

ACER Decision on the harmonised allocation rules for long-term transmission rights: Annex II

*For information only*

## **Evaluation of responses to the public consultation on the harmonised allocation rules for long-term transmission rights**

### **1 Introduction**

On 25 July 2021, ENTSO-E submitted, ‘on behalf of all TSOs’, the amended ‘Harmonised allocation rules for Long Term Transmission Rights (‘HAR’) in accordance with Article 51 of Commission Regulation (EU) 2016/1719 of 26 September 2016 establishing a Guideline on Forward Capacity Allocation’ (the ‘Proposal for amendment’) to ACER for approval, pursuant to Article 5(2) of Regulation (EU) 2019/942.

In order to take an informed decision, ACER launched a public consultation on 19 July 2021 inviting all interested stakeholders, including ENTSO-E, regulatory authorities, TSO and market participants to provide comments on the Proposal for amendment. The closing date of the public consultation was 27 August 2021.

More specifically, the public consultation invited the stakeholders to comment on the proposed cap for remuneration of long-term transmission rights (‘LTTRs’).

### **2 Responses and ACER’s assessment of the responses**

By the end of the consultation period, ACER received comments from 14 respondents.

This evaluation paper summarises all of the respondents' comments and provides ACER's view on those comments.

In the present Decision, ACER concluded that the proposed cap on the remuneration of LTTRs introduced in Article 59(5) of the Proposal for amendment is not compliant with the FCA Regulation and lacks a sufficient legal basis. Therefore, the proposed cap could not be approved. For this reason, ACER deemed it not necessary and not appropriate to discuss conclusively the comments received regarding the cap on remuneration of LTTRs, as far as these comments concern non-legal aspects. The views of ACER, which are presented in the following with regard to the non-legal aspects of those comments should, therefore, be considered as preliminary findings.

Respondents' views	ACER views
<p><b>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.</b></p>	
<p>11 respondents (Eurelectric, Edison, Österreichs E-Wirtschaft, EDF, CRE, TIWAG, Europex, ČEZ, Energie-Nederland, EFET and AIGET) agree with the deletion of the remuneration cap for the following reasons:</p>	
<p>Legal viewpoints:</p> <ul style="list-style-type: none"> <li>- Compensation of capacity curtailments and remuneration of LTTRs are fundamentally different events taking place before and after, respectively, of the day-ahead firmness deadline and cannot be compared or assessed together.</li> <li>- The provisions determining the remuneration of LTTRs cannot illegally profit from being placed to a section covering the caps for compensation of capacity curtailments, just to enjoy the benefits of its provisions, because the FCA Regulation only allows the introduction of a cap on compensations. Article 35 of the FCA Regulation, as well as Article 48 of the HAR envisage the remuneration of LTTRs based on market spread, therefore no cap is possible.</li> <li>- A modification of the HAR to allow caps on the remuneration of LTTRs in case of decoupling would require amendments to the FCA Regulation.</li> <li>- The wording of Article 35(3) of the FCA Regulation clearly states that the prescribed remuneration regime is an obligation ('shall comply with', 'shall be equal to market spread'), which does not provide flexibility for alternatives.</li> </ul>	<p>ACER assessed the legal provisions of the FCA Regulation in its reasoning in the recitals of the present Decision and concluded that the inclusion of a cap for remuneration of LTTRs in the HAR lacks legal basis and that, consequently, the proposed cap could not be part of the HAR.</p>

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<p>Economic viewpoints:</p> <ul style="list-style-type: none"> <li>- The necessity for an introduction of a cap for remuneration in case of decoupling was justified by TSOs by the missing congestion income (i.e. the negative difference between collected congestion income from fallback explicit allocation and the remuneration of LTTRs), which has negative impact on consumers in terms of increased tariffs, but there are many other aspects and possible side effects not taken into account (increased hedging risks for market participants, lower future value of cross-zonal capacity resulting in lower collected congesting income).</li> <li>- Challenging firmness (by an introduction of a cap) could have detrimental effects on the market participants for the period of decoupling, as they cannot fully hedge themselves.</li> <li>- Challenging firmness (by an introduction of a cap) could have detrimental effects on the tariff payers, because TSOs could collect less congestion revenues from LTTR auctions due to a decrease in capacity prices caused by less reliable hedging.</li> <li>- An introduction of a cap for remuneration is not an appropriate solution to address the malfunctioning of shadow auctions (it is suggested to improve communication with the market participants and to train them more for being ready for such events).</li> <li>- TSOs present the remuneration during decoupling as overcompensation, but the approach is misleading, as they compare an average daily LTTR auctions' revenue against the revenue of a shadow auction during decoupling, while they should compare all the benefits and costs for auctioning and remunerating LTTRs, i.e. the yearly revenues compared to yearly remunerations.</li> <li>- The remuneration of LTTRs should be equal to the market spread to foster the efficiency of the LTTRs themselves.</li> </ul>	<p>The fact that the explicit auctions in case of fallback perform poorly should not be a reason to conclude that the remuneration mechanism has been set in a wrong way. Such finding should rather trigger an improvement of the fallback mechanisms.</p> <p>ACER finds that the reasoning provided by all TSOs misses some crucial parts that would enable the identification of possible side effects of the introduction of a remuneration cap. The TSOs omitted in their analysis some elements that could have detrimental effects on the markets. Firstly, the introduction of the remuneration cap would deteriorate the quality of hedging. This reduction of firmness could result in a decreased value of LTTRs and, in turn, lead to a decreased amount of the collected congestion income in the future. The TSOs described in their consultation input a situation, where the congestion income suffers a great loss during one day of decoupling, but the potentially decreased value of LTTRs would result in lower congestion income collected during every day of the year. This effect remains unexplained. Therefore, the detrimental effect to the end-consumers in terms of increased tariffs feared by the TSOs could occur</p>
<p>1 respondent (ENTSO-E on behalf of all TSOs) does not agree and would like to keep the remuneration cap for the following reasons:</p>	
<ul style="list-style-type: none"> <li>- Since the existing remuneration mechanism in case of an explicit fallback procedure does not rely on market fundamentals and the underlying price against which LTTRs are settled, the LTTRs remuneration is no longer representing the value of DA cross border capacity and cannot be considered as hedging opportunity against</li> </ul>	

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<p>DA congestion pricing in the meaning of the Electricity and FCA Regulations (i.e. the financial resale value of capacity). This non-correlation explained above usually leads to overcompensation of LTTRs holders because the revenues from the explicit fallback auction are not enough to cover the compensations due to market participants (i.e. 'missing money' issue). In such a case, LTTRs go beyond their objective as hedging product and provide a subset of market participants (i.e. those market participants having LTTRs on the borders subject to an explicit fallback auction) with unjustifiable overcompensation to the detriment of tariff payers.</p> <ul style="list-style-type: none"> <li>- Overcompensating market participants through the remuneration of LTTRs in case of fallback distorts the technical evolution of the transmission system in the EU and provides a disincentive to offer LTTRs.</li> <li>- The LTTRs remuneration mechanism is inconsistent with the objectives of the Electricity and FCA Regulations. The LTTRs remuneration mechanism is unlawful and in contradiction with the following governing principles of the operation of electricity markets:             <ul style="list-style-type: none"> <li>o the need for an orderly price formation of transmission capacities (i.e. market rules shall encourage free price formation and shall avoid actions which prevent price formation based on demand and supply);</li> <li>o the need to promote effective long-term cross-zonal trade with long-term cross-zonal hedging opportunities for market participants (i.e. the definition and objective of LTTRs);</li> <li>o the need to ensure fair treatment of TSOs and market participants (including consumers); and</li> <li>o the need to contribute to the efficient long-term operation and development of the electricity transmission system and electricity sector in the Union.</li> </ul> </li> <li>- It is to be highlighted that holders of the LTTRs have no incentives to participate in the fallback capacity auction, considering that LTTRs guarantee them quite generous payoffs that increase especially when the fallback mechanism performs poorly.</li> <li>- Nothing in the legal and regulatory framework prohibits the imposition of a remuneration cap to mitigate duly justified TSOs' and consumer's risks in case of decoupling events.</li> <li>- The last decoupling event caused around 24M€ of additional costs on society, because the holders of the LTTRs were remunerated by the market spread using explicit capacity allocation. This revenue inadequacy and non-correlation between the remuneration of LTTRs holders and market fundamentals is in clear contradiction with the principles governing the operation of electricity markets.</li> </ul>	<p>through the introduction of the remuneration cap.</p> <p>Secondly, the TSOs included in their analysis only one variable, which is the lost congestion income. The TSOs did not take into account the possibly increased costs of market participants to obtain additional hedging instruments to be fully hedged (as in the situation of no cap) and to obtain energy 'locally' in the absence of the possibility or the incentive to access cross-zonal capacity).</p> <p>ACER is of the opinion that the hedging opportunities for market participants should be provided in full scope and should not be limited by a potential application of a cap.</p> <p>Moreover, ACER would like to clarify that Articles 48(1)(c) and 59(1)(b) of HAR describe a situation, in which it is not possible to determine a price during implicit allocation, because at least one of the bidding zone's prices is missing. For such a situation the remuneration principles were not defined in the FCA Regulation and it was not clear which remuneration mechanism should be used for such an event (i.e. either the price of the initial LTTR auction or the price of the</p>

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<ul style="list-style-type: none"> <li>- ACER adopted Articles 48(1)(c) and 59(1)(b) to substitute LTTRs remuneration at the price of the initial auction with the one of the DA explicit auction. The argument put forward by ACER was the existence of a market price in (at least) one of the two relevant bidding zones (result from the fallback solutions) reflecting more adequately the price situation than the marginal price of the initial LTTRs auction. As this argument equally holds for Articles 48(1)(a) and 59(1)(a) of the HAR, TSOs called for a consistent revision of the HAR compensation rules to apply market-based prices for all the cases where they exist.</li> </ul>	<p>shadow auction). Therefore, as the legal background is clearly defined for the cap for remuneration in case of fallback, an analogy to the approach used for Articles 48(1)(c) and 59(1)(b) cannot be used.</p>
<p>2 respondent (IFIEC and RAP) do not take a direct position towards keeping or deleting the cap for remuneration but stress some principles that should be carefully evaluated:</p> <ul style="list-style-type: none"> <li>- An important prerequisite of a well-functioning market is a well-functioning fallback mechanism, which would prevent the creation of possible windfall profits for market participants.</li> <li>- A wrong setting of the fallback mechanism or the remuneration scheme would increase the negative income of TSOs. This would be reflected in tariffs to the detriment of the consumers.</li> <li>- A different remuneration cap could be envisaged, e.g. based on the value of lost load.</li> </ul>	<p>ACER agrees that the TSOs should focus on improving the fallback mechanism, in order to prevent negative financial consequences.</p>
<p>Other views:</p> <ul style="list-style-type: none"> <li>- The costs for remuneration should be paid by those, who are responsible for the decoupling event.</li> </ul>	<p>In the current legal and governance framework, where the day-ahead coupling is operated by all NEMOs, it is not possible to hold a single party liable for decoupling.</p>

Respondents' views	ACER views
<b>Question 2: Do you have any other comments on the HAR methodology?</b>	
<ul style="list-style-type: none"> <li>- NEMOs and TSOs should focus on preventing decoupling and if decoupling happens, on improving the communication with market participants and improving the competition during shadow auctions.</li> <li>- TSOs should focus on improving the fallback auction process so that it reflects the actual capacity price.</li> </ul>	<p>ACER agrees with the focus on preventing the decoupling events as the most efficient tool to achieve proper functioning of the market coupling. Nevertheless, it is clear that a fallback situation cannot be completely avoided. Therefore, all the market participants should be well trained and prepared to be able to efficiently take part of the fallback solution. This fallback solution should be continuously improved to secure a reliable and competitive approach.</p>
<ul style="list-style-type: none"> <li>- Article 9 Submission of information: The Single Allocation Platform should accept documents concerning the approval process e.g. commercial register excerpts at least in all official languages of Luxembourg or in all official languages of the EU.</li> </ul>	<p>The FCA Regulation does not define an obligation for the Single Allocation Platform to accept documents in all EU languages. Article 52(2)(b) of the FCA Regulation demands that the HAR includes provisions on the applicable language and Article 78 of HAR does fulfil that obligation by setting out English as the applicable language.</p>
<ul style="list-style-type: none"> <li>- Article 24 Modifications of Collaterals: 2) Fund withdrawals from the dedicated business account take too much time. The procedure requires sending a stamped paper and seems not to be very resilient against fraud, since paper and signatures are not fraud-proof. An electronic approval process with a good authentication standard can be used.</li> </ul>	<p>The Proposal for amendment focuses, among other topics, on the introduction of electronic signatures. Therefore, all TSOs covered the electronic approval process by the proposed amendments to HAR.</p>
<ul style="list-style-type: none"> <li>- Article 41-43 Transfer of Long Term Transmission Rights: The transfer of transmission rights between participants should be facilitated. A secondary market for transmission rights with frequent trading and price indications could increase the quality of FTRs as hedging instruments, in line with Article 3 of the FCA Regulation. But this cannot be achieved, unless FTRs are clearly exempted from financial instruments' regulation.</li> </ul>	<p>A creation of a secondary market, as well as the regulation of financial instruments are out of the scope of the HAR.</p>

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<ul style="list-style-type: none"> <li>- Article 32 Bid registration: The bid registration process should be reconsidered and the participant should receive a positive or negative confirmation, whether the issued bid is effectively placed in the auction system.</li> </ul>	<p>All market participants can access the list of accepted bids through a dedicated platform, therefore there is no need for an additional confirmation of rejected bids.</p>
<ul style="list-style-type: none"> <li>- Article 57 Process and notification of curtailment: All responsible balance groups in a bidding zone (not only the transmission rights holders) should be informed adequately, if capacity is curtailed, since this may severely change the prices in the Day-Ahead auctions.</li> </ul>	<p>All curtailments are reported on a dedicated platform in a way that should not allow for an unequal treatment of market participants and that should prevent a potential misusing of the insider information.</p>
<ul style="list-style-type: none"> <li>- Article 59(2) and (3): The cap-formula: We suggest to replace “Return” with “Return of FTRs”.</li> </ul>	<p>ACER clarified the word ‘Return’ and changed it in ‘Return of LTTRs’, as even the physical transmission rights can be returned.</p>
<ul style="list-style-type: none"> <li>- Article 76 Assignment and subcontracting: Outsourcing must not be the outsourcing of responsibility and liability. Subcontractors or parties that provide services for the Single Allocation Platform must have quality management systems in place, such that the participants receive the same system quality as otherwise offered by the allocation platform itself.</li> </ul>	<p>Delegating tasks does not lift the responsibility from the single allocation platform. The single allocation platform remains responsible for all services that are outsourced. These principles are set out in the FCA Regulation and do not need to be repeated in the HAR.</p>

### 3 List of respondents

Organisation	Type
AIGET - The Italian Association of Energy Traders & Suppliers	Association
CEZ, a.s.	Energy company
Commission de Régulation de l'Energie (CRE)	Regulatory authority
EDF	Energy company
Edison S.p.A.	Energy company
Eurelectric	Association
EFET- European Federation of Energy Traders	Association
Energie-Nederland	Association
ENTSO-E	Association
Europex	Association
IFIEC Europe	Association
Österreichs E-Wirtschaft	Energy company
Regulatory Assistance Project (RAP)	Association
TIWAG - Tiroler Wasserkraft AG	Energy company