

## **ENTSO-E consultation on the review of the Harmonised Allocation Rules for long-term transmission rights and Core and GRIT Annexes**



### **EFET response – 3 June 2021**

The European Federation of Energy Traders (EFET) welcomes the opportunity to provide comments on ENTSO-E consultation on the on the review of the Harmonised Allocation Rules (EU HAR) for long-term transmission rights for Core and GRIT regions in accordance with Article 6 and 68.5 of Regulation 2016/1719 (FCA GL).

#### **General comments**

EFET has followed the initial drafting and approval of the EU HAR and its Annexes, and we continue to exercise scrutiny on any type of proposed amendment. With time, the quality of the EU HAR has significantly improved, and we welcome this as they are core to a reliable allocation process of forward transmission capacity in Europe. Risk management through (cross-border) hedging is a key element in sourcing and providing electricity to customers competitively, as it allows market participants to avoid exposure to short-term price volatility and imbalance costs. Allocation of long-term transmission rights (LTTRs) to market participants also provides long-term signals to the TSOs regarding potential congestion on certain cross-border elements. This provides an indication to the TSOs regarding forward market activities and could potentially help in forecasting additional congestion revenues that TSOs receive as a congestion income.

#### **Core CCR specific Annex 1**

We acknowledge the proposal to include caps on the compensation for curtailed LTTRs at the HU/SI border in accordance with Article 59(2) of the HAR.

#### **GRIT CCR specific Annex 3**

We welcome the deletion of article 2 on the temporary arrangement for the curtailment deadline at the Italy SOUTH-Greece bidding zone border (applicable until implicit allocation was available at this border) given that SDAC went live at this border on 15th December 2020.

<sup>1</sup> The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent and liquid wholesale markets, unhindered by national borders or other undue obstacles. We build trust in power and gas markets across Europe, so that they may underpin a sustainable and secure energy supply and enable the transition to a carbon neutral economy. EFET currently represents more than 100 energy trading companies, active in over 27 European countries. For more information: [www.efet.org](http://www.efet.org)

## **Extension of HAR Article 59 ("Compensation for curtailments to ensure operation remains within Operational Security Limits before the Day Ahead Firmness Deadline") to decoupling events**

**We strongly oppose the proposed addition of a paragraph 5 to article 59 EU HAR.** With this amendment, the TSOs seek to change one of the fundamental rules of financial firmness of long-term allocation, namely the remuneration of LTTRs at the day-ahead market spread. This measure would be detrimental to market participants' ability to hedge positions across borders, fundamentally affect the firmness of LTTRs in all circumstances – decoupling periods or not – and in turn reduce their value to the detriment of TSOs themselves. As a consequence, we doubt that the measure would even be beneficial for consumers.

### *Context*

Article 59 EU HAR lays out the requirement for the compensation of LTTRs in case of curtailment to ensure operation remains within Operational Security Limits before the day-ahead firmness deadline. Compensation at the day-ahead market spread is the rule, unless no day-ahead price has been calculated in at least one of the concerned bidding zones (paragraph 1).

Paragraphs 2, 3 and 4 foresee the possibility for TSOs to apply caps on compensation payouts in case the total congestion income collected by the relevant TSOs in all timeframes at the concerned bidding zone border during the relevant calendar year (for AC lines) or month (for DC lines) does not cover the compensation expenditures.

The TSOs propose to add a paragraph 5 to article 59, which would read as follows:

*5.- Irrespective of whether it is a Direct Current interconnector or not, the cap described in paragraphs 3 and 4 of this Article shall also apply to the remuneration of Long Term Transmission Rights holders for non-nominated Physical Transmission Rights and Financial Transmission Rights in case of fallback Allocation for Implicit Allocation.*

### *Legal critique*

As mentioned above, article 59 EU HAR deals with compensation for curtailments to ensure operation remains within Operational Security Limits before the day-ahead firmness deadline (11:30 CET). The matter that the TSOs seek to address in their proposed paragraph 5 is out of scope of article 59 EU HAR, in so far as:

- it concerns the remuneration of LTTRs – and not compensation for curtailments
- it applies to events happening after the day-ahead firmness deadline – and not before

The remuneration of LTTRs, including in cases of decoupling, is already tackled in article 48 EU HAR. Article 48.1(a) EU HAR foresees that LTTRs are remunerated at the day-ahead market spread when day-ahead market coupling is in place at a given bidding zone border, whether the allocation actually occurred implicitly or via a fallback process. Should the TSOs want to include a cap on the remuneration of LTTRs in case of decoupling, then a modification of article 48.1 EU HAR would be in order, rather than article 59.

Further, a modification of the EU HAR to allow caps on the remuneration of LTTRs in case of decoupling would require amendments to the FCA GL, which forms the legislative basis on which the EU HAR have been adopted. Like article 48 EU HAR, article 35 FCA GL foresees that LTTRs are remunerated at the day-ahead market spread when day-ahead market

coupling is in place at a given border, whether the allocation actually occurred implicitly or via a fallback process. This principle does not suffer any exception in the FCA GL. Article 54 FCA GL, which foresees the possibility for TSOs to established caps on compensation, only applies to curtailed LTTRs and can therefore not serve as a basis to amend article 59 EU HAR in the direction pursued by the TSOs.

Our take is hence that the TSOs seek to amend the wrong article in the EU HAR, and without a legal basis to do so in the FCA GL.

### *Fundamental critique*

We acknowledge the concern of the TSOs with regard to the remuneration of LTTRs in case of decoupling. In times of normal operation of market coupling, TSOs cash in the day-ahead market spread in congestion rent that they can then redistribute to LTTR holders. For TSOs, this means a null-sum game in the day-ahead timeframe, plus a net benefit from the long-term allocation. In cases of decoupling, fallback allocation in the form of explicit auctions is organised, and TSOs cash in the revenues from day-ahead explicit auction of transmission rights while they have to remunerate LTTR holders at the day-ahead market spread. As the explicit fallback auctions and the day-ahead market prices of the concerned bidding zones are not necessarily connected, this may result in discrepancies between the day-ahead congestion rent collected by the TSOs and what they need to payout for LTTR remuneration. As such discrepancies have been observed in the recent past, the TSOs propose to change to rules of remuneration of LTTRs.

As the proposal of a new paragraph 5 to article 59 EU HAR comes with no explanatory document, our analysis below is based on the presentation made by the TSOs at the MESC meeting of 11 March 2021<sup>2</sup>. We recall that any significant departure from well-established market design features should be thoroughly justified and proportionate. Hence, we would expect the TSOs to properly assess and demonstrate:

- (a) **the necessity of the proposed measure**: i.e. that the existing remuneration rules put an unsustainable financial burden on the TSOs even with a few rare days of decoupling;
- (b) **the proportionality of the proposed measure**: i.e. that a modification of the remuneration rules do not have a detrimental impact on the allocation of LTTRs and their value.

Regarding point (a) on the necessity of the measure, the TSOs present the remuneration of LTTR at the day-ahead market spread in case of decoupling as an “overcompensation”. They base their claim on a comparison between, on the one hand, the average daily TSO revenue of LTTR auctions (which correspond to the average value of yearly and monthly LTTRs over the entire period covered by these products extrapolated for the single days when decoupling events occurred) and, on the other hand, the revenues captured by the TSOs with the shadow auctions organised on three decoupling days in 2019, 2020 and 2021. And then compare those two values to the remuneration of LTTR for those specific decoupling days to MPs. We believe this approach is misleading, and that the TSOs should compare all the remuneration paid out

<sup>2</sup> See the TSOs presentation at: [https://eepublicdownloads.azureedge.net/clean-ndocuments/Network%20codes%20documents/MESC/2021%20MESC%20documents/210321\\_MESC\\_3.1\\_Remuneration%20of%20LTTRs\\_v2.pdf](https://eepublicdownloads.azureedge.net/clean-ndocuments/Network%20codes%20documents/MESC/2021%20MESC%20documents/210321_MESC_3.1_Remuneration%20of%20LTTRs_v2.pdf).

to LTTRs, including during the unfortunate situations of decoupling, compared to the total revenues coming from the allocation of cross-zonal capacity at different timeframes annually (as this is done in the case of the cap on remuneration in case of LTTR curtailments).

When reverse-engineering the numbers presented by the TSOs, we can see observe the following:

- Decoupling event of 07/06/2019: LTTR payout on the day = 2,8% of forward congestion rent for 2019:
  - o LTTR allocation revenues for 2019: EUR 693.5 million
  - o Compared to: LTTR remuneration for 07/06/2019: EUR 19.6 million
- Decoupling event of 04/02/2020: LTTR payout on the day = 0,9% of forward congestion rent for 2020:
  - o LTTR allocation revenues for 2020: EUR 22.7 million
  - o Compared to: LTTR remuneration for 04/02/2020: EUR 208,000
- Decoupling event of 13/01/2021: LTTR payout on the day = 2% of forward congestion rent for 2021:
  - o LTTR allocation revenues for 2021 (without accounting for monthly LTTRs, we assume): EUR 191.9 million
  - o Compared to: LTTR remuneration for 13/01/2021: EUR 4 million

Reverse-engineering the data presented by the TSOs shows that the remuneration they paid out to LTTR holders during days of decoupling was far from reaching the congestion rent they collect only in the forward timeframe in each concerned year. Of course, a thorough assessment should look for each year at all the payouts of TSOs to LTTR holders (including outside of decoupling days) compared to all the congestion rent collected in all timeframes for the whole year. The TSOs did not provide this full picture, but we consider it unlikely to fundamentally change the orders of magnitude presented above.

Regarding point (b) on the proportionality of the measure, we are missing an assessment by the TSOs of the effect that their proposed measure may have on the allocation of LTTRs and their value. The wording used by the TSOs that firmness “would be reduced in case of decoupling” is once again misleading, as changing the rules of remuneration for LTTRs in case of decoupling effectively diminishes the firmness of all LTTRs at the time of allocation, whether or not they are redeemed on a day of decoupling at a later stage.

It should be taken for granted that any change in the remuneration rules for LTTRs will be accounted by market participants when they participate in the long-term auctions. Hence, any reduction of firmness, in particular for events that market participants are unable to mitigate, will reduce the overall value that market participants place in LTTRs and are willing to pay for. This would significantly affect the revenue that TSOs capture with the sale of LTTRs all year round. How far this loss of revenue from the allocation of diminished LTTRs for all delivery periods would counteract the objective of the TSOs to reduce payouts to LTTR holders during days of decoupling should have been considered and properly assessed by the TSOs.

In conclusion, and in the absence of a demonstration otherwise by the TSOs, we believe that the TSOs proposal is neither justified, nor proportionate to their aim.

*Proposed way forward*

The concerns of the TSOs are directly linked to the more frequent occurrence of decoupling events in the last two years. We believe that the primary focus of the TSOs, in cooperation with NEMOs, should rather be to minimise the probability of decoupling events by investing in the day-ahead market coupling process and its resilience.

As explained above, we do not believe there is an intrinsic problem in the remuneration rules for LTTRs in case of decoupling, as they have been long negotiated between market participants, TSOs and NRAs back in the mid 2010s, and approved as part of the FCA GL. However, the low participation in shadow auctions that we have seen especially in the decoupling event of 07/06/2019 has triggered concerns on all sides. Hence, rather than seeking a change of the EU HAR, we invite the TSOs to focus on the management of decoupling events, and investigate, in particular, in the following directions:

- a) avoid decoupling events by reinforced testing/improvements of the SDAC process.
- b) improve communication towards market participants in case of (a risk of) decoupling to reduce the level of uncertainty ahead of the shadow auctions.
- c) Improve competition in the shadow auctions, with:
  - intensifying training towards market participants to incentivise their participation in shadow auctions in case of decoupling.
  - exploring the possibility to provide more time to prepare competitive capacity bids with full information, ahead of the shadow auctions.
  - streamlining the shadow auction tool to facilitate participation in the auctions, notably for those market participants active on multiple borders.

These improvements will allow the valuation of cross-border capacity allocated under a shadow auction process to better reflect the spread between the energy auction prices in each bidding zones.