



EFET position on the draft EC congestion management guidelines (versions April and August 2004)

September 2004

Introduction

EFET welcomes the opportunity to comment on the draft guidelines again in advance of the 11th Electricity Regulatory Forum in Rome on 16 September 2004. We remain concerned that the guidelines do not adequately reflect the overriding principles laid down in the Cross-Border Exchanges Regulation (1228/2003) and do not give regulators and TSOs sufficiently tight guidance on how to observe those principles in practice.

Key issues for EFET members are:

- Maximising allocated capacity,
- Transparency and co-operation from and between TSOs,
- Market based capacity allocation mechanisms, and
- Market based congestion management.

These issues are all crucial to the goal that fully traded power markets are established throughout Europe. *Insufficient unbundling of transmission system operators and lack of open communication between them* remain core impediments to the establishment of robust traded markets. We expect these guidelines to make it clear that TSOs no longer have an option to restrict the transparency of system information provided to each other and to the market, nor to push congestion artificially to national borders. At worst a combination of non-market based allocation (or even some explicit capacity auctions) and common ownership of power generation and grids make international congestion management vulnerable to manipulation. We thus equally expect enhanced vigilance on the part of regulators in relation to observance of all provisions of the cross border Regulation.

Maximising allocated capacity

The April 2003 EFET paper entitled, “Recommendations for objective quantification and allocation of continental European cross border power transmission capacity” contained detailed discussion of capacity optimisation. Our recommendations are still relevant to the development of the guidelines; but they did not go far beyond the

obligations on TSOs, which can be inferred from the Regulation. We believe that significant progress towards optimisation can be achieved quickly, if regulators would seek immediate and effective implementation of the core obligation in the Regulation for TSOs to maximise the availability of capacity to the market.

Process of estimating NTC and ATC

We believe that the figures adopted by ETSO for NTC in the last three years are in many cases fundamentally flawed. TSOs need to develop and harmonise accredited, sophisticated predictive flow models which include objective approaches to capacities necessary for security, capacity reserved under legacy contracts, historical patterns and expected running of generation units in their control areas (especially predictions for “must run” generation) as well as demand expectations. They should result in full hourly, day-ahead exchanges of data and predictions between TSOs, including an open dialogue about corresponding expected flows. We are sure that a consistent and determined expansion of information sharing of this nature will lay a firm foundation for the true maximisation of capacity availability to the market. (It incidentally seems to us that the draft guidelines are drafted principally with co-ordination between two adjacent TSOs in mind, whereas maximising capacity in a meshed system requires pan-regional involvement. In the case of continental Western Europe it is essential that the guidelines contemplate extension of such co-ordination across non-EU borders such as those with Switzerland and Norway.)

In addition to exchange of information, TSOs should now be working closely with regulators to agree new methodologies, enabling a thorough revision of NTC and ATC values. Specifically, we believe that the use of a common PTDF model, as alluded to in the recent study commissioned by DG TREN and performed by Consentec and Frontier Economics (“Analysis of Cross-Border Congestion Management Methods for the EU Internal Electricity Market”, July 2004) will contribute to achievement of true maximisation. Regulatory involvement is essential for ensuring that the assessment of capacity occurs on a consistent basis, and that the information and processes used are transparent to the market. Procedures for detailed regulatory approval should be described in the guidelines.

TSO duties consequential upon the primary obligation to maximise capacity

We consider that further obligations on TSOs should be included in the guidelines, by way of clarification of what the process of maximisation must entail:

- An obligation to allocate intra-day any remaining capacity after year, month and/ or day ahead allocations have been honoured;
- The facilitation of cross border balancing;
- A key role in promoting and developing a secondary market;
- An obligation to offer firm capacity in such a manner that system operation risks are not attributed exclusively to system users. (For example, a TSO should not be permitted to curtail the use of transmission capacity, in order to avoid its own need to purchase generation reserve.)

Market based congestion management and capacity allocation mechanisms

Eliminating methods which do not entail some form of auction

We note that the draft guidelines do not in specific terms exclude allocation approaches such as ‘first-come, first-served’ and pro-rata methods. EFET considers such measures quite simply are not market based. Therefore the guidelines themselves and the accompanying explanatory memorandum should not entertain their inclusion in any form. Providing any scope for not implementing true market based mechanisms will encourage further fruitless argument on the meaning of ‘market based’ and could result in the ineffective implementation of congestion measures.

EFET supports the immediate implementation of truly market-based solutions, such as explicit auctions of forward capacity and/or transparent, flow based market-coupling. Transparent explicit auctions based on a realistic, progressive estimation of ATC will reveal the value placed on capacity, and ensure that capacity is allocated to those who value it most. Such auctions may also be a transitional tool to ensure that there will be sufficient capacity available to the market in the future: So that congestion is not perpetuated, income from capacity auctions should be used to improve the physical flow capacity, whenever this is an economically efficient option.

“Value revealing” congestion management approaches

Thus EFET continues to suggest explicit capacity auctions offer a pragmatic and fair solution to market participants at major continental congestion points. However, the design and implementation of multiple auctions is by no means an easy task. The use of exclusively explicit auctions in the meshed UCTE systems may eventually need to be limited to points of severe congestion. Transparency in availability of network, generation and demand data remains essential but very unevenly provided. Once transparency improves and market opening is completed, implicit auction methodologies are preferred for short-term allocation. Optimal power flows across bottlenecks (including national borders) should then be established technically by system operators and managed economically through a combination of co-ordinated re-despatch, counter- trade and market splitting (coupling), using day-ahead markets.

If market coupling and explicit auctions are to be used in parallel in relation to some borders, then careful attention will be required as to the split between the two methodologies. Competition policy considerations and the overall principles of objectivity and non-discrimination will necessitate a non-arbitrary approach to the allocation of capacity through power exchanges. For example, the allocation of a percentage of capacity organised by power exchanges, in accordance with day ahead bids for the underlying commodity, should not preclude the underlying long term capacity rights being sold in an explicit market over a longer time period.

Guaranteeing “use it or lose it”

EFET strongly urges a presumption in the guidelines in favour of allocations of potentially constrained capacity being firm. Article 6 of the Regulation states that curtailment procedures shall only be used in emergency situations and must be applied in a non-discriminatory manner. It goes on to specify that those market

participants, who have been allocated firm capacity, shall be compensated for any curtailment. However, it follow also that there can be a need for a market-based mechanism, to reallocate capacity in the event of congestion. Thus there should be a paragraph in the guidelines anticipating an arrangement, under which TSOs can buy back allocated capacity. “Recaptures of capacity”, subject to appropriate compensation by the affected TSO (whose cost of compensation should then be allowed in its regulated cost base), could be used more broadly in congestion management than is currently the case in continental Europe. It is useful also within national boundaries and for general system management in the case of power plant outages or unscheduled maintenance or transmission line works, as long as a TSO is given the correct tools and incentives by the regulator. EFET is currently preparing a position paper in which this approach will be explained further.)

A consequence of the application of a reallocation methodology can be the separation of system security criteria from the process of determining capacity to be allocated initially. That in turn can result in the provision of a further incentive for the TSO to allocate maximum capacity in an efficient manner.

Implementation of congestion management guidelines in tandem with security guidelines

Regulators should be acting to eliminate incentives for TSOs to restrict available capacity through over-cautious estimates of ATC, on the pretext of guaranteeing system security. To this extent Security Guidelines should be developed in parallel with the Congestion Management Guidelines.

In this parallel treatment, the highly sensitive issue of the so-called Transmission Reliability Margin – (“TRM”) must be addressed. As is well known, the total transfer capacity calculated between two control areas (TTC), is habitually reduced by an amount equal to the deemed TRM., Supposedly such reduction is designed always to accommodate unintended deviations attributable to primary and secondary control, as well as contingent needs for common reserve and for emergency exchanges., Standardisation of the calculation of TTC through such reduction in all circumstances is questionable. The calculation of the TRM remains completely opaque and at the discretion solely of TSOs and their representative organisations. To this extent, regulators will find it impossible to monitor the TSOs’ compliance with the obligation to maximise capacity

This regulatory *lacuna* must be addressed in the two sets of draft guidelines.

Role of regulatory bodies

The effective implementation of specific guidelines requires a greater level of scrutiny from regulatory bodies such as Member State regulators and the European Commission. For example:

- In ensuring that TSO coordination is as great as possible.

- Undertaking an audit and review of the approaches used by TSOs to determine available capacity, with all of the relevant information made public.
- Assessing the quality of TSO forecasting.
- By assessing and developing economic tools and incentive mechanisms to allow and encourage TSOs to manage the system in an economic and efficient manner.
- In ensuring that used definitions are consistently understood and applied throughout all Member States. (Market participants would value a clear statement on how Regulators will ensure that a multitude of interpretations do not emerge. Significant divergence will reduce the effectiveness of the Regulation.)

EFET calls for a new section of the guidelines spelling out the role which individual regulators, and regulators acting in concert across regions, are expected to play in the achievement of widespread compliance with the Regulation.

Other key principles

Timetable for nominations at borders and capacity allocation

We are dubious about the proposed timetable, starting two days ahead, for capacity nominations. As drafted it may reduce market flexibility, thereby increasing risks for market participants. EFET considers that the timetable should be shortened to at maximum one day. For intra-day purposes EFET prefers a permanent rolling timetable for capacity allocations and nominations (e.g. allocation in hour H for use of capacity in hour H+2). We are undertaking more work on harmonisation requirements in this area.

Use of congestion income

EFET has a preference for revenue to be used to guarantee the firmness of the allocated capacity.

Lack of precision in definitions

EFET has concerns about some subjective language used in the draft guidelines. This is particularly a problem in cases where TSOs and market participants may interpret the meaning differently, which would reduce the level of harmonisation. Some examples of areas needing improved definition are:

- ‘acceptable level’ in paragraph 1.2
- ‘significantly’ in paragraph 1.3
- ‘decreased firmness’ in paragraph 2.3
- ‘economically efficient level’ (explanatory note §3)

The development of comprehensive guidelines provides an important opportunity to facilitate the effective implementation of the Regulation. As the finalised guidelines may be difficult to amend, it is important to ensure that the initial guidelines are

drafted in such a way that leaves little room for differing interpretations and covers all the relevant areas necessary to encourage the development of the competitive market.

Annexes (on request):

- Position paper on congestion and allocation, April 2003
- Position paper on transparency of information, July 2003
- Marked-up version of the draft Congestion Management Guidelines

EFET, September 2004