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Association of Electricity Distribution System Operators
"Association DSO (E) – Ukraine"

European Commission
Directorate General for Energy
Director General Ditte Juul Jørgensen
Directors Catharina Sickow-Magny, Cristina Lobillo Borrero

Brussels, 7 September 2021

Dear Director General Mrs Juul Jørgensen,
Dear Directors Mrs Sickow-Magny, Mrs Lobillo Borrero,

The Association of Electricity Distribution Systems Operators of Ukraine DSO(E) and the Union of the Electricity Industry Eurelectric fully support the European Commission to establish a Working Group to deal with the modernisation of the Ukrainian power sector focusing on the synchronisation with the European power grids.

We would like to express our appreciation for the European Commission's support to introduce the RAB tariff regulation in the Ukrainian electricity market from 2021. We look forward to a continuous fruitful cooperation with the European Commission and its Working Group.

In view of climate change and the recent environmental cataclysms, Europe is facing significant challenges which can be tackled only together through the common efforts of all European countries. In this context, we propose that the Working Group also covers the development of carbon–free energy in Ukraine in line with the European Green Deal as well as the modernisation of Ukrainian distribution networks as a key driver for ensuring security of electricity supply and boosting the energy transition in Eastern Europe.

Considering the difficult investment environment of the electricity sector in Ukraine and the obligations of Ukraine under the Association Agreement, as well as under the Agreement on Ukraine's accession to the Energy Community, Association DSO(E) – Ukraine and Eurelectric:

- assure full assistance for the European Commission and its Working Group in all efforts for synchronisation of energy systems between the European Union and Ukraine;
- bring to your attention the critical need to modernise the Ukrainian distribution grids as a key element of electricity market for ensuring uninterrupted and secure supply of electricity to all industrial, commercial and private consumers;
- appeal to the European Commission to support Ukrainian distribution networks by establishing a Working Group being special investment platform for this sector. The investment gap in Ukrainian DSOE companies can be addressed only together with European partners, in accordance with the Association Agreement between the EU and Ukraine;
- stress the importance of involving Ukraine in realisation of the European Green Deal;
- underline the need for more intensive development of new technologies and solutions in the Ukrainian electricity sector (carbon–free energy sources, energy storage facilities, smart grids, infrastructure for E–mobility, demand response management, cybersecurity);
- call upon the European Commission to create a special program of the Working Group "Modernisation and restoration of small hydropower in Ukraine".

Association DSO(E) – Ukraine and Eurelectric would welcome an opportunity to organise meetings with the Working Group to discuss the situation and solutions for Ukraine.

Yours sincerely,

Kristian Ruby
Secretary General, Eurelectric

Iryna Zavada
President, Association DSO(E) - Ukraine

Annex 1: Factsheet on Electricity Distribution Sector in Ukraine

At present, 90 percent of electricity produced in Ukraine is supplied to consumers through distribution networks. The complete length of the Ukrainian electricity distribution grids is estimated at 820145 km, 90,25% of these being overhead power lines.

However, the level of technical deterioration of this infrastructure reaches at least 70 percent. In 2020, the average duration of power outages (SAIDI) was over 800 minutes making it the worst indicator in Europe (e.g., compared to Germany's 20 min). Electricity losses in distribution grids in 2020 reached up to 10,13 percent of the distributed electricity's volume (3–5 % in Europe). Such a situation undermines the principle of a secure and uninterrupted supply of electricity to consumers as the main goal of the 2017 Law "On the Electricity Market in Ukraine".

The distribution investment programmes approved by the National Energy and Utilities Regulatory Commission of Ukraine (NEURC) fall short of addressing the current needs and demand. The Ukrainian distribution companies do not have the possibility to invest in an adequate manner not only in grid extensions, but even in maintenance of the existing infrastructure.

The introduction of the stimulating tariff setting (RAB tariff) in Ukraine is one of the solutions for this underinvestment in grids. This is an issue of crucial importance for all Ukrainian distribution companies; however, it remained unresolved until 2020.

With the support of the European Commission and other international partners the Ukrainian National Regulator introduced the RAB tariff regulation on Ukrainian electricity market since beginning of 2021 which increased the DSO investment programme by 59%, but experts suppose the real positive impact of this crucial decision no sooner than in some years.

The following arguments played an important role for the introduction of RAB tariff and continue to be representative for the current issues:

- distorted structure of the Ukrainian electricity tariff where only 9 percent (2-3 times less than in the EU countries) relates to distribution, therefore discriminating distribution in favor of the generation sector, whose share amounts 80-90 percent;
- relation between levels of profitability (rates of return) of electricity distribution, and government bonds (currently the most stable investment tool). Ukrainian distribution companies operate with zero profitability, while the profit on government bonds is the highest in Europe – between 12,3 (3-years bonds) and 12,75 percent (6-years bonds) in August 2021;
- cost of credit resources (the rates of long-term lending in Ukraine is 12-20 percent, compared to 2-5 percent in Europe).

We would appreciate if the European Commission could set up a dedicated investment platform for Ukrainian distribution networks by its Working Group and push the Ukrainian government to create an attractive and stable investment climate especially for energy sector, in accordance with the Association Agreement between the EU and Ukraine *(Article 338).* We are convinced that the investment gap issue in Ukrainian DSOE companies can be solved only together with support of our European partners.

Only if adequately modernised, distribution grids in Ukraine can ensure security of electricity supply while facilitating the integration of ever-increasing shares of carbon–free energy sources in line with the European Green Deal. The National Regulator and international energy experts recently estimated the investment needs in the Ukrainian electricity distribution networks approximately at the level of 3,5 billion Euro for the next five years.

Source. NEURC/ National Regulator of Ukraine, Ukrenergo, Annual reports 2020

Annex 2: Factsheet on Small Hydropower in Ukraine

Ukraine has enormous potential for the development of small hydropower. The installed capacity of small hydropower plants in Ukraine is about 200 MW, and the potential (according to various estimations) is up to 2000 MW. Practically, only 10 percent of hydropower capacity is used in the Ukraine. Most of the operating small hydropower plants in Ukraine were put into operation in the 1950s and remain operating only thanks to the enthusiasm of staff who maintain these plants.

Involvement of small hydroelectric power plants in the regulation of the daily schedule of the United Energy System (UES) of Ukraine in the future will reduce the cost of electricity in general and, as a consequence, reduce retail electricity prices. The morning maximum load of the UES of Ukraine lasts about 2-3 hours with a difference of 250-500 MW. The evening maximum load of the Ukrainian UES lasts about 4-5 hours with a difference of 1000-1500 MW. For the purpose to minimise number of starts/stops of TPP units (approx., up to 3-4 units), it is necessary to have an additional load adjustment of power plants in the morning zone by 500 MW, and in the evening by 1500 MW. Small hydropower plants can become this crucial balancing instrument.

Currently small hydropower plants in Ukraine operate at a specific "green" tariff rate, but it covers much-needed overhauls of hydropower plants and cannot cover the costs of the large-scale modernisation under existing lending conditions in Ukraine (up to 20 percent) and in the world (2–5 percent). Ukraine is presently implementing direct (official tariff reduction) and indirect (introduction of excise duty on electricity generated by renewable energy sources) steps to reduce the "green" tariff, and in accordance with the current legislation, in 2030 these tariffs will be phased out.

From 2030, Ukraine's small hydropower plants have to operate in the electricity market on general terms. Small hydropower plants will be able to "survive" only if they fully operate in the markets of ancillary services and balancing (participation in all types of daily regulation). To achieve this aim small HPPs must be modernised and fully automated until 2030, otherwise the enormous potential of small hydropower in the Ukraine will be wasted.

We would appreciate if the European Commission could therefore as well establish a special program of its Working Group "Modernisation and restoration of small hydropower in Ukraine" for implementation of innovative projects to ensure rational consumption of resources while preserving our planet for future generations, especially given the prospects of large-scale use of renewable energy sources in the sector of small hydropower.

The extensive implementation of reconstruction and restoration projects for small hydropower plants in Ukraine with full automation of the process of control of the work of hydropower units will ensure:

- development of distributed generation in Ukraine using renewable energy as an integral part of United Energy System of Ukraine;
- significant increase of the possibility for the involving European companies and producers of hydroelectric equipment in joint European projects of the reconstruction and restoration of small hydropower plants in Ukraine;
- will overall help reduce greenhouse gas emissions in accordance with the European Green Deal.

Source. Energy Ministry of Ukraine