



Informal translation produced by European Commission services:

SUBJECT: COMMUNICATION TO THE EUROPEAN COMMISSION ON DEROGATION FROM THE ELECTRICITY SECTOR RULES APPLICABLE TO NON-MAINLAND TERRITORIES FOR THE PURPOSES OF IMPLEMENTING DIRECTIVE (EU) 2019/944 AND REGULATION (EU) 2019/943 ON THE INTERNAL MARKET FOR ELECTRICITY

1. BACKGROUND

1.1. EU LEGAL FRAMEWORK

Regulation (EU) 2019/943 of the European Parliament and of the Council of 5 June 2019 on the internal market for electricity and Directive (EU) 2019/944 of the European Parliament and of the Council of 5 June 2019 on common rules for the internal market for electricity and amending Directive 2012/27/EU provide for the possibility of derogations from their application for small connected and small isolated electricity systems that meet the conditions laid down therein.

The following articles regulate the **possibility of a derogation** that would apply to the Spanish electricity system:

Regulation (EU) 2019/943:

'Article 64. Derogations

1. Member States may apply for derogations from the relevant provisions of Articles 3 and 6, Article 7(1), Article 8(1) and (4), Articles 9, 10 and 11, Articles 14 to 17, Articles 19 to 27, Articles 35 to 47 and Article 51 provided that:

(a) the Member State can demonstrate that there are substantial problems for the operation of small isolated systems and small connected systems;

(b) outermost regions within the meaning of Article 349 TFEU cannot be interconnected with the Union's energy market for evident physical reasons.

In the situation referred to in point (a) of the first subparagraph, the derogation shall be limited in time and shall subject to conditions aiming to increase competition and integration with the internal market for electricity.

In the situation referred to in point (b) of the first subparagraph, the derogation shall not be limited in time.



The Commission shall inform the Member States of those applications before adopting the decision, protecting the confidentiality of commercially sensitive information.

A derogation granted under this Article shall aim to ensure that it does not obstruct the transition towards renewable energy, increased flexibility, energy storage, electromobility and demand response.

In its decision granting a derogation the Commission shall set out to what extent the derogation is to take into account the application of the network codes and guidelines.

[...]

3. This Regulation shall not affect the application of the derogations granted under Article 66 of Directive (EU) 2019/944 [...].'

Directive (EU) 2019/944, in addition to the articles providing for derogations, contains a definition of the small connected and small isolated systems to which the derogations would apply, as well as applying to the outermost regions¹, if authorised by the European Commission:

'Article 2. Definitions

[...]

(42) "small isolated system" means any system that had consumption of less than 3 000 GWh in the year 1996, where less than 5 % of annual consumption is obtained through interconnection with other systems;

(43) "small connected system" means any system that had consumption of less than 3 000 GWh in the year 1996, where more than 5 % of annual consumption is obtained through interconnection with other systems;

Article 66. Derogations

1. Member States which can demonstrate that there are substantial problems for the operation of their small connected systems and small isolated systems, may

¹ There are nine outermost regions according to Article 349 TFEU: Guadeloupe, French Guiana, Martinique, Mayotte, Reunion Island and Saint-Martin (France), the Canary Islands (Spain), the Azores and Madeira (Portugal).



apply to the Commission for derogations from the relevant provisions of Articles 7 and 8 and of Chapters IV, V and VI.

Small isolated systems and France, for the purpose of Corsica, may also apply for a derogation from Articles 4, 5 and 6.

The Commission shall inform the Member States of such applications before taking a decision, taking into account respect for confidentiality.

2. Derogations granted by the Commission as referred to in paragraph 1 shall be limited in time and subject to conditions that aim to increase competition in and the integration of the internal market and to ensure that the derogations do not hamper the transition towards renewable energy, increased flexibility, energy storage, electromobility and demand response.

For outermost regions within the meaning of Article 349 TFEU, that cannot be interconnected with the Union electricity markets, the derogation shall not be limited in time and shall be subject to conditions aimed to ensure that the derogation does not hamper the transition towards renewable energy.

Decisions to grant derogations shall be published in the Official Journal of the European Union [...].'

1.2. SPANISH LEGAL FRAMEWORK

The current electricity sector legislation concerning non-mainland territories² (NMTs) is as follows:

Law 17/2013³ of 29 October 2013 on security of supply and increasing competition in electricity systems on islands and outside of mainland Spain brought about a comprehensive reform of the regulatory framework for these systems in order to reduce their vulnerability and ensure greater overall technical and economic efficiency, while at the same time improving security of supply. It establishes an administrative procedure which includes consultation with the regional administrations concerned and is based on technical criteria proposed by the system operator and economic criteria that strengthen efficiency signals. In order

² Activities on islands and outside of mainland Spain were previously regulated by: Law 54/1997 of 27 November 1997 on the electricity sector (mainly Article 12); Royal Decree 1747/2003 of 19 December 2003 regulating electricity systems on islands and outside of mainland Spain, which was implemented by Order ITC/913/2006 of 30 March 2006 and Order ITC/914/2006 of 30 March 2006. This framework was revised by Royal Decree-Law 13/2012 of 30 March 2012 and Royal Decree-Law 20/2012 of 13 July 2012, the principles of which were laid down in Law 17/2013 and Law 24/2013.

³ <https://www.boe.es/buscar/act.php?id=BOE-A-2013-11332>



to be entitled to the additional remuneration scheme for electricity generation in these territories, a 'resolution of compatibility' must first be obtained. This resolution declares that the installation is compatible with the technical criteria assessed by the system operator and with the economic criteria for an effective reduction of electricity supply costs.

Law 24/2013⁴ of 23 December 2013 on the electricity sector sets out in detail the principles established in the previous legislation. Article 10 of the Law allows electricity supply activities carried out in electricity systems in NMTs to be the subject of special regulations implementing the following mechanisms:

- a) the planning of electricity transmission network infrastructure;
- b) the establishment of a scheme to provide remuneration for electricity generation;
- c) the promotion of renewable energy where this is technically feasible and entails a reduction in system costs;
- d) the integration of NMT systems into the Spanish mainland market, where there is an interconnection with the mainland with sufficient commercial capacity;
- e) the establishment of economic incentives for the system operator to progressively reduce the cost of electricity generation in NMT systems while maintaining security;
- f) the incorporation of efficient price signals to consumers so that they can adjust their demand.

Article 14 of Law 24/2013 then sets out the specific principles for regulated remuneration of supply activities. Article 14(6) provides that the Government may establish additional remuneration to cover the difference between the costs of investing in and carrying out electricity generation activities in NMT electricity systems on the one hand, and the revenue earned from those generation activities on the other. The additional remuneration scheme is based on the following principles:

- a) only the extra costs specific to these electricity systems due to their location and, where applicable, their isolated nature are taken into account;

⁴ <https://www.boe.es/buscar/act.php?id=BOE-A-2013-13645>



b) the costs of investing in and carrying out energy generation are determined on the basis of the entire regulatory lifetime of a 'standard installation' [the theoretical model used to determine which remuneration criteria apply to a given installation, based on technology, age, capacity, etc.] managed by an efficient and well-run undertaking;

c) to allow for remuneration appropriate for a low-risk activity, the remuneration rate for recognised net investment is linked to the ten-year government bond yield on the secondary market, plus an appropriate spread.

In addition, Article 14 provides as follows:

a) Remuneration must be calculated on the basis of the costs required by an efficient and well-run undertaking to carry out the activity.

b) The additional financial scheme must allow for remuneration appropriate for a low-risk activity.

c) Remuneration for activities must be determined by issuing regulations using objective, transparent and non-discriminatory criteria.

d) Remuneration for activities must incentivise improvements to operational effectiveness, economic and technical efficiency of the activities and the quality of the electricity supply.

e) The remuneration parameters of the additional remuneration scheme must be determined taking into account the point in the economic cycle, electricity demand and an appropriate rate of return for these activities for regulatory periods lasting six years.

f) The remuneration parameters may be reviewed before the beginning of the regulatory period. This review may include an amendment to the remuneration rate applicable to those activities, which must be set in law.

Finally, Article 15 of the Law, concerning the network criteria and the operating criteria for generating installations subject to regulated remuneration, lays down additional criteria in order to safeguard the transfer to consumers of costs unrelated to electricity supply and the application of uniform criteria throughout the territory. The principles provided for in this article are thus summarised as follows:

a) The remuneration methodologies to be established must take into account only the costs arising from the application of the aforementioned criteria.



b) Best practices in transmission, distribution and generation, the quality indices established in national legislation and the environmental protection levels resulting from national and European legislation must all be taken into account.

c) Where the application of specific rules results in higher operating costs for undertakings holding network assets and electricity-generating installations subject to regulated remuneration, those undertakings may establish agreements or other mechanisms with the public authorities to cover the additional costs incurred. Under no circumstances may the additional costs caused by these rules be included as part of the investment or operating costs used to calculate the remuneration for these undertakings, and may not therefore be defrayed by electricity system income.

d) The Government must issue regulations laying down the conditions in which, exceptionally and on a temporary basis, authorisation may be given for additional costs charged against electricity system income and derived from fuel changes in NMT electricity-generating systems, which are not justified for technical reasons and which are essential to guarantee supply in those territories.

In application of the previous legal provisions, Royal Decree 738/2015⁵ of 31 July 2015 regulating the production and dispatching of electricity in the electrical systems of non-mainland territories sets out the additional remuneration scheme for electricity generation in NMT electricity systems. The remuneration received by installations under this scheme and participating in the production dispatch (a mechanism which replaces the market system used on the mainland) covers both the investment and recognised operating costs. This scheme⁶ is based on two remuneration components: one for the investment made and other fixed costs, and one for the variable costs incurred during operation.

As well as the additional remuneration scheme, Royal Decree 738/2015 of 31 July 2015 regulating the production and dispatching of electricity in the electrical systems of non-mainland territories also implements other provisions contained in Law 17/2013 of 29 October and Law 24/2013 of 26 December 2013. It regulates the procedure for obtaining from the Directorate-General for Energy Policy and Mines the 'favourable resolution of compatibility' provided for in Law 17/2013 of

⁵ <https://www.boe.es/buscar/act.php?id=BOE-A-2015-8646>

⁶ In its Decision of 28 May 2020, the European Commission (DG COMP) concluded that the compensation mechanism under Royal Decree 738/2015 fulfils the conditions of the 2012 SGEI Framework and is this compatible with the internal market pursuant to Article 106(2) TFEU. The Decision is available at:
https://ec.europa.eu/competition/state_aid/cases1/202028/266654_2172578_212_2.pdf



29 October 2013, which is a prerequisite for entitlement to the additional remuneration scheme.

It also regulates the economic and administrative framework for pumped-storage facilities owned by the system operator, which are necessary for the operation of the system and the integration of renewable energy sources.

The Royal Decree also provides for a dispatch based on variable costs in each of the isolated systems in NMTs. Generating installations, retailers and direct consumers all participate in the dispatch, either directly or through their representatives. Were the NMT systems to be integrated into the mainland market (the Balearic Islands being the only potential candidate), the regulations applicable to that market would apply to the owners of generating installations.

Finally, in accordance with Law 24/2013 on the electricity sector, the Royal Decree also provides for the establishment of an economic incentives scheme for the system operator, which is intended to progressively reduce generating costs in NMT systems and incorporate efficient price signals so that consumers can adjust their demand, all while maintaining security.

In addition to the aforementioned laws and royal decrees, the regulatory framework specific to NMTs is supplemented by the following implementing legislation:

- Ministerial Order/1158/2018⁷ of 29 October 2018 approving the additional remuneration scheme for existing electricity-generating installations in the non-mainland territories of Menorca, Gran Canaria and Tenerife that have to make additional investments as a result of compliance with regional or national legislation in order to continue operating.
- Ministerial Order/1172/2018⁸ of 5 November 2018 redefining isolated electricity systems in the non-mainland territory of the Balearic Islands and amending the methodology for calculating the demand purchase price and the sale price of electricity in the production dispatch of non-mainland territories.
- Ministerial Order/1260/2019 of 26 December 2019 laying down the technical and economic parameters to be used in calculating the remuneration for electricity generation activities in non-mainland territories

⁷ <https://www.boe.es/buscar/doc.php?id=BOE-A-2018-15080>

⁸ <https://www.boe.es/buscar/act.php?id=BOE-A-2018-15515>



with an additional remuneration scheme during the 2020-2025 regulatory period and revising other technical issues.⁹

- Ministerial Order TED/776/2020 of 4 August 2020 revising the product and logistics prices to be used in determining the price of fuel and setting a limit on the start-up time used for settlement calculations per 'standard installation' type, applicable to the generating installations located in non-mainland territories with an additional remuneration scheme¹⁰.
- Royal Decree 1623/2011 of 14 November 2011 regulating the effects of the entry into operation of the link between the mainland and Balearic electricity systems and amending other provisions in the electricity sector.

2. NON-MAINLAND TERRITORIES OF THE CANARY ISLANDS, THE BALEARIC ISLANDS, CEUTA AND MELILLA

2.1. APPLICATION OF THE DEFINITION OF SMALL ISOLATED AND SMALL CONNECTED SYSTEMS

The derogations provided for in both Directive (EU) 2019/944 and Regulation (EU) 2019/943 relate to the definitions of small isolated and small connected systems, which are based on system consumption in 1996. The non-mainland territories of the Canary Islands, the Balearic Islands, Ceuta and Melilla have undergone transformations since 1996 due to an increase in interconnections between isolated electricity systems. The most recent connection between systems was recognised by way of Ministerial Order/1172/2018 of 5 November 2018 redefining isolated electricity systems in the non-mainland territory of the Balearic Islands and amending the methodology for calculating the demand purchase price and the sale price of electricity in the production dispatch of non-mainland territories, which entered into force on 1 December 2018.

As a result of that Order, the NMTs of the Canary Islands, the Balearic Islands, Ceuta and Melilla are currently made up of the following isolated electrical systems:

⁹ https://www.boe.es/diario_boe/txt.php?id=BOE-A-2019-18620

¹⁰ https://www.boe.es/diario_boe/txt.php?id=BOE-A-2020-9339



Canarias	Illes Balears	Ceuta	Melilla
Gran Canaria.	Mallorca-Menorca-Ibiza-Formentera.	Ceuta.	Melilla.
Tenerife.			
Lanzarote-Fuerteventura.			
La Palma.			
La Gomera.			
El Hierro.			

For the purposes of applying the definitions of ‘small isolated systems’ and ‘small connected systems’, the electricity demand – measured at power station busbars – in the electricity systems in question in 1996 is set out in the following table (drawn up by Red Eléctrica de España, S.A.¹¹):

	1995	1996	Δ %
Mallorca	2.321,5	2.456,2	5,8
Menorca	285,7	292,4	2,3
Ibiza-Formentera	352,1	369,2	4,9
Islas Balears (*)	2.959,3	3.117,9	5,4
Gran Canaria	1.998,5	2.056,1	2,9
Tenerife	1.691,2	1.761,0	4,1
Fuerteventura	228,5	244,7	7,1
Lanzarote	386,7	419,3	8,4
La Palma	147,7	145,1	-1,8
Gomera	33,2	33,7	1,3
Hierro	16,6	17,6	5,9
Islas Canarias	4.502,4	4.677,4	3,9
Ceuta	92,1	99,7	8,2
Melilla	90,5	97,5	7,8
Ceuta y Melilla	182,6	197,2	8,0

As the table shows, in 1996, from a regulatory point of view, the Ibiza-Formentera system was the only interconnection between islands, and all electricity systems had a demand of less than 3 000 GWh.

¹¹ <https://www.ree.es/sites/default/files/downloadable/inf96.pdf>



As regards consumption through interconnections with other systems, the interconnector linking the island of Mallorca with the mainland electricity system currently covers approximately 25% of demand in the current Mallorca-Menorca-Ibiza-Formentera system, defined as such by Ministerial Order/1172/2018 of 5 November 2018.

In accordance with the definitions in Article 2 of Directive (EU) 2019/944, the electricity systems of the Canary Islands, Ceuta and Melilla meet the requirements to be defined as small isolated systems, while the electricity systems of the Balearic Islands would meet the definition of a small connected system, meaning that derogations under both Directive (EU) 2019/944 and Regulation (EU) 2019/943 may be requested under different conditions in accordance with those texts.

2.2. OUTERMOST REGIONS

The Canary Islands are one of the outermost regions recognised under Article 349 of the Treaty on the Functioning of the European Union (TFEU). Each of the Canary Islands' isolated electricity systems would therefore fall into this category for the purposes of implementing the provisions of the Electricity Directive and Electricity Regulation in question.

2.3. SPECIFIC SITUATION OF NON-MAINLAND TERRITORIES

The electricity systems in NMTs have a number of unique characteristics that affect the economic framework for the supply of electricity:

- small market size, preventing the economies of scale that are achieved in systems with higher 'critical mass' such as the mainland system;
- isolated systems, resulting in a greater need for installed reserve capacity;
- higher costs associated with the fuel mix, resulting in higher electricity generation costs.

These distinctive features mean that these systems differ from the mainland's electricity system, entailing higher production costs than on the mainland, and must therefore be treated differently in practice. Furthermore, due to the historical development of these territories, with a single business group traditionally performing all energy supply functions, there is no effective competition in these territories.



In order to solve the problems associated with a lack of competition and high costs (and a lack of incentive to reduce costs), the sector has been undergoing a vertical disintegration process, and competition has been introduced into activities where feasible. New incentive-based remuneration schemes have also been introduced for those activities that continue to be regulated. A range of measures has been taken to reduce the risks associated with these systems, rationalise certain cost items and introduce economic incentives to encourage operational efficiency in the installations and reduce generating costs.

In conclusion, a market mechanism identical to the one in place on the mainland cannot be established in these territories, and it was therefore decided to exclude electricity generation in NMTs from the bidding system on the mainland market. Instead, these systems use a mechanism of economic precedence: a dispatch is established, in which the system operator ranks the generating plants in order of economic merit based on variable costs until demand is covered, taking into account the technical constraints and the reserves necessary to ensure supply.

Those on the demand side buy their energy at prices equivalent to those under the bidding system in place on the mainland.

Electricity generation in NMTs therefore constitutes a system of regulated remuneration instead of a market remuneration system and is applied in conditions where a wholesale market could not function and where costs, for geographical and territorial reasons, are higher than electricity generation costs in mainland Spain. The remuneration for this activity takes into account all the specific costs of electricity generation that could not be covered by the income obtained in those territories, including periodic reviews to adjust those costs.

2.3.1. Production dispatch

As stated above, in NMTs a dispatch system is in place, in which the system operator ranks the generating installations in order of economic merit. In general, generating units are divided into two categories, A and B, with the latter corresponding to non-dispatchable renewable energy installations. The dispatch carried out by the system operator takes account of the generating installations' variable costs, although an 'instrumental' price is assigned to category B installations to secure maximum generation from them in accordance with security criteria.

In these production dispatches, direct consumers and retailers notify the system operator of the hourly demand in each isolated system, and following the daily dispatch they purchase their energy at a price equivalent to that of the mainland.



In view of the increased generating costs to be expected in NMTs and the structure of isolated systems, an economic compatibility mechanism was put in place to ensure that prices equivalent to those resulting from the bidding system in place on the mainland are maintained and to prevent discrimination against consumers and retailers without undermining the energy efficiency and the economic efficiency of each system. In addition, direct consumers and retailers have to pay for any deviations between the electricity actually purchased and the purchase forecast sent to the system operator for the purpose of the daily dispatch.

The mechanism itself ensures that the electricity system and the public budget cover the extra cost resulting from the difference between the higher generating costs in these systems (specified in the regulated remuneration scheme under Royal Decree 738/2015 of 31 July 2015, which covers the costs of an efficient and well-run undertaking with a rate of return corresponding to a low-risk activity) and the price equivalent to that on the mainland (paid by all consumers irrespective of the system in which they consume energy).

The functions of price publication, energy settlement and the guarantee scheme are also similar to those on the mainland.

Furthermore, in relation to the retail market, final electricity consumers have the right to choose their supplier on the same terms as mainland consumers. Similarly, the concept of vulnerable consumers, which is linked to certain social, consumption and purchasing power characteristics, is defined for the whole of Spain and, in general, supply is organised uniformly through the country. In this respect, there are no differences between the mainland and non-mainland retail markets.

2.3.2. Specific situation in the Balearic Islands

As regards the Balearic Islands' electricity system, it should be noted that, until 2012, this system was completely isolated from the mainland system.

As explained throughout this document, due to the physical obstacles described and the historical development of these territories, all energy generation functions have always been performed by a single business group.

So far, it has not been possible to fully integrate this system, despite the efforts made to increase competition in these systems, the connection of the Mallorca-Menorca electricity system to the mainland and the increase in the number of connections between the islands in the system.



The cable connecting the Mallorca-Menorca electricity system (now the Mallorca-Menorca-Ibiza-Formentera system) to the mainland has been in operation since the end of 2012, and covers approximately 25% of the system's electricity demand. This energy is remunerated and purchased at the marginal price of the mainland production market.

Royal Decree 738/2015 of 31 July 2015 provides that isolated electricity systems will no longer be considered as such when they are effectively integrated with the mainland system, i.e. when the capacity of their connection with the mainland is such that they can enter the mainland production market and there are market mechanisms in place to integrate their electricity. This must be established by order of the Minister for Ecological Transition and the Demographic Challenge (as this portfolio is now known), following a report from the system operator and the market operator.

There is therefore a clear desire to integrate this system with the mainland, although under the current circumstances it is not yet possible to integrate it into the Iberian Electricity Market (MIBEL) given the systematic difference in prices resulting from the gap between the generating costs in the Balearic system and the mainland system for the reasons described in detail above, and also because the cable does not have the capacity to fully meet demand. The low level of competition in this system would also make it more difficult to establish a market mechanism to solve the technical restrictions resulting from the demand not covered by the MIBEL.

In view of the above, until it can be declared that this isolated electricity system has been effectively integrated, completing the process which is currently under way, it should be treated in the same way as the other isolated electrical systems.

With regard to this electricity system, the 2015-2020 electricity transmission network plan, which was approved in October 2015, included two new links between the stations on Mallorca and Ibiza. Their implementation represented further progress in integrating the two existing isolated electricity systems (Mallorca-Menorca and Ibiza-Formentera), creating a single system to increase the quality and security of supply for these islands, which have now been operating as a single system since December 2018. Subsequent changes to the plan included various measures to enable, among other things, power generated from renewable sources to be fed out across the islands.



In addition, the publication on 1 March 2019 of Ministerial Order/212/2019 of 25 February 2019 began the process of preparing the 2021-2026 electricity transmission network plan, which provides for a second link with the mainland.

Furthermore, as part of the drive to increase the amount of electricity generated from renewable sources in this system, in 2018 the terms and conditions for granting aid – cofinanced by ERDF funds – for investment in non-mainland installations generating electricity from wind and photovoltaic energy were approved by Ministerial Order/1380/2018 of 20 December 2018. A first call for applications for aid for investment in photovoltaic installations in the Balearic Islands was issued by a Resolution of the Directorate-General of the Institute for Energy Diversification and Saving of 27 March 2019.

In the context of the objective of increasing the deployment of electricity generation from renewable sources, the measures set out in the Integrated National Energy and Climate Plan (2021-2030) should also be highlighted, both at national level and for the islands in particular, and Law 10/2019 of 22 February 2019 of the Balearic Islands on climate change and energy transition, which contains specific targets for deploying renewable energy sources and cutting electricity generation from fossil fuels.

2.3.3. Operation of the mainland-Mallorca cable

The operation of the exchange of electricity via the link between the Balearic electricity system and the mainland system and the settlement of energy are detailed in Royal Decree 1623/2011 of 14 November 2011 regulating the effects of the entry into operation of the link between the mainland and Balearic electricity systems and amending other provisions in the electricity sector, and its implementing legislation. Article 4 of the Royal Decree provides that ‘the system operator shall determine the maximum hourly energy value that can be scheduled through the link between the Balearic and mainland electricity systems while ensuring compliance with the security and reliability criteria laid down in the legislation in force’.

For each hour of each day, and for the daily scheduling and real time adjustments to the daily scheduling, the system operator calculates the maximum energy capacity that can be transported via the link from the mainland to Mallorca in accordance with the security criteria laid down in the legislation. When doing so, it takes into account the expected demand scenario, the availability of generation capacity and of the transmission system, which could affect the link, and the technical constraints required by the link itself in order to operate.



Once the maximum hourly capacity in the link has been calculated for the following day, blocks of bids are obtained, which are to be sent to the mainland market after the first economic dispatch, which does not take the link into account. These bids are sent in decreasing order of price until the maximum capacity that can be scheduled is reached. The bids are then presented on the mainland market via the 'reference retailers', which are the retailers required to offer certain reduced tariffs. Following matching on the daily market, the energy matched on the mainland market is transferred to the generators in a second economic dispatch in decreasing order of price up to the maximum value of the energy matched in each hour.

After the mainland daily market, any necessary modifications to the capacity value must be made in the same way via the various intraday market sessions.

At all times, therefore, the use of the link between the mainland and Mallorca is being maximised economically speaking, while respecting security criteria and guaranteeing the quality and security of electricity supply in the Balearic Islands with the help of the mainland's generating capacity.

2.4. STORAGE FACILITIES

Law 17/2013 of 29 October 2013 provides that storage facilities in NMTs whose main purposes are to guarantee supply, ensure system security and integrate non-dispatchable renewable energy sources must be owned by the system operator.

Hydraulic pumped-storage facilities have proved essential to providing electrical systems with a rapid and safe response capacity and ensuring they can operate properly. This is particularly necessary in small and isolated systems, such as electricity systems in the NMTs.

The incorporation of pumped-storage facilities into these systems will encourage the penetration of non-dispatchable renewable energy sources, which have a very positive environmental impact and also lead to cost reductions in these systems.

For this reason, a mechanism is required so that, if private initiatives do not meet these needs, ownership of new pumped-storage facilities can exceptionally be assigned to the system operator so that security of supply, system security and the integration of non-dispatchable renewable energy sources are not compromised.

The economic and administrative framework for the pumped-storage facilities owned by the system operator and the procedure for assignment of ownership



where these facilities are necessary for the operation of the system and the integration of renewable energy sources are set out in Royal Decree 738/2015 of 31 July 2015.

In this procedure, the needs for long-term coverage of demand are analysed, technical assessments are carried out on the needs of new generating installations and different renewable energy deployment scenarios are drawn up. This analysis examines the existing need for thermal capacity and, where appropriate, for pumped storage. The need to install pumped-storage facilities owned by the system operator has to be declared by the Council of Ministers.

Plans for a 200 MW pumped-storage hydropower plant at Chira-Soria in Gran Canaria, owned by the system operator, are currently going through the authorisation process, as set out in the aforementioned Law 17/2013 of 29 October 2013.

All pumped-storage facilities, regardless of ownership, must participate in the dispatch, although the pumped-storage facilities owned by the system operator are to be integrated as an ancillary service to ensure supply and security for each system. The operating criteria for integrating these facilities into the ancillary services have to be established by ministerial order.

2.5. MAIN DIFFERENCES COMPARED WITH MAINLAND REGULATION

From the above, it is clear that the main differences between the activities carried out in NMTs and those carried out by undertakings located on the mainland are as follows:

- Generation: there are significant differences, as a market cannot be established and the systems are not integrated with the mainland system.
- Retail: this activity is liberalised and the regulation is similar to that of the mainland.
- System operation: in these systems, given the absence of a market, the operator carries out a production dispatch based on technical and economic criteria. It should be noted that on the island of Gran Canaria, the system operator is currently developing a pumped-storage facility in order to increase security of supply and integrate more renewable power.
- Transmission and distribution: regulation is similar to that of the mainland.

3. REQUEST FOR DEROGATIONS UNDER DIRECTIVE (EU) 2019/944 AND REGULATION (EU) 2019/943 IN THE NON-MAINLAND TERRITORIES OF THE CANARY ISLANDS, THE BALEARIC ISLANDS, CEUTA AND MELILLA



In light of the above, and of Article 66 of Directive (EU) 2019/944 and Article 64 of Regulation (EU) 2019/943, derogations from the application of the following Articles are hereby requested for the Canary Islands, as an outermost region, for Ceuta and Melilla, as small isolated systems, and for the Balearic Islands, as a small connected system pending full integration with the mainland system:

3.1. DIRECTIVE (EU) 2019/944:

1. Articles 4, 5 and 6: Free choice of supplier, market-based supply prices and third-party access

The Directive provides for a derogation from these Articles for small isolated systems.

As indicated above, the electricity sector has been undergoing a vertical disintegration process and competition has been introduced to activities where this is feasible, such as supply activities. There is therefore a free choice of supplier in these territories, as on the mainland.

Furthermore, in order to avoid discrimination against consumers and retailers, the prices applicable in these territories are equivalent to those resulting from the bidding system in place on the mainland.

Finally, third-party access to the transmission and distribution systems is provided under the same conditions as on the mainland market.

In view of the above, it is not deemed necessary to request a derogation from these Articles for the Canary Islands, Ceuta and Melilla, while the Balearic Islands cannot be granted a derogation as that system is defined as a small connected system.

2. Article 7: Direct lines

The direct line arrangements are currently the same for the entire Spanish electricity system, and it is therefore not deemed necessary to request a derogation from this Article.

3. Article 8: Authorisation procedure for new capacity



The administrative authorisation procedure for new generating installations follows requirements similar to those of the mainland system, with each autonomous community or autonomous city responsible for determining its own administrative procedure until the isolated electricity systems are fully integrated into the mainland electricity system.

For its part, access to the economic scheme associated with new capacity installed in these territories is granted in different ways for category A and category B installations, but is always granted in a transparent manner and is open to any operator wishing to invest in these systems.

The economic scheme for new non-dispatchable renewable capacity is granted in accordance with procedures similar to those in place on the mainland, but with specific parameters reflecting the size and isolated nature of the system.

The current framework for category A installations establishes competitive tendering mechanisms either to cover a capacity deficit in the long term or to reduce the costs of the electricity system. This competitive tendering mechanism to cover capacity requirements involves both new installations and existing installations that wish to extend their operational life with or without further investment, thereby promoting the renewal of dispatchable generating capacity from a technical and economic point of view. The current regulation of these mechanisms encourages new players to participate as generators by placing restrictions on dominant players in the competition mechanisms. This is particularly relevant in systems such as the Balearic Islands, which is gradually becoming more interconnected with the mainland system.

However, as part of Spain's ongoing energy transition, it seems necessary that the islands play host to unique projects and act as a testing ground for energy transition technologies and policies that can then be exported to the mainland, as reflected in the Integrated National Energy and Climate Plan.

It is therefore deemed appropriate to request a derogation from this Article for the Canary Islands, the Balearic Islands, Ceuta and Melilla, both in order to maintain the current regulation encouraging the addition of new generators and to establish new capacity allocation mechanisms that could be unique to these territories.

4. Chapter IV, Articles 30 to 39: Distribution system operators



The rules governing the activities of distribution system operators are currently the same for the entire Spanish electricity system.

The new Directive contains new elements concerning management of losses and the possibility to develop system operation services and flexibility services, among other things.

The principles and functions for the performance of these tasks have to be the same throughout the Spanish electricity system, so it is generally not deemed necessary to request a derogation for these elements.

5. Chapter V, Articles 40 to 42: General rules applicable to transmission system operators

The tasks of the transmission system operator, the requirements placed on the operator and on transmission system owners and their powers with regard to the connection of new generating and storage installations are defined generally for the entire Spanish electricity system.

It is therefore not deemed necessary to request a derogation from these Articles for NMTs.

6. Chapter VI, Articles 43 to 56: Unbundling of transmission system operators

The model used to determine the transmission system operator in Spain is the same for the entire Spanish electricity system.

Nevertheless, Article 54 provides for the handling of storage facilities by transmission system operators, which may own these facilities if they are considered to be fully integrated network components or following a tendering procedure.

As stated above, hydraulic pumped-storage facilities in NMTs must be owned by the system operator if their main purposes are to guarantee supply, ensure system security and integrate non-dispatchable renewable energy sources. This ownership must be declared by the Council of Ministers, and the corresponding remuneration system will then be established by ministerial order for the entire lifetime of the pumped-storage facility.

Given that such ownership of these storage facilities arises from needs and circumstances that differ from those under Article 54, a derogation from



Article 54 is hereby requested for the non-mainland territories of the Canary Islands, the Balearic Islands, Ceuta and Melilla.

Specifically, this derogation would apply to the Chira-Soria pumped-storage facility in Gran Canaria, the plans for which are currently undergoing the authorisation process, and to future pumped-storage facilities owned by the system operator where this is justified as the best alternative in accordance with the legislation in force.

3.2. REGULATION (EU) 2019/943

As previously stated, in particular in section 2.3 of this document, electricity generation in NMTs is excluded from the mainland market's bidding system. Instead, a dispatch system is in place in which the system operator ranks the generating installations in order of economic merit based on variable costs until demand is met, taking into account technical constraints and the reserves necessary to guarantee supply.

However, the energy purchase price in the dispatch is equivalent to the price on the mainland market. Where possible, the dispatch operates in a similar way to the electricity markets, for example with the existence of daily and intra-day dispatches.

Nonetheless, general market rules, congestion management and resource adequacy, all laid down in Regulation (EU) 2019/943, cannot be applied to these production dispatches.

It should be noted, however, that the legislation in force in Spain that applies to these territories refers wherever possible to the rules for the mainland market, to which Regulation (EU) 2019/943 applies in full. This is the case for the probabilistic coverage assessments carried out for NMTs.

1. Chapter II, Articles 3, 6, 7(1), 8(1) and (4), 9, 10 and 11: General rules for the electricity market

As already stated, electricity generation in NMTs is governed by a dispatch system, in which the demand purchase price is based on the mainland price and not on the recognised costs incurred by generators in carrying out their generating activities, including regulation services.



The criteria for market price formation and balancing markets therefore cannot be adopted in NMTs.

With regard to Articles 7 and 8, due to their isolated nature, dispatches are operated independently of the mainland and European markets – aside from the reference price for the purchase of energy being based on the mainland price – with the dispatches being based on hourly schedules.

Likewise, in accordance with the above, the integration of forward markets, technical bidding limits and the value of lost load referred to in Article 9 to 11 do not apply to dispatches in NMTs.

2. Chapter III, Articles 14 to 17 and 19: Network access and congestion management

The system operator carries out a production dispatch in each of the non-mainland isolated electricity systems. These dispatches take into consideration the energy transferred via links between islands forming a single isolated system, such as Lanzarote and Fuerteventura, and also the energy transferred via the link with the mainland in the case of the Balearic electricity system.

In the event of congestion in these links, the system operator will reorganise the dispatch of the available generating capacity in order to ensure supply without affecting the energy purchase price in each NMT.

Articles 14 to 17 and 19 therefore do not apply.

3. Chapter IV, Articles 20 to 27: Resource adequacy

Given the above, the resource adequacy assessments carried out by the system operator for these territories are not integrated into the European resource adequacy assessment.

As indicated in reference to Article 8 of the Directive, there is a specific mechanism in these territories for allocating new capacity, which must be maintained given their unique nature.

Although the aforementioned Articles are not applicable, the aim as far as possible is to match the treatment in these territories to the existing treatment on the mainland market, for example in terms of levels of security of supply or the methodology for carrying out resource adequacy assessments.



4. Chapter V, Articles 35 to 47: Transmission system operation

With regard to Articles 35 to 47 of Chapter V concerning regional control centres, it is not initially necessary to establish a regional control centre in each of those territories.

In view of the above, and of Article 64 of Regulation (EU) 2019/943, derogations from the application of the following Articles are hereby requested for the Canary Islands, as an outermost region, for the Balearic Islands, as a small connected system, and for Ceuta and Melilla, as small isolated networks: Articles 3, 6, 7(1), 8(1) and (4), 9, 10, 11, 14 to 17, 19 to 27 and 35 to 47 of Regulation (EU) 2019/943.