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French-Spanish electricity interconnection capacity allocation: EFET welcomes new signs of progress

EFET welcomes, as a temporary measure, the announcement by the French Commission de la Regulation de l'Electricite ("CRE") on 10 October, that it has approved a revised, though still non-market based, allocation methodology for this interconnection capacity. This is in spite of our certainty that market based management of congestion is necessary at all European borders, to ensure that proper price signals are sent to the market, and to encourage either the construction of new generation and/ or transmission infrastructure or the shedding of load, depending on the relevant economics. (EFET has consistently since its foundation in 1998 advocated the use of market based methods of allocating any truly constrained transmission capacity inside and between TSO control areas. The desirability of using market-based methods on a cross border basis has been clearly recognized by participants in the Florence Forum since March 2000. They will be compulsory in the European Union from July 2004.)

Because of the lack of progress towards a permanent market based approach for allocation at the French-Spanish border, and even though all stakeholders agree about the need to put one in place, a majority of wholesale suppliers active in both countries, and belonging to EFET France and/ or EFET Iberia had proposed an alternative, temporary pro-rata mechanism earlier this year. RTE had expressed its willingness to immediately implement this mechanism if it were approved by the CRE. It involves an allocation pro-rated per transaction, with tranches of limited to a maximum of 25 MW for any one company (including its affiliates). This is similar to the system applied or soon to be applied on the interconnections from France to Belgium and Germany, where EFET France has also played an active role in reform discussions. It will allow, at least, a surer use of the interconnection by a larger number of market players, and may deliver some short-term economic efficiency improvement, pending introduction of a market based mechanism. Its implementation can now apparently be immediate, since it does not require any regulatory changes on the Spanish side.

The decision of the CRE follows a conference in Brussels about "Congestion Management and Market Power" organised on October 2nd by ETSO and the European Commission. This conference attracted around 250 representatives of TSOs, traders, suppliers, generators, power exchanges, regulators, universities, and large customers. **EFET used the opportunity of this gathering to organise a panel discussion about the interconnection between Spain and France in the early evening the same day.** Panellists were:

- Pierre Bornard, Chairman of Powernext and Director of system operation at French TSO, RTE
- Jean-François Conil-Lacoste, CEO of French power exchange, Powernext
- María Luisa Huidobro, Chairman and CEO of Spanish market operator, OMEL
- María Luisa Llorens, Director of market operation at Spanish TSO, REE
- Michel Massoni, Director of network access at French regulator, CRE

The session attracted around 45 representatives of entities active or interested in the Spanish and French power markets, and was moderated by Peter Styles, Chairman of the Electricity Committee of EFET.

Some facts emerged about the interconnection:

- Its capacity is small, representing no more than 3% of the peak demand in the Iberian system.
- About two thirds of this capacity is reserved for a long-term contract between REE and EdF, concluded prior to the liberalisation of both national markets.
- There are significant price spreads between Spain and France, and therefore the interconnection is heavily congested.
- The management of this congestion, in transactions from France into Spain, is, apparently, very complex, since it should combine the "first come, first served" rule applied by RTE with a market mechanism on the Spanish side (which integrates market bids with bilateral contracts).
- In reality only minimal quantities are authorised by comparing border schedules and effectively non- market based criteria (corresponding to "first come, first served") are applied to the remainder.
- The timing co-ordination for bids and nominations between the two markets is poor and discourages stronger competition for capacity, which would occur with co-ordinated application of the use-it-or-lose-it principle.
- It is a relatively simple interconnection, since only slight effects from neighbouring systems, and no loop-flows at all, are observed. Thus any capacity allocation mechanism could be implemented between the French and Spanish institutions without involving third countries.

Questions from attending representatives revealed widespread dissatisfaction in the wholesale power community about the current non-market based congestion management system. Frustration with lack of change was also clearly expressed by all the panellists. A proposal for reform was put forward jointly by REE and RTE *as long ago as the end of 2000* to implement a market-based mechanism applying on both sides of the border. The TSOs proposed explicit auctions for yearly, monthly and weekly allocations, outside the long-term contract between EdF and REE. Day ahead capacity then remaining would have reverted to despatch by OMEL under this proposal; at the time Powernext did not exist. The plan was readily accepted by the regulators in both countries and was supported by most market players. However, the necessary regulatory changes, to allow explicit auctions to be organised, have not been introduced in Spain.

With the more recent rapid development of liquidity on the French power exchange, it would now be feasible to implement a market coupling scheme. OMEL expressed its clear preference for this type of method in its presentation during the panel discussion, arguing that explicit auctions are discriminatory, increase market power and make international exchanges more difficult. REE and RTE, on their side, insisted that their explicit auction system is the only one which could be put in place in time for the deadline, imposed by the recently approved EU Regulation on cross border trade in electricity (July 2004). They suggested that the system could, within the deadline, be amended to involve the two power exchanges in jointly despatching spare day ahead capacity. Market players in the audience repeated that any market-based system would be better than the current impasse.

Despite the fact that calls for action, including suggestions of a binding timetable or the creation of a working group, heard from some stakeholder representatives, were not taken up by the panel members, most present felt the discussion was worthwhile. The need for moderation of unbending positions on implicit or explicit auction methods became clear. A revised, probably more efficient and fair, non-market allocation is immediately in prospect as a result of the CRE announcement on 10 October. With channels of communication re-opening, there is now also no reason why a new French-Spanish institutional consensus on a market based mechanism should not be built.

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