

EFET¹ response to the CREG consultation on the implementation of the EU Harmonised Allocation Rules



18 September 2015

The European Federation of Energy Traders (EFET) welcomes the initiative to harmonise the allocation rules for long-term transmission rights in Europe. EFET believes the establishment of harmonised allocation rules have the potential to move forward in the integration of electricity markets and should facilitate the management of portfolios on a cross-border basis.

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 rights to market participants also provides long term signals to the TSOs regarding potential congestion on certain cross-border points. 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.

However, as stated previously in the consultations run by ENTSO-E, we believe that the EU HAR as proposed by TSOs largely fail to reach these objectives. The progress compared to the current situation seems to be limited and in several cases undermined by a regional/border specific Annexes. Our expectation was that the HAR would be fully in line with the FCA network code and ACER's recommendations. We expected to see harmonised rules and a higher or improved degree of firmness on most of the borders, if not all.

One of the main concerns of EFET in the implementation of the EU HAR relates to the introduction of Financial Transmission Rights (FTR) options at the Belgian borders replacing Physical Transmission Rights (PTRs). CREG should bear in mind that over-the-counter (OTC)

¹ The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent, sustainable and liquid wholesale markets, unhindered by national borders or other undue obstacles. We currently represent more than 100 energy trading companies, active in over 28 European countries. For more information, visit our website at www.efet.org.

wholesale markets still concentrate the majority of electricity liquidity and trading in Europe, supported by the state-of-the-art transparency requirements of REMIT and the Transparency Regulation. As mentioned at many occasions, market participants appreciate and highly rate the optionality that PTRs provide to physically flow power from one zone to another. With the Elia proposal, FTR options will be the only option available to the market, so that this optionality will be removed, without any added value as to the level of firmness and the volume of the forward rights.

Despite the above-mentioned reservations, EFET acknowledges the fact that FTR options are envisaged in the ACER Framework Guidelines and in the draft FCA network code. However, we believe that the introduction of FTR options should only be effective once all the details and characteristics of the proposed rights are well known. Of particular importance would be a study on cost-benefits analysis on the introduction of FTR options. This study should also explain the need for such a change, including an explanation on any issues related to PTRs nominations which, according to us, has never been substantiated. For this reason, we would like to highlight few elements that require the attention of the regulator:

- The **exclusive** use of FTR options ties market participants to power exchanges, as physical OTC cross-border transactions in the forward timeframe will not be available anymore and market participants will have to revert to the day-ahead market for physical transactions. This restricts market participants' ability to weigh the benefits and drawbacks – in financial terms and practical arrangements – of using OTC platforms or power exchanges for their physical cross-border transactions. In practical terms, this also means that market participants will need to close positions on the day-ahead market on both sides of the border, with all the practical and financial implications that trading on a power exchange implies – mandatory membership to the power exchange, exchange and clearing fees.
- CREG should be aware that in case of partial clearing, the outcome will be different than with PTRs due to a potential remaining imbalance at BRP side. However, first, market participants should still be able to rely on cross-border capacities to balance their portfolio, as the case might be. The switch from PTRs to FTR options does not change the interconnection capacity available to the market. As a result, this implementation should not result in a regression in the functioning of the market. Second, the introduction of FTR options should not come with a risk of paying high imbalance prices that would not have been there in case of PTRs.
- Furthermore, firmness of the transmission rights is crucial for market participants. In case of curtailment, EFET recognises the risk that TSOs may bear if compensation for the curtailed rights is done without a cap. It is however important to note once again that for market participants, long-term capacity rights represent hedging instruments and therefore an investment. The use of congested network is not free of charge and congestion costs are an important market signal. The congestion income naturally goes to the TSOs as the main body managing congestion in real-time, short and long term. The congestion incomes should primarily be used by the TSOs to relieve the congestion and ensure the firmness of transmission capacity rights. Therefore:

- Compensation for curtailment of the allocated rights **in case of Emergency Situation** should only be subject to a cap that mirrors both the risks of TSOs and those of market participants. Therefore, CREG should not approve any cap that is below the standards set by ACER in its Recommendation on the FCA network code of 22 May 2014, i.e. a cap calculated on yearly congestion income from all timeframes at the concerned bidding zone border. Monthly congestion income caps do not provide any incentive for TSOs to avoid or reduce curtailments.
- EFET does not agree with the introduction of price caps in case TSOs curtail the transmission capacity **for reasons of System Security** before the Long Term Firmness Deadline. The broad definition of this situation allows for too much interpretation on TSO actions – TSOs are supposed to ensure system security at all times – and covers a time horizon sufficiently before real time for TSOs to take countermeasures. To the extent that the TSOs have full control over the means to anticipate and manage the network difficulties, we believe that the concept of Emergency Situation is sufficient to tackle risks of unexpected situation on the side of TSOs. The inclusion of caps for such a vague reason undermines the value of Long-Term Transmission Rights as a hedging instrument. For this reason, EFET asks CREG that, if TSOs do want to retain the possibility for curtailment for this reason, they compensate market participants for the full price risk exposure, without caps. In any case, looking at historic data, this does not represent a financial risk for the TSOs.

In conclusion, we urge CREG to reconsider its draft opinion on the Elia proposal for the introduction of FTR options as it stands. Elia should perform and publicly disclose its assessment of the need for and impact of the introduction of FTR options at the Belgian borders. If introduced, FTR options should be proposed at enhanced firmness conditions in order to maintain the integrity of the forward market and continue to provide sound hedging opportunities to market participants at the Belgian borders.