

ACER consultation on the harmonised allocation rules for long-term transmission rights



EFET response – 27 August 2021

The European Federation of Energy Traders (EFET¹) welcomes the opportunity to provide comments to the ACER consultation on the Harmonised Allocation Rules (HAR) for long-term transmission rights in accordance with Article 51 of Commission Regulation (EU) 2016/1719 of 26 September 2016 establishing a Guideline on Forward Capacity Allocation (FCA GL) and which was submitted to ACER for decision.

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.

¹ 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

Question 1: *Do you agree with the deletion of Article 59(5)? Please, substantiate your choice from (i) legal and/or (ii) economic point of view.*

We absolutely agree with deletion of Article 59(5). We trust that a cap on LTTRs remuneration is neither permitted by the FCA GL, nor economically justified or proportionate.

Legal viewpoint

Art. 59 EU HAR, which the TSOs seek to amend, deals with compensation for curtailments to ensure operation remains within Operational Security Limits before the DA firmness deadline (11:30 CET). The matter that the TSOs seek to address in their proposed paragraph 5 is out of scope of art. 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 DA firmness deadline – and not before

The remuneration of LTTRs, including in cases of decoupling, is tackled in art. 48 EU HAR. Art. 48.1(a) EU HAR foresees that LTTRs are remunerated at the DA market spread when DA 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 (explicit allocation as fallback of DA market coupling), then a modification of art. 48.1 EU HAR would be in order, rather than art. 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 of the EU HAR. Like art. 48 EU HAR, art. 35 FCA GL foresees that LTTRs are remunerated at the DA market spread when DA 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. Art. 54 FCA GL, which foresees the possibility for TSOs to established caps on compensation, only applies to curtailed LTTRs and can therefore not be used to amend art. 59 EU HAR in the direction pursued by the TSOs.

In summary, we see that the TSOs seek to amend the wrong article in the EU HAR, without a legal basis to do so in the FCA GL.

Economic viewpoint

For such a significant departure from the well-established principle of financial firmness of LTTRs, 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 does not have a detrimental impact on the allocation of LTTRs and their value, and eventually improves social welfare.

Regarding point (a) on the necessity of the measure, the TSOs present the remuneration of LTTR at the DA 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 corresponds to the average value of yearly and monthly LTTRs over the entire period covered by these products extrapolated for the individual days of decoupling) and, on the other hand, the revenues captured by the TSOs with the shadow auctions organised on three individual decoupling days in 2019, 2020 and 2021. These values are then compared to the remuneration of LTTRs to market participants for those three decoupling days.

We believe this approach is misleading. To get a fair representation of whether the TSOs have actually incurred an unbearable burden from the remuneration of LTTRs on days of decoupling, the TSOs should compare all benefits from the sale and expenditures from the remuneration of LTTRs over the same period of time, i.e. all the remuneration paid out to LTTRs holders, including during days of decoupling, compared to the total revenues from the allocation of cross-zonal capacity at different timeframes. We also believe that this analysis should be performed on an annual basis, at the very least for AC lines, as is the case for the calculation of the cap on compensation in case of LTTR curtailments.

As we are lacking information on TSOs congestion rent (either aggregated or per border) as well as on payouts to LTTR holders, the only numbers that we had at hand to perform some type of analysis – despite repeated requests – are those presented by the TSOs at the MESC and Florence Forum meetings of the spring of 2021. When reverse-engineering these numbers, we can observe that the LTTR payout on the decoupling event represented:

- on 07/06/2019: 2,8% of aggregated 2019 EU congestion rent (forward allocation only)
- on 04/02/2020: 0,9% of aggregated 2020 EU congestion rent (forward allocation only)
- on 13/01/2021: 2% of aggregated 2021 EU congestion rent (annual LTTRs allocation only)

The data presented by the TSOs shows that LTTR remuneration during days of decoupling was far from reaching the congestion rent they collect in each concerned year, even if looking only at forward allocation revenues (i.e. not taking account of additional transmission revenues from DA, ID or balancing). Of course, as we highlighted above, 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 miss an assessment by the TSOs of the effect that their proposed measure may have on the allocation of LTTRs and their value, as well as on social welfare in general. The wording used by the TSOs that firmness “would be reduced in case of decoupling” is once again misleading: indeed, changing the rules of LTTR remuneration 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.

Any change in the LTTR remuneration rules will be accounted for by market participants when they bid in long-term auctions. Hence, any reduction of firmness, in particular for events such as decoupling that market participants are unable to forecast or mitigate, will reduce the overall value they place in LTTRs, and are willing to pay for. This could significantly affect the revenues that TSOs capture from the sale of LTTRs all year round.

In addition, lower firmness of LTTRs will translate into less ideal hedging opportunities for market participants. All things equal, a lower risk coverage would translate into directly higher costs to hedge a specific risk on the market, costs which will ultimately be passed on to consumers.

The TSOs failed to assess the magnitude of both their loss of revenue from the allocation of diminished LTTRs for all delivery periods and the increase in the cost of hedging for the market. Whether these side-effects could counteract the objective of the TSOs to reduce payouts to LTTR holders during days of decoupling should have been properly analysed by the TSOs as part of their proportionality assessment.

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.

Question 2: *Do you have any other comments on the HAR methodology?*

As explained above, we do not believe there is an intrinsic problem in the remuneration rules for LTTRs in case of decoupling. They have been long negotiated between market participants, TSOs and NRAs back in the mid 2010s, and approved as part of the FCA GL. Ensuring full financial firmness of LTTRs is vital for market participants to conduct their operations. And this full firmness also guarantees a certain level of revenue for the TSOs from the sale of LTTRs.

We acknowledge the concerns of the TSOs with regard to what happened on the decoupling days of 2019, 2020 and 2021, and we do not disregard the financial consequences these days have had for a few individual TSOs. The low participation in shadow auctions that we have seen especially on the decoupling event of 07/06/2019 has triggered concerns on all sides. However, market participants are not responsible for decoupling events, nor have any way to control their occurrence. Hence, rather than seeking a change of the EU HAR and putting the financial burden of decoupling events on market participants, we invite the TSOs (and NEMOs, where relevant) to focus on the management of decoupling events, and investigate, in particular, the following directions:

- a) avoid decoupling events by reinforced testing/improvements of the SDAC process, including the algorithm and all communication processes.
- 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 day-ahead cross-border capacity allocated under a shadow auction process to better reflect the spread between the energy auction prices in each bidding zones.