

## CEER Note on Stranded Assets in the Distribution Networks

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#### 1 Background

In 2019, the Council of European Energy Regulators (CEER) launched a project on stranded assets. In light of the energy transition and current decarbonisation policies, stranded assets may become important for the energy sector, including for regulators, to deal with. Experiences with this issue and case studies on stranded assets are very valuable, for both the natural gas and electricity sectors.

#### **What do we mean by stranded assets?**

It is not an easy task to define stranded assets. According to the *CEER Study on the Future Role of Gas from a Regulatory Perspective*<sup>1</sup> in most regulatory frameworks, there is no clear and uniform regulatory definition for stranded assets. Similarly, no regulatory treatment or measures for those assets have been developed at a European level.

Nevertheless, regulated gas or electricity assets can be considered to be stranded when it is expected that regulated companies, as owners of those assets, cannot recover their efficient investment costs under the conditions for allowed revenues given the changes between the current and expected environment. One of the main reasons for such a situation is underutilisation of the assets, due to low demand, technical/environmental constraints, or policy decisions, among others.

The recovery of efficient costs in such cases could imply an increase in regulated tariffs, a need to obtain funds from outside of the regulated environment (for example the national budget) or, in extreme scenarios, the need to decommission assets or repurpose them for other uses.

According to the referred CEER study, regulators could apply different approaches to address stranded assets, such as depreciation policy (accelerated depreciation), asset valuation, and adjustment of cost of capital; governments may also decide to apply explicit compensation outside of network tariffs. The study presents different approaches and potential options for the regulatory treatment of stranded assets.

Via an internal questionnaire distributed at the end of 2019, CEER gathered information from its Member and Observer National Regulatory Authorities (NRAs) about their treatment of stranded or underused assets in the natural gas and electricity distribution networks. More specifically, CEER aimed to gather insights regarding whether NRAs were concerned with the risk that some assets may become stranded, which measures they have taken so far to address this issue and what the role of the NRA is. The factors that could trigger assets to be become stranded were also part of the questionnaire, e.g. evolution of demand, energy transition, decarbonisation, technological changes, government or political decisions or others. Actions that NRAs may be able take protect consumers from the costs of them was the final component of the internal questionnaire. A total of 26 NRAs responded to the questionnaire.

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<sup>1</sup> [CEER Future Role of Gas \(FROG\) Study](#), C17-GPT-04-01, 6 March 2018.

## 2 Main Issues

The majority of the participating NRAs agree with the definition of stranded assets as mentioned in the background section of this note. As for the main reason that may cause an asset to become stranded, NRAs refer to the significant reduction of grid usage, or structural demand reduction, due to shifts in energy consumption (brought about by decarbonisation policies).

In general, the majority of the NRAs that answered the questionnaire do not consider stranded assets as a problem for the time being. Most of them state that they do not yet have experience with stranded assets and therefore, only a few current cases were mentioned.

In response to the question “Have you had any cases of stranded assets in your distribution network (please specify whether in gas or electricity)?”, only seven NRAs answered ‘yes’.

The cases mentioned are equally divided between the electricity and gas sectors and are quite diverse, therefore, no trend could be identified. The cases include replacement of smart meters, write-downs related to a security of supply incentive, a system connection built for a large industrial consumer and lean gas (L-gas) infrastructure. In general, the financial and structural impact on the system (or on the concerned DSO) of considering the costs resulting from these specific cases was small.

Many NRAs indicated that they do not have any specific methods for addressing stranded asset issues. More specifically, in most countries there is no established framework or methodology for infrastructure decommissioning decisions. However, some mechanisms and regulatory methodologies were referred as possible solutions to help to mitigate the risk of stranded assets such as:

- Incentives for efficient investment;
- Development and utilisation of grids, creating alternative uses for assets (e.g. hydrogen and renewable gases);
- Changes in depreciation policies (accelerated depreciation); and
- Adjustments to the cost of capital.

Furthermore, CEER observes the following, more general, conclusions about regulation of the electricity and natural gas sectors:

- Only a couple of NRAs have formal responsibility over the economic sustainability of the distribution networks. However, most are responsible for determining a set of regulatory variables that, at least indirectly, seek to ensure the economic sustainability of the regulated distribution activity;
- Most NRAs are involved, to some extent, in the planning and development of distribution networks, although their specific responsibilities may vary; and
- The projected demand volume and any subsequent differences are assessed mainly by the regulated company, and the NRAs examine and confirm them in the process of setting tariffs and policies.

## 3 Conclusion

CEER will continue to follow the issue of stranded assets and if deemed relevant, conduct further research on the topic.