmission agent will not be sure whether these investments will be recognised until after they have been made.

Renovation is one of the two measures that the CNMC includes in the article that aims to establish the management process associated to extending the useful life of the facilities of the transmission grid that reach the end of their useful life, although, in Red Eléctrica's opinion it does not comply with the energy policy guideline related to incentivising the extension of the operation of these facilities, avoiding the need to replace them at a higher cost.

The second of the measures included in the Draft Circular to be applied to facilities that end their useful life is the term of 'remuneration for the extension of useful life' (*REVU* – which is the Spanish acronym for *Remuneración por Extension de Vida Útil*), which is exactly the same term as the one contemplated in Royal Decree 1047/2013 and consists of an increase in the remuneration for operation and maintenance (starting with a percentage of 15% during the first 5 years and then increases year by year by 1%, 2% or 3% as appropriate).

This remuneration, conceptually, simply returns the additional maintenance cost incurred by the transmission agent for maintaining in service facilities that have reached the end of their useful life, provided that the percentages actually reflect the extra cost incurred.

A concept that simply serves as consideration for the costs incurred cannot be considered as an incentive and therefore does not respond to the energy policy guidelines when it states that "the remuneration methodology should incentivise extending the operation of those facilities that have exceeded their remunerated useful life, in order to contribute to an optimal management of national resources and under the principle of optimising the return on investment for consumers and keeping assets that are already built and depreciated in appropriate operating conditions, avoiding the need to replace them at a higher cost."

Additionally, there is a new discrimination in the quantification of the value associated with this term, given that in other regulated activities the percentage established by the CNMC starts at 30%.

In short, the measures contemplated by the CNMC in the Draft Circular, by not establishing a real incentive to keep the facilities in service, may result in a real and gradual deterioration of the facilities necessary to guarantee the continuity of the supply and the integration of renewable energy required by the Energy Transition.

Faced with a problem of this magnitude, which affects a significant percentage of the transmission grid in service today, requires solutions that truly respond to this problem and incentivise the extension of its effective useful life beyond its remunerated useful life.

The aforementioned measures, together with the rest of the impacts of other measures included in the Draft Circular, will result in a decrease in the Company's profitability levels and, potentially, could hinder the fulfilment of the CNMC ratios, mentioned in the previous section, as of 2023. This situation would not, in turn, comply with the energy policy guideline consisting of the principle of financial prudence that should govern the remuneration methodology as the proposed measures make it difficult to comply with the aforementioned ratios.

2.1.4. Operation and Maintenance

The Draft Circular and its associated Report 'anticipate a significant reduction' in the of operation and maintenance (O&M) unit values and consequently of the transmission agent's revenue for this concept. This reduction was verified once the CNMC published the Draft Circular on 25 July approving the standard facilities and unit values of the transmission activity. Similarly, the Draft Circular does not incentivise efficiency improvements, which in the medium term will harm both the system and consumers.

Just as the unit values of investment are a reference of the average construction costs, those of O&M are a reference of the average cost of maintaining a facility throughout its useful life. An activity with a high cyclical component would advise carrying out an analysis of the costs of the O&M activity taking the broadest possible multi-year period as a reference, so that all the sets of actions that are going to be carried out during the life of the facility are taken into account.

In addition to the above, this revision of the unit values that are being proposed based on the historical cost incurred at a given time (a two year period), completely neglects the context that the transmission agent will face in the next period, during which the massive integration of renewable energy 'will deplete' for example, among other factors, the capacity of suppliers, with the consequent upward pressure on the prices of materials and services.

In an activity such as operation and maintenance that, as indicated above, has a high cyclical component, it would seem a methodological error to consider an observation period of only two years to carry out a review of the costs associated to such activity. It would seem reasonable to wait for the end of the next regulatory period to have in 2025 at least an 8-year cost period (2016-2023), to draw conclusions about the validity of the current unit values that have only been in force since 2016.

The proposals that will be made not only in the Comments to the wording of the articles of the present Circular but also those that will be made to the Draft Circular approving the standard facilities and the unit values of the transmission activity, will try to 'counteract' these issues.

Finally, the Draft Circular does not explicitly recognise any incentive factors linked to the incorporation of new technologies and innovation in the maintenance activity, unlike what happens in other activities, which incorporate concepts in this regard.

2.1.5. Incentive for Grid Availability

The Draft Circular maintains the same methodological basis for the economic incentive for grid availability set out in Royal Decree 1047/2013. The methodology consists of comparing the availability of each year with the average availability of the 3 previous years (to which the quantity of 0.5 was subtracted) and with an 'availability target'. However, the Draft Circular modifies the incentive, increasing the availability target from 98.5% to 99% (above the value established by Royal Decree 1955/2000), and eliminating the reduction of 0.5 of the average availability of the previous 3 years, resulting in a significant reduction in the economic value of the incentive

This mechanism is conceptually unfair, as obtaining good availability rates in a given year penalises future incentives, resulting in a financially inefficient relationship between the cost overrun associated with achieving these rates and the low economic incentive or even the penalisation it may entail.

The incentive value will fluctuate depending on the volume of maintenance actions and of faults/breakdowns, but it will also be affected by the volume of investment in new facilities to be incorporated into the grid, as well as by the volume of renovation work to be carried out. As a result of the Energy Transition, which will entail the need to integrate new renewable generation, these last two aspects will have a significant impact on grid availability in the coming years.

The impact of the change in this parameter is estimated in the Report on the Draft Circular, reducing the annual incentive estimate from 8 to 2 million euros. This means reducing the weight of the incentive in the remuneration, which will only assume 0.1% of the total remuneration compared to the value of 0.5% which it previously stood at.

It seems clear that neither before (nor now) the mechanism was (nor is) incentive in nature at all, and in practice, seeing its quantification of the value associated with it, it means leaving the activity without incentives.

2.1.6. Remuneration adjustment for the use of regulated assets and resources in other activities

The Draft Circular contemplates a reduction in the remuneration for the use of assets and resources financed by the transmission activity in activities other than that of electricity transmission. The measure is based on a premise that is considered erroneous because the electricity system does not finance any assets, it simply remunerates the service provided by transmission assets through its capital cost, its depreciation and its operation and maintenance.

This new adjustment is not conceptually designed as an instrument to prevent the existence of so-called cross-subsidies between activities, as advocated by both national and European regulations.

Additionally, the measure disincentivises that regulated companies carry out other activities that in addition to the economic benefit that they generate for the company can result in benefits for society.

2.2. Summary of the main proposals that Red Eléctrica will make as transmission agent

As a follow-up to the comments just made in the previous section, the main lines of the proposals contained in the specific Comments are listed below:

2.2.1. Solving the problem of assets that reach the end of their useful life.

The Draft Circular introduces two measures, one consisting of enabling the renovation of facilities and the other, which was already included in the remuneration model currently in force, consisting of assigning a remuneration to the facilities that end their useful life through an increase in the remuneration for operation and maintenance.

In the opinion of Red Eléctrica, these two measures do not respond in any case to the MITECO guidelines as renovation, from a conceptual perspective, is not an incentive to extend the operation of these facilities but a way to make investments in them gradually, and remuneration for extending the useful life consisting of an increase in the remuneration for operation and maintenance, conceptually, it simply comes to return the additional cost of maintenance incurred by the transmission agent for maintaining in service facilities that have reached the end of their useful life, provided that percentages will really reflect the extra cost incurred. Therefore, none of the measures can be considered an incentive.

For this reason, the proposal of Red Eléctrica to try to solve this issue focuses on three measures:

- Apply the gradual adoption and implementation process established by the energy policy guidelines, so that, in the absence of solutions that incentivise the lengthening of the life span of facilities that reach the end of their useful life, their remuneration does not decrease to 'zero' in a single year and that the reduction occurs in a gradual way.

  This proposal is similar to that used by the CNMC itself for the gas transmission activity, establishing a gradual period of four years to space out the impact of the fall in the remuneration of facilities that reach the end of their useful life, a period that begins in the year following the last one in which these facilities have reached the end of their remunerated life.

  In the case of electricity transmission, the application of the proposed measure would cover a period of four years extending it to the third regulatory period, which is necessary to gradually absorb, as established by the MITECO energy policy guidelines, the effect of the disappearance of these assets from the remuneration base.

  This temporary measure, which is projected for the third regulatory period, does not compromise the global methodology of remuneration for the transmission of electricity defined in the Draft Circular which, following the principle of legal certainty established by the Law 39/2015, of 1 October, of the Common Administrative Procedure of Public Administrations, should have a focus of continuity beyond the next regulatory period.

  Additionally, and to provide a true incentive to keep facilities in service beyond their useful life, it is proposed that the last annuity of the period in which the gradual adoption and implementation process is applied be kept constant, provided that the facilities continue to provide service and have not undergone replacement or renovation.

  The introduction of this gradual process mechanism would also allow compliance with the principle of financial prudence contemplated in the energy policy guidelines.

- Implement mechanisms to provide the necessary agility to renovate facilities so that they can be operational. Ensuring that the renovation is bound by both its inclusion in a Planning document (with the lengthy deadlines that this process entails) and to the subsequent request and approval by the CNMC makes the mechanism proposed by the Circular unpredictable a priori and tremendously slow.

- Adjust the value of the term 'remuneration for the extension of useful life' ('REVU'). The term proposed by the CNMC is exactly the same as that contemplated in Royal Decree 1047/2013, which was set without any methodological basis. The remuneration for extending the useful life is calculated using the remuneration for operation and maintenance multiplied by a coefficient that takes the value 1.15 (15%) during the first five years in which the regulatory life has been exceeded.

In this case, there is discrimination in the quantification of the value associated with this term with regard to other regulated activities, in which the coefficient takes the value of 30% during the first five years in which the useful life has been exceeded and, as in transmission, it increases as of the fifth year in a phased and progressive manner.

Therefore, it is proposed to consider this remuneration term independent of the operation and maintenance remuneration and increase it, so that, in no case, it is set below the value established for other activities.

2.2.2. Operation and Maintenance revenues

In section 2 of article 8 of the Draft Circular, the remuneration for operation and maintenance introduces a factor that aims to share, among the transmission companies and the system, the margin between the remuneration for operation and maintenance calculated according to reference unit values of the preceding regulatory period and those in force in the new regulatory period.

The "α" parameter is used to distribute the margin, which, according to section 1 of the second additional provision of the Draft Circular, will take the value 0.2 for the period 2020-2025.

The proposals put forth by Red Eléctrica are the following:

- Regarding the information to be taken into account to establish the operation and maintenance costs in the next regulatory period, as previously mentioned in order to calculate the new unit values a multi-year period should be taken as a reference and not just two fiscal years (2016 and 2017) as mentioned in the Report that accompanies the Draft Circular approving the standard facilities and the reference operation and maintenance unit values for the transmission activity, sent and communicated by the CNMC on 25 July.

  Additionally, it should also be noted that in recent years, Red Eléctrica has solely carried the cost associated with significant incidents that affected the transmission grid. The great effort made in the restoration of the service of the facilities impacted, has meant a lower recurrent scheduled maintenance on other facilities of the transmission grid, generating higher maintenance costs.

  Furthermore, the significant renovation and improvement work carried out on in-service assets acquired prior to 1998, included in the REPEX 2015-2018 Plan - considered as an investment - has resulted in the fact that these assets have not since then required maintenance, therefore actually resulting in a lower maintenance cost.

  Therefore, the nature of the characteristics of the operation and maintenance actions performed, many of which do not have an annual periodicity, together with the incidents and the renovation and improvement works mentioned above, would advise the use of the aforementioned multi-year period for the establishment of the new unit values, in order to truly reflect the true evolution of the average cost of the unit values associated with operation and maintenance activities.

  It would seem reasonable that, in addition to establishing broad observation periods, and since only three complete years of application of the current unit values have elapsed (of which the CNMC has only information that has been analysed for two of them, 2016 and 2017), the current values for the new 2020-2025 regulatory period be extended, proposing that they be revised for the next regulatory period, at which time sufficient verified information will be available to carry out said revision.

- Notwithstanding the foregoing, if the CNMC should finally decide to carry out the revision of the unit values, it would be necessary to correct the proposed "α" parameter.

  In relation to said "α" parameter, the proposed value of 0.2 to be used for sharing the margin among the transmission companies and the consumer implies that 80% of the efficiency gained by the transmission agent is transferred to the consumer while the former only retains 20% of said efficiency. This asymmetric distribution included in the Draft Circular translates into the absence of incentives to maintain an on-going improvement policy, which allows the introduction of efficiency measures, thereby being detrimental to the consumers in the following regulatory periods.

In addition, the proposed asymmetric distribution of the margin between the system and the transmission agent regarding the operation and maintenance activity is not consistent with the 50/50 distribution of the margin between the system and transmission agent that is used for the construction activity.

Establishing a symmetrical sharing of the efficiencies between the transmission agent and the consumers encourages the transmission agent to carry out its activities at the lowest possible cost. Setting this sharing percentage at 20% disincentives the transmission agent, who observes that practically all its efforts regarding efficiency are transferred asymmetrically to the consumer, which in the long run will entail a greater cost for the latter.

Therefore, as is the case in other countries around us, it is proposed to increase the percentage of the margin established by the Draft Circular as an efficiency factor from 20% to 50%, whereby the "α" parameter should take a value of 0.5.

Additionally, in application of the gradual adoption and implementation process required by the energy policy guidelines so that the remuneration methodologies do not generate sudden impacts on the remuneration of regulated activities, it will be proposed that this 50/50 efficiency distribution be achieved over the next regulatory period. As already previously mentioned, the non-consideration of a gradual adoption and implementation mechanism would additionally bring with it not complying with the principle of financial prudence.

2.2.3. Remuneration adjustment for the use of regulated assets and resources in other activities

Red Eléctrica understands that the approach proposed by the Circular to make the adjustment based on 'revenue' (article 18) or 'profits' (article 19) is unwise. In the case an adjustment is to be considered, this should be based on the cost that has been supported by the electricity transmission activity due to the installation of surplus fibre optic capacity in its facilities. In addition, said approach does not take into account those other activities, resources or assets (other than those that are regulated) that have contributed to obtaining the benefits, nor the risks that the Company has assumed in carrying out such activities and that are inherent to the overall benefit obtained .

Therefore, it is proposed that the adjustment established under the terms provided for in articles 18 and 19 of the Draft Circular be eliminated.

2.2.4. Other proposals

As mentioned above, the deferral in the accrual and collection of the transmission remuneration should not be considered in the new remuneration period. The current 'n + 2' criteria has ceased to make sense and has ceased to have legal support.

In this regard, RDL 1/2019 amended section 14.8 of the LSE (Spanish Power Sector Law) by eliminating the three principles that said law established in relation to the remuneration of transmission and distribution activity, including the principle regarding remuneration in the year 'n + 2'. As a result, said principle has disappeared completely from the LSE and, what's more, it is not included either in the Energy Policy Guidelines for the drafting of the Circular on the Methodology for the Remuneration of Electricity Transmission.

Therefore, it is proposed that the remuneration of the transmission activity begin to be received from the moment the facilities are commissioned or, where appropriate, from the regulatory acknowledgement thereof. In this way, the same treatment and considerations contemplated in the regulation for gas transmission and distribution facilities would also be guaranteed for electricity transmission facilities.

In relation to the gradual adoption and implementation mechanism that the previous remuneration methodology incorporated regarding the Financial Rate of Return (variation between two consecutive years shall not be greater than 50 basis points), it will be proposed that it continue to be maintained, as this measure in addition to allowing changes to be gradual in order to transition between regulatory periods and therefore be aligned with the MITECO guidelines, it serves to protect both the consumer, in the cases the Financial Rate of Return increases, as well as the transmission agent in the cases it decreases.