

ACER Consultation on Forward Risk Hedging products & Harmonization of Long Term Capacity Allocation Rules

Response to the Public Consultation Document PC_2012_E_13

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CAO Central Allocation Office GmbH (“CAO”) welcomes this public consultation as it provides the opportunity for all stakeholders to present their views about the development of long term capacity allocation in the European market. CAO is deeply engaged especially in the area of capacity calculation principles as well as the area of explicit PTRs allocation (including the development of Allocation Rules and related processes). In particular, CAO gained valuable experience in the work of harmonizing auction rules when preparing the almost fully harmonized CEE auction rules (there are only differences in nomination timings) together with CEE TSO in 2010. Based on these records CAO provides its answers accordingly.

Although CAO cooperates on regular basis with market participants in order to offer the best possible services, we are certain that the results of the consultation will enable CAO to recognize some of the market participants’ requests more in detail and to further develop its services.

Question 1-5: no response provided

Question 6: **Would you like to change, add or delete points in this wish-list? If so, please indicate why and how.**

- **Background and Scope**

The wish-list does not contain a concrete description on the process which should be followed in order to achieve the “European Rules for Long Term Capacity Allocation”. Besides the definition of common requirements, it is also important that NRAs and TSOs agree on principles for the work on harmonization, e.g. principles for cooperation between concerned regions or countries. Auction offices usually have a central role in the development of auction rules. Thus, CAO would appreciate clear guidance for the future work.

Regarding the starting point for harmonization, CAO acknowledges that the structure of the HAR implemented in the Central-West and Central-South regions and Switzerland was the

basis for preparing the wish-list and performing the consultation. However, we recommend an open and transparent best-practice approach when it comes to the concrete work on harmonization. This would ensure an efficient involvement of all concerned parties and a good outcome.

- **Format of Auction Rules**

Incorporating border or country specific provisions into the main body of the Auction Rules disable or at least complicate the possibility of parties to distinguish which part of the document shall be subject to approval of all parties (affecting all parties) and which part are subject of individual/country specific approval. Moreover it is a question if an approach where all exceptions are incorporated to the main body of auction rules increase lucidity of the regulations or if it is vice-versa.

- **Auction Rules**

Auction Rules represent a contract between the Auction Office and the Auction Participant, i.e. especially set forth rights and obligations of the Auction Office and the Auction Participant. These rights shall be considered when modifying the Auction Rules.

Auction Rules and their changes shall be subject to approval by NRAs, TSOs and the Auction Office. The approval process shall enable smooth introduction of changes in a shortest possible time. Possibility to comment on the Auction Rules by the Auction Participants shall be ensured by the consultation process. Proposals of all parties shall be carefully assessed each time keeping the common interest of stakeholders to allocate transmission capacity in transparent and market oriented way in mind and also respecting the role of each party in the process.

- **Entry into force and consequences**

Harmonization of the rules shall accompany the changes of the platform (see response to question 22), therefore, should be respected also when deciding on the date of the new Auction Rules entry into force.

- **Fallback (to market coupling)**

Inclusion of such procedures depends on the fallback solution chosen for the respective MC procedure.

- **Entitlement**

Related to CAO, there is no need of a separate procedure for the registration of market participants interested only in the secondary market. The general requirements for the registration of participation in auctions are so basic that they cannot be further simplified.

- **Definitions, Suspension and withdrawal of the entitlement**

The definitions, suspension and withdrawal of the entitlement shall respect the framework of legal requirements given by governance law of the Auction Rules, which is determined (ideally) by the place where the auction office is registered. Apart from that CAO supports the idea of harmonization.

- **Fallback mode of yearly and monthly auctions**

Although CAO is ready to perform long-term auction in fallback mode and this process is supported by Auction Rules, CAO does not consider this issue critical as the auction can be postponed.

- **Contestation period**

Auction Participants have the possibility to check the Auction Results independently whether the contestation period is introduced or not and it is rather important what would happen if results are proven to be incorrect.

If the contestation period would be introduced the opportunity for market participants to challenge the auction results is clearly constrained only to this period. Taking the fact into account that the market participants usually make their decisions to buy or sell energy immediately after the auction results are published, CAO does not consider it practical to introduce the possibility to change the auction results during the contestation period.

CAO has serious doubts regarding the benefits of the contestation period and suggests to delete this point from the wish-list.

- **Resale**

CAO experience shows that the possibility to resell yearly capacity to monthly auction is not used (reference is made to 2011). CAO asked the traders in the CEE-region before removing the resale possibility yearly -> monthly for their opinion and received the following feedback - Conclusion of CAO Customer Advisory Committee 29 June 2011:

In case that an automatic resale (not nominated PTR is considered resold) is implemented, market participants do not find it necessary to have a resale to the monthly auction process, i.e. one general definition of resale from long term auctions to daily auctions in the Auction Rules is sufficient.

- **Nomination agents**

It is not clear to CAO why "The possibility for a capacity holder to delegate the nominations task to another entity must be part of the harmonized set of rules where nominations rules do not enable it." As it is not clear what will be the market players' benefit and as it would incur costs on side of CAO, we suggest to delete this point from the wish-list.

- **Valuation of Reductions in Held Capacities and of Cancellation of an Auction after the end of the Contestation Period**

Cancellation of an Auction after the end of the contestation period respectively after the publication of Auction Results is not foreseen by the CEE Auction Rules followed by CAO. CAO sees the introduction of such an option - moreover with a compensation limitation to 110% of the original payments by traders - as a limitation of market participants' rights. Therefore CAO suggest to delete this point from the wish-list.

- **Issuance of invoice and self-billing**

CAO agrees with the view of ACER that self-billing shall be supported – CAO provides this support to the majority of the registered Auction Participants. CAO however believes that it should only be introduced as an option which might be accepted by Auction Participants, since some market participants might be interested to keep the option to control the settlement process by issuing invoices on their own.

- **Payment Deposit/Recovery of payments:**

CAO is convinced that both, the deposit and the bank guarantee, shall be a form of collaterals accepted under harmonized Auction Rules. The collaterals are required to secure the access to electricity transmission capacities and the use of the respective rights, and to avoid a

misuse of the Auction Participant's rights (if the collaterals would not be requested or the requested amount should be underestimated an Auction Participant might distort the Auction Process/Auction Price without bearing appropriate financial consequences). Secure allocation is a prerequisite for an effective competition in the EU internal electricity market.

Both kinds of collaterals shall be accepted independently with respect to the product secured by these collaterals - it is not clear to CAO why ACER proposed to determine the amount of necessary collaterals depending on the way of providing the collateral.

Moreover it is not clear why according to ACER a dedicated bank account becomes a necessity to participate in the auctions. CAO uses one account for deposits of all Auction Participants for several years without a single problem – CAO does not see a reason to force market participants to open a bank account in the house bank of the respective auction office (and to force them to cover fees connected).

The concept of "promise of PTR" currently in place at CAO is at all not connected to the use of one bank account or individual bank accounts.

- **Duration and amendment of auction rules:**
CAO would be happy if the amendment and in particular NRAs approval process would be harmonized in order to ensure smooth changes of Auction Rules.

Also the idea to distinguish between the amendment of "core issues" and other issues where approval might be simplified will be welcomed by CAO although it is not fully clear how this categorization would be formally introduced.

- **Points to be added:**
VAT application - Clarity of rules for VAT application should be ensured, i.e. description shall be part of AR and shall be harmonized.

Information publication- CAO believes that requirements on published information should be harmonized (requirement for a list of anonymized bids published after each auction; Aggregated information on resold PTRs published after the nomination gate-closure/before the start of daily auction).

Examples - In order to increase the understanding of the processes by auction participants examples of auction algorithm, risk management, curtailment functioning should be part of the AR Annexes. This has proven to be useful in case of CEE auction rules.

Use of PTRs for delivery of Balancing Energy - CAO is convinced that the rules for a use of allocated PTRs for deliveries of Balancing Energy shall be harmonized/introduced if applicable taking into account also current work on design of cross-border balancing frameworks.

Question 7-10: no response provided

Question 11: Would allocating the products at the same time represent an improvement for market players? Why? Where, if not everywhere, and under which conditions?

It is CAO's understanding that the general goal of any harmonization and coordination is to apply the same procedures at the same time everywhere - if possible. Therefore CAO believes that the question should rather be "What are the reasons for not to allocate the products at the same time?".

However, to answer the question as it is posed in the consultation document - in order to ensure appropriate consideration of the interdependencies between capacities flow-based capacity calculation is to be introduced in daily and at least enhanced NTC (see more detailed explanation in response to question 12) in LT auctions. Such step consequently means that the capacity at the borders included in the enhanced NTC or flow-based shall be allocated in the same time – optimization across different borders takes place in both cases, i.e. allocation of capacity to the border which is valued the most as far as technically possible. Decision how capacities are shared between interdependent borders should be done transparently based on market conditions represented by bids, energy prices or in a similar way – not by an Auction Office or the TSOs.

In addition it shall be taken into account that a different timing of the allocation process also disables the possibility of an appropriate analysis of published prices as one cannot compare auction prices if allocation took place in another point in time – market conditions have changed in-between. Also, if capacities are not allocated at the same time we could hardly talk about optimal, but rather suboptimal solutions due to additional constraints introduced (capacities allocated on the borders where allocation process is finalized first represent additional constraints in allocation process for the rest of the borders). This decrease welfare gain achieved within allocation process.

Question 12: How important is it that capacity calculation for the long-term timeframe is compatible and/or consistent with the short-term capacity calculation and that capacity is interdependent and optimised across different borders?

First of all it is necessary to mention that interdependency of capacities is a matter of fact, which means that we are not sure how to interpret the question “How is it important that capacity is interdependent and optimized across different borders?”. The issue of interdependency can basically be approached in three ways: (1) by the flow-based method, which considers interdependencies directly during the allocation process – under way in CEE and CWE for day ahead allocation; (2) by enhanced NTC, which considers interdependencies directly during the allocation process – introduced in CEE by technical profiles representing the limit for more border connections/PSE O and 50HzT border/; (3) by a coordinated NTC method where the interdependency is assessed ex ante i.e. before the allocation process/bidding phase starts. The last option however considers interdependencies in the most restricted way where TSOs, based on in advance agreed rules, decide which part of capacity would be assigned to an individual border irrespectively to recent market needs.

Bearing in mind an equal treatment of market participants participating in LT or daily¹ allocation process, a high level of compatibility between timeframes is required. In addition, compatibility is an essential point in view of firmness of capacity. However, this does not exclude the possibility of the application of different methods as each method has some benefits and some drawbacks which need to be weighted with benefits of an ideal solution when one method can be used for all time frames.

The flow-based approach and the enhanced NTC are compatible in this context as both methods take the interdependencies between borders into account. CAO has gained experience with both methods on the long-term timeframe.

¹ In case of market coupling market participants participate indirectly in capacity allocation.

Question 13: Please indicate the importance of availability of different hedging products with respect to their delivery period (e.g. multi-year, year, semester, season) for efficient hedging against price differential between bidding zones. What do you think of multiple-year products in particular?

The products to be offered and splitting of capacity between the time frames should respect market needs and uncertainty of the transmission network capacity availability. We understand that market participants might be interested in multi-year products however, the more for a future time frame the product is allocated, the larger uncertainties and therefore a higher probability of curtailment exists (which then cannot be connected only to emergency situations but also e.g. to regular maintenance normally planned on yearly basis). Further, the more allocation products covering the same time period, the less capacity can be allocated per product which decreases liquidity.

Question 14: no response provided

Question 15: While products with planned unavailability cannot be standardised and harmonised throughout Europe, they enable TSOs to offer more long-term capacity on average than standardised and harmonised products would allow. Do you think these products should be kept in the future and, if so, how could they be improved?

Although the increased harmonization of the capacity calculation and harmonization is complicated by products with planned unavailability, we believe that also in the future these products should be kept as it enables to allocate more long term capacities. On the other hand CAO would recommend to introduce at least basic limitations for such a product formed in the way as e.g. duration of unavailability should not be longer than 30% of the product duration, maximum of unavailability periods within one product is 3 etc. – this would assure necessary user-friendliness and transparency of the process otherwise e.g. a 1 hour-product could be offered in a monthly auction process by notifying that for all other hours an unavailability is planned. The basic limitations can be introduced based on the market participants' and TSOs' discussion.

Question 16: Products for specific hours reflect market participants' needs. What should drive the decision to implement such products? How should the available capacity be split between such products and base load ones in the long-term timeframe?

CAO sees two possible drivers for the implementation of products for specific hours (e.g. peak) – (1) technical reasons: if on regular basis the amount of capacity during respective hours is significantly different than during other hours; (2) market needs. Taking especially the market needs into account, a well defined objective function and the optimization algorithm should enable allocation of different products within one auction, i.e. traders will decide by their bids on a split of available capacity between the products. This will be a similar approach as applied today by PX when clearing the orders in spot exchange and it is the only approach how to reflect actual market conditions directly in the allocation process.

Question 17-20: no response provided

Question 21: Looking at the current features offered by the different auction platforms (e.g. CASC.EU, CAO, individual TSO systems) and financial market platforms in Europe, what are the main advantages and weaknesses of each of them?

We believe that the platforms reflect the functionalities requested for the respective process (e.g. different capacity calculation and allocation methods, other functionalities specified by the auction rules) by TSOs and market participants of the respective region. Therefore any comparison needs to be done very thoroughly, considering also technical and commercial factors which are not visible to market participants. CAO recommends that when deciding on a single European platform very detailed and comprehensive analysis on specific issues, taking into account the needs and experience of market participants, shall be carried out to build a future European platform based on best practice of recent local platforms.

Question 22: How do you think the single auction platform required by the CACM Framework Guidelines should be established and organised?

It is the task of the TSOs and TSO designated entities (as CAO and CASC) to establish and organize the single auction platform since the allocation of cross-border transmission capacities is the responsibility of the TSOs.

- **How do you see the management of a transitional phase from regional platforms to the single EU platform?**

The implementation of a single European platform shall go hand-in-hand with the harmonization of long term capacity allocation rules, identification of TSOs' and market participants' requirements and with the phase out of the regional platforms.

- **Should current regional platforms merge via a voluntary process or should a procurement procedure be organised at European Union level (and by whom)?**

As expressed already in the answer to question 21 the platforms reflect requested functionalities to be provided for a respective process, i.e. it is very important to identify all TSOs' and market participants' requirements, functionalities and experience available now and then to find the most efficient way on how to get from the current local platforms to the single European one. Whether the procurement procedure would be necessary or not depends on the selected path for the single European platform.

- **Should the Network Code on Forward Markets define a deadline for the establishment of the single European platform? If so, what would be a desirable and realistic date?**

When deciding on a deadline for the establishment of the single European platform it is necessary to take into account that the implementation of a single European platform shall go hand-in-hand with the harmonization of the long term capacity allocation rules, identification of TSOs' and market participants' requirements and with the phase out of the regional platforms.