BEFORE THE COMPETITION AND MARKETS AUTHORITY
IN THE MATTER OF AN APPEAL UNDER SECTION 173 ENERGY ACT 2004

B E T W E E N:

(1) SSE GENERATION LIMITED

(2) THE ENTITIES LISTED IN SCHEDULE 1 TO THE NOTICE OF APPEAL

Appellants

-and-

THE GAS AND ELECTRICITY MARKETS AUTHORITY

Respondent

SUMMARY OF RESPONDENT'S REPLY TO NOTICE OF APPEAL

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1. The Respondent, the Gas and Electricity Markets Authority (**"GEMA"**), is the gas and electricity markets regulator for Great Britain (**"GB"**). The Appellants are generators of electricity, who have appealed to the Competition and Markets Authority (**"the CMA"**) against two related decisions of GEMA, both dated 17 December 2020 (**"the Decisions"**). The effect of the Decisions was, in broad terms, to approve a proposal to modify the contractual framework which governs charging for electricity transmission in GB. In so doing, GEMA rejected various other modification proposals, including some put forward by representatives of the Appellants.

2. The Decisions relate to the mechanism, known as the **"CUSC Calculation"** which is intended to secure compliance with a legal requirement that *"annual average transmission charges"* paid by generators in GB fall within a range between €0/MWh and €2.50/MWh (the **"Permitted Range"**). This requirement was laid down by Commission Regulation (EU) 838/2010 (**"the ITC Regulation"**), which continues to apply in GB pursuant to s.3 of the European Union (Withdrawal) Act 2018, subject to amendments which are not material. The ITC Regulation stipulates that, for the purposes of calculating *"annual average transmission charges"*, no account is to be taken of *"charges paid by producers for physical assets required for connection to the system or the upgrade of the connection"* (the **"Connection Exclusion"**) and *"charges paid by producers related to ancillary services"* (the **"Ancillary Services Exclusion"**).

3. There are four key elements of context to this appeal:

3.1. First, many of the same Appellants appealed to the CMA in 2017 against a previous decision of GEMA relating to the ITC Regulation. The CMA dismissed that appeal in February 2018, and in so doing held that (as GEMA had concluded) the CUSC Calculation is based on an erroneous interpretation of the Connection Exclusion. This gives rise to a risk that the CUSC Calculation may not be effective in securing compliance with the Permitted Range. Under the *status quo*, the risk of a breach of the Permitted Range is high.

3.2. Second, the procedure by which the relevant domestic GB charging rules may be amended involves proposals being developed by industry representatives, and submitted to GEMA for consideration. GEMA can approve one of the proposals submitted, reject them all, or send them back for further consideration. GEMA cannot, however, simply impose a proposal of its own devising.

3.3. Third, the transmission charging arrangements currently applicable in GB include a flat negative charge, known as the *"Transmission Generation Residual"* (**"the TGR"**). The TGR is received by some, but not all, generators, and thus tends to distort competition. GEMA concluded in 2019 (i) that the TGR should therefore be removed, subject to a mechanism to adjust charges insofar as necessary to avoid a breach of the Permitted Range; and (ii) that this change should be implemented in April 2021. Neither the Appellants nor anyone else challenged that decision, which is known as the **"TCR Decision"**.

3.4. Fourth, the Decisions concern proposals formulated by industry with a view (at least ostensibly) to (i) giving effect to GEMA's decision that the TGR should be removed; and (ii) amending the CUSC Calculation so that it is no longer based on an erroneous interpretation of the ITC Regulation. The Appellants challenge GEMA's decision to approve one of the proposals that was submitted to it, rather than the proposals that they would have preferred to see implemented.

4. GEMA concluded that none of the proposals submitted to it are based on a correct interpretation of the ITC Regulation, but that the proposal approved would give rise to only a low risk of a breach of the Permitted Range, at least in the next few years. GEMA therefore concluded that the best course of action was (i) to approve the proposal, rather than allow the *status quo* to remain in place, with its associated high risk of breach of the

Permitted Range; and (ii) to indicate that further proposals should be formulated, with a view to reflecting the correct interpretation of the ITC Regulation in the CUSC Calculation from 2022 onwards.

5. The Appellants challenge the Decisions on six grounds:

   5.1. First, the Appellants allege that GEMA erred in its interpretation of the Connection Exclusion. Much of this argument is directed towards showing that the proposal that GEMA approved does not correctly reflect the Connection Exclusion. The Appellants thereby erect and attack a straw man, since GEMA expressly concluded that all of the options presented to it were based on erroneous interpretations of the Connection Exclusion. The Appellants fail to show any error in GEMA's interpretation, and ignore conclusions that the CMA reached in 2018.

   5.2. Second, the Appellants allege that GEMA breached various *"public law principles"* by approving a proposal which did not reflect the correct interpretation of the Connection Exclusion. This argument is wrong, since GEMA's choices were limited to the options presented to it, none of which reflect the correct interpretation of the Connection Exclusion. GEMA selected the best of the imperfect options available, and did not commit any public law error in so doing.

   5.3. Third, the Appellants allege that GEMA erred in its interpretation of the Ancillary Services Exclusion. This argument is hopeless, not least since the provisions of EU law on which it rests (which do not appear in the ITC Regulation itself) have been materially amended in GB with effect from the end of the Transition Period. The Appellants simply ignore the most important of these amendments.

   5.4. Fourth, the Appellants allege that GEMA underestimated the detriment to generators associated with the Decisions, and overestimated the benefit to consumers. These arguments are wrong, and rest on (i) an assertion that GEMA has caused vast losses to generators, when what it has in fact done is fail to provide them with benefits that they had no reasonable grounds to expect; and (ii) unwarranted manipulations of forecasts of consumer benefits (e.g. disregarding two years' worth of benefits).

5.5. Fifth and sixth, the Appellants allege that GEMA was wrong to reject proposals which would, in effect, reintroduce the TGR by the back door and/or partially postpone its removal beyond April 2021. Such arguments amount to a collateral attack on the TCR Decision, which the Appellants did not challenge at the relevant time, and should be dismissed for that reason alone. To do otherwise would be contrary to principles of legal certainty, since market participants will have organised their affairs on the footing that time for any challenge to the TCR Decision has long ago expired. The Appellants' arguments in favour of the back-door reintroduction of the TGR and/or the partial postponement of its removal are in any event without merit, and demonstrate no error (still less any material error) in the Decisions.

6. For the reasons summarised above, and set out in more detail in the Decisions and the Reply to the Notice of Appeal, the appeal should be dismissed.

KASSIE SMITH QC
LIGIA OSEPCIU
GEORGE MOLYNEAUX

2 February 2021