

## RTE consultation on an impact assessment of the French capacity remuneration mechanism



### EFET response – 13 March 2020

We thank RTE for the opportunity to give input to their planned impact assessment of the French capacity remuneration mechanism (CRM). This exercise will complement the regular adequacy assessments performed at national and EU level, aimed to identify a potential gap in security of supply. We trust the impact assessment will be very useful to provide a sturdy analysis of the effectiveness of the CRM (i.e. filling a potential gap in security of supply identified in adequacy assessment), as well as its efficiency (i.e. whether its design is fit for purpose). It will also contribute to the fulfilment of France's obligation to its CRM according to article 21.6 of the recast Electricity Regulation 2019/943.

#### **Part 1: contribution of the CRM to respecting the reliability standard**

##### ***Questions 1.1 on the contribution of the capacity mechanism to security of supply***

*Do you share an interest in building a counterfactual scenario of what the electricity system would have been for the period 2017-2020 "without capacity mechanism" in order to assess the contribution of the capacity mechanism to security of supply?*

Yes, a counterfactual scenario is necessary to assess the effectiveness of the mechanism, i.e. check whether the CRM is actually needed.

*Do you share the principle of building this counterfactual scenario on the basis of economic analyses on the profitability of power generation and demand response?*

Yes, this should include revenues from the energy market, ancillary services, and the CRM.

*Do you have quantified elements to share (publicly or confidentially) on the economic situation of the different business and the effect of the capacity mechanism on their continued existence in the electrical system?*

No. EFET is willing to help RTE get in touch with our members to retrieve such information when comes the time of the analysis.

*In order to assess the income earned on the energy markets, it is necessary to represent sales strategy on the markets and in particular on what horizon sales are made on forward products. Are you ready to share the proportion of volumes that are sold on the futures markets, 2 years, 1 year, 6 months before delivery, etc.?*

This information is generally publicly available on the websites or reports of market participants, at least for large undertakings. This information is also collected by CRE on a regular basis.

If needed, EFET is willing to help RTE get in touch with our members to retrieve such information when comes the time of the analysis.

*Given the temporality of the capacity mechanism since its launch (opening of delivery years at most 2 years before the delivery period), which capacities do you consider might have been closed, mothballed or not developed if the capacity mechanism had not been put in place? And on the basis of which economic criteria?*

No opinion.

### **Questions 1.2 on the consistency between the adequacy forecast and the capacity mechanism**

*Do you share an interest in an ex-post analysis of the differences between the vision of security of supply conveyed by the adequacy forecast (Bilan Prévisionnel) and that of the capacity mechanism? Do you identify other relevant benchmarks to analyse? Do you have any analysis to share?*

Yes, this analysis will be useful to identify potential gaps between the security of supply visions in the national adequacy assessment and the CRM, and why.

In our view, this analysis is a way to check whether the French CRM is in line with article 22.1.c of Regulation 2019/943, requiring CRMs to “not go beyond what is necessary to address the adequacy concerns referred to in Article 20 [i.e. identified in the European or national adequacy assessments.]” We therefore suggest taking also account of the European adequacy assessment in this gap analysis.

### **Questions 1.3 on availability checks**

*Do you share an interest in carrying out an analysis of the methods of making capacity available and the level of checks carried out? Specify the aspects on which you consider useful that it be complemented.*

No comment.

### **Questions 1.4 on a cost-benefit analysis for society**

*Do you share an interest in carrying out an analysis of the costs and benefits of the capacity mechanism, based on its functioning over the past years?*

Yes, a cost-benefit analysis (CBA) of the CRM would be useful to assess the efficiency of the mechanism, i.e. check whether the design chosen for the CRM is actually the right one.

*In your opinion, which components of costs and benefits should be included in the analysis?*

As far as the costs and benefits linked to the operation of the CRM itself are concerned, the CBA should include the following components:

- Costs:
  - o **costs of participating in the CRM for obliged suppliers** (cost of acquiring capacity certificates, transactions costs on the OTC and exchange markets, power exchange fees related to the auctions on the organised market, other administrative and HR costs)
  - o **costs of participating in the CRM for capacity owners** (transactions costs on the OTC and exchange markets, power exchange fees related to the auctions on the organised market, other administrative and HR costs)
  - o **costs of being excluded from the CRM for storage operators and foreign capacity owners** (missing revenues)
  - o **costs of running the CRM for RTE** (pre-qualification and qualification, availability checks, registry, other administrative and HR costs)
  - o **costs of establishing and monitoring the CRM for the Energy Ministry and CRE** (administrative and HR costs)
- Benefits:
  - o **benefits of participating in the CRM for capacity owners** (revenues from capacity certificates, avoided cost of capital, capture of missed revenues from the CRM for storage operators and foreign capacity owners)
  - o **benefits of running the organised market for power exchange(s)** (fees related to the auctions on the organised market)

If the RTE assessment aims to assess the efficiency of the French CRM, the CBA should be approached with a view to assess the welfare benefit of the mechanism, compared to a counterfactual scenario without CRM. Hence, beside the elements

listed above, the welfare analysis should include effects on investments costs, outage costs (link to the VoLL), avoided costs of capital, and effects on the energy market. Operational costs and revenues in the energy market are also important. When new capacity is developed via the CRM, this impacts future energy revenues for existing assets along with the operational costs. Energy prices will be on average lower (impacting energy revenues) and a few power plants will run less hours compared to a situation where no capacity market is implemented.

This analysis should also compare to the CRM revenues received by the capacity providers over the period 2017-2020, compared to a scenario without CRM, to ensure that the capacity remuneration appropriately tackles the missing money problem; without over- or under-compensation.

*In particular, could you provide an estimate of the investment and operational costs incurred on your side following the implementation of the capacity mechanism?*

EFET is willing to help RTE get in touch with our members to retrieve such information when comes the time of the analysis.

*Furthermore, do you consider that the implementation of the capacity mechanism (certificates exchange for one-year deliveries and/or long-term tendering) results in a risk reduction likely to generate profit? If so, how does it materialise in practice for you?*

The CRM is intended as a societal risk reduction mechanism in terms of security of supply, which naturally translates in practical terms in an individual risk reduction mechanism in terms of return on investment for capacity owners.

### **Questions 1.5 on a cost analysis for the consumer**

*Do you share an interest in carrying out a consumer cost analysis? Do you have any recommendations regarding the methodology to be used?*

Yes, but the consumer cost analysis should not be stand alone, rather a follow-up to the general CBA proposed in part 1.4. Once the overview of the costs is clear, RTE can perform a distributional analysis to see how these costs are allocated. Also, it will be important to take account of potential benefits for consumers, so that the analysis shows only “net costs” incurred by consumers because of the CRM.

## **Part 2: Contribution of the CRM to the energy and climate objectives**

### ***Questions 2.1 on the link between the CRM and the energy and climate roadmap***

*Do you share an interest in analysing the link between the capacity mechanism and the government's energy and climate roadmap? Do you have quantitative elements to feed this analysis?*

Yes, consistency between the CRM and other policy objectives at French and European level is important.

Bearing in mind our wish to see CRMs remain technology neutral, but considering the carbon emissions limit established in article 22.4 Regulation 2019/943, it would be important to consider including ACER's guidelines on CO<sub>2</sub> emission limits for generation capacity in the framework of the French CRM to ensure consistency of this element of its design with that of other European capacity mechanisms.

Among the elements listed by RTE, we note that both implicit demand response and storage assets cannot currently participate in the French CRM. We would welcome recommendations to remedy this situation and ensure that the CRM is truly technology neutral, in line with article 22.1.h of Regulation 2019/943.

As far as the contribution of the CRM to the financing of RES-E development is concerned, we have no fundamental objection to RTE looking into this but we wonder about the added value of this part of the analysis since the financing would otherwise be granted via the CSPE.

### ***Questions 2.2 on long-term tendering***

*Do you share an interest in focusing on long-term tendering? Which aspects of this tender are important to analyse according to you?*

It is rather early for an impact assessment of the AOLT especially with regard to its contribution to the energy and climate objectives. Like for the main part of the CRM, the AOLT should be technology neutral and allow the participation of assets/services currently excluded from the CRM. This includes all types of demand response, storage, but also foreign capacity assets – as explicit cross-border participation is for the moment still not available.

## **Part 3: CRM participants' behaviour**

No comment.

## **Part 4: Mechanism design and complexity**

### **Questions 4.1 on the diagnosis of the complexity of the mechanism**

*Do you share an interest in objectifying the debate on the complexity of the mechanism by identifying the most complex elements of the mechanism, and objective indicators? In particular, could you share, as part of this consultation, quantified elements on the resources and investments that your company has mobilised on the different aspects of the mechanism (obligation, certification, exchanges ...) and in the different types of tasks (regulatory, IT operation, operations)?*

Yes, we agree with this objective. EFET is willing to help RTE get in touch with our members to retrieve such information when comes the time of the analysis.

*Did the complexity of the capacity mechanism contribute to causing errors on your side? If yes, on which subject? Do you have other indicators to suggest to RTE to identify the main sources of complexity of the mechanism?*

No comment.

### **Questions 4.2 on the arbitration between complexity and precision of the mechanism**

*Do you share an interest in analysing some potentially complex provisions compared to the interest in terms of precision that they provide? Do you have any comments or proposals on the scope of the provisions to be considered?*

Yes, probably a good idea, but these things seem difficult to compare. We expect this part of the analysis to be rather qualitative, making it difficult to weigh the pros and cons. We believe the primary objective of an impact assessment would be to provide recommendations on what to amend or not in the CRM, so RTE should focus on elements where their analysis can result in conclusions and recommendations.

### **Questions 4.3 on the temporality of the mechanism**

*Do you share an interest in revisiting the temporality of the capacity mechanism? What particular aspects seem important to analyse according to you?*

No comment.

#### **Questions 4.4 on the modalities of cross-border participation**

*Do you share an interest in revisiting the terms of cross-border participation, with regard to its current functioning?*

Yes. We would like the framework to be reformed to ensure effective direct participation of foreign capacities in the capacity mechanism, and to see all the capacities contributing to French security of supply properly rewarded.

a. Effective cross-border participation

**The current functioning of direct cross-border participation of foreign capacity assets in the French CRM is currently non-existent.** Recent updates on the subject provided by RTE show that contacts with neighbouring TSOs on the establishment of bilateral cooperation agreements are only nascent, and actual negotiations have not really started.

We have repeatedly warned RTE against the complexity of the system they have put in place for explicit cross-border participation, and in particular how the reciprocity clause for cost sharing with neighbouring TSOs could threaten their willingness to establish bilateral agreements<sup>1</sup>.

Indeed, the application of a reciprocity clause for the sharing of rents from entry capacity allocation creates a very concrete hurdle to the explicit cross-border participation of foreign capacities in national CRMs. With no perspective to benefit from revenues of the sale of interconnection tickets, and heavy processes and potential costs to allow the direct participation of assets in the French CRM, foreign TSOs have no incentive to enter into negotiations with RTE. It leads to the de facto exclusion of foreign capacities from appropriate remuneration to the added security of supply they bring to the French system.

**We believe a serious reconsideration of the framework for explicit cross-border participation is required to ensure the effective direct participation of foreign assets in the French CRM in practice, not only on paper. This should in a spirit of truly facilitating such participation, as laid out in article 26 of Regulation 2019/943.**

This exercise should also feed into ENTSO-E's work on methodologies for cross-border participation in CRMs<sup>2</sup>. These methodologies have unfortunately been largely designed on the French model, which RTE seems to be questioning now.

<sup>1</sup> See our paper on reform proposals to improve the current functioning of the French CRM and ensure effective participation of foreign capacities, dated 11 January 2018 and available at:

[https://efet.org/Files/Documents/Downloads/EFET%20paper\\_French%20CRM\\_11012018.pdf](https://efet.org/Files/Documents/Downloads/EFET%20paper_French%20CRM_11012018.pdf), and our response to the RTE consultation on cross-border participation in the French CRM, dated 9 June 2017 and available at: [https://efet.org/Files/Documents/Downloads/EFET\\_RTE-consultation-XB-CRM\\_09062017.pdf](https://efet.org/Files/Documents/Downloads/EFET_RTE-consultation-XB-CRM_09062017.pdf).

<sup>2</sup> See our response to the ENTSO-E consultation on methodologies for cross-border participation to capacity mechanisms, dated 13 March 2020 and available at:

[https://efet.org/Files/Documents/Downloads/EFET\\_ENTSOE%20consult%20XB%20CRM\\_13032020.pdf](https://efet.org/Files/Documents/Downloads/EFET_ENTSOE%20consult%20XB%20CRM_13032020.pdf).

b. Scope of cross-border participation

We invite RTE to reconsider the double requirement that foreign capacities must be located in an adjacent EU Member State to be allowed to participate explicitly in the mechanism.

With the requirement that the capacity be located in an EU Member State to participate explicitly in the mechanism, RTE and French authorities have closed the door to an explicit participation of Swiss capacities to the French CRM. We understand that the agreement with DG Competition of 2016, and now article 26.1 Regulation 2019/943, only concern borders with other EU Member States. However, **these rules do not explicitly exclude opening up CRMs beyond EU borders. We therefore request that Swiss capacities be considered for explicit participation in the mechanism, and the security coefficient be adjusted accordingly.** This could be facilitated by a bilateral agreement between RTE and Swissgrid. The example of the recent EU- Switzerland agreement on the linkage of their respective Emissions Trading Systems is a good example of effective cooperation in the energy field even in the absence of a wide-ranging energy agreement between Switzerland and the EU.

Also, we believe that capacities located in non-directly adjacent bidding zones do contribute to the security of supply of the zone where a CRM is established. In practice, this of course adds layers of complexity, requires multilateral agreements or bilateral agreements beyond France's direct neighbours, and would likely make capacity available for the French CRM in indirect neighbours scarcer than in direct neighbours. However, **no outright exclusion should apply if concrete contribution to the French CM can be evidenced.** As a matter of fact, the statistical analysis of RTE will only be realistic if it models countries beyond direct neighbours, as it is done for the "Bilan Prévisionnel" adequacy studies. So we assume the necessary data to be available. We therefore advise RTE not to study the possibility of an explicit participation of capacities from non-adjacent bidding zones altogether, and to consider extending the mechanism – and adjusting the security coefficient accordingly.

**Question 5 on the ambit of the impact assessment**

*Please provide any additional feedback on the ambit of the impact assessment*

The cohabitation of a decentralised approach (initial design of the French capacity market with an obligation on electricity suppliers) and a centralised approach (AOLT mechanism) adds complexity to ensure security of supply on the one hand, and makes the interaction between the French CRM and other similar mechanisms in neighbouring countries more complex, on the other hand. We would welcome an assessment by RTE of this double feature of the French CRM, and whether a reform would be appropriate to ensure an easier compatibility of the mechanism with other European CRMs.