

CRE consultation on the future of EU energy regulation



EFET response – 4 April 2019

We thank CRE for the opportunity to provide our views on the future of EU energy regulation. It is indeed important to us that national regulators are involved in the discussions leading to the adoption of new rules for the internal energy market, and closely monitor their implementation once approved.

Question 1: *What are, according to you, the challenges that the implementation of the new Electricity Directive and Regulation will pose?*

Like CRE, EFET generally welcomed the adoption of the recast Electricity Directive and Regulation. Both instruments have been agreed by the European Commission, Parliament and Council following long and constructive discussions that should ensure an ambitious and coherent application throughout Europe of the rules they lay out.

We particularly welcome in the Electricity Directive and Regulation – but also in other instruments negotiated as part of the Clean Energy Package (CEP), notably the recast Renewable Energy Directive – the **great emphasis placed on market mechanisms**, notably thanks to:

- the principle of free price formation (including doing away with price caps),
- the facilitation of market entry for all technologies and market participants,
- the application of balancing responsibility to all market participants (with some exceptions),
- the application of non-discriminatory access rules and transparency to balancing mechanisms and the energy market,
- the removal of barriers to cross-border transactions, including in the forward timeframe, and
- the reassertion of the unbundling principle.

We see a strong role for CRE in planning already now the implementation of these principles on the French market. This should include:

- in terms of free price formation: ensuring that the imbalance settlement price truly reflects the value of energy in real time by doing away with the k coefficient

- and the reference to day-ahead prices in aFRR pricing¹; designing a plan for the move to a 15-minute ISP and aligning day-ahead and intraday products on it;
- in terms of transparency: ensuring that the implementation of forward, day-ahead and intraday CCMs comes along with full transparency on the calculation process (incl. data input, algorithms and patches), taking lessons from the struggles faced by market participants in the functioning of CWE flow-based market coupling²;
 - in terms of unbundling and no-discrimination between market participants and/or technologies: ensuring that the TSO and the DSOs keep their roles of neutral market facilitators and procure services based on clearly defined needs to which the market can respond with the most competitive technologies³.

We also welcome the fact that **the CEP opens EU legislation to new types of technologies and market participants**. At EFET, we have always been supportive of making sure that all the non-regulated actors of the energy sector can be active on the energy market. Hence, we welcome the greater focus of the Package on electricity consumers (domestic, commercial and industrial), as well as on storage technologies. We are also happy to see that initial versions of the Directive text that granted network (and potentially financial) privileges to certain categories of new business model operators were reviewed during the negotiation process to ensure. Provisions on aggregators, for instance evolved from full privileged access to the market (including immunity from balancing responsibility) to a more balanced approach where aggregators are treated like any other market participant – at least as far as the wholesale market is concerned, some elements of privileged having been retained on the retail side.

Given our assessment on the ever-too-slow progress made on TSO-TSO cooperation and the non-transparent use by TSOs of congestion income from the issuance of transmission rights, we do not really share CRE's relief concerning the "flexibility" of European rules in these two areas. The same goes with regard to the establishment of capacity mechanisms and their design: we deplore the weakening of the European adequacy assessment; and as far as the design of mechanisms is concerned, many provisions have been introduced at the last minute in the negotiation process and obviously tailored for the French capacity mechanism, including on matters where we have expressed our serious concerns at multiple times⁴.

¹ EFET letter to CRE on the evolution of balancing mechanisms at European level and in France, dated 27 March 2019 and available at: https://efet.org/Files/Documents/Downloads/EFET%20letter%20CRE%20EU%20and%20FR%20balancing_27032019.pdf.

² For detailed information on this subject, see the EFET, IFIEC Europe and MPP open letter to CWE NRAs on flow-based transparency, dated 31 October 2018 and available at: https://efet.org/Files/Documents/Downloads/Market%20letter%20to%20NRAs%20CWE%20FBMC%20transparenc y_31102018.pdf, and the EFET response to the ACER consultation on the CORE CCM, dated 21 December 2018 and available at: https://efet.org/Files/Documents/Downloads/EFET_ACER%20consult%20Core%20CCM_22122018.pdf.

³ See notably the EFET reaction to the RTE RINGO project, dated 16 October 2017 and available at: https://efet.org/Files/Documents/Downloads/EFET%20reaction%20RTE%20RINGO%20project_16102017.pdf, and the EFET response to the CRE survey on battery storage, dated 28 February 2019 and available at: https://efet.org/Files/Documents/Downloads/EFET_CRE%20storage_28022019.pdf.

⁴ See notably the EFET paper on reform proposals to improve the current functioning of the French CRM and ensure effective participation of foreign capacities, dated 11 January 2018, available at: https://efet.org/Files/Documents/Downloads/EFET%20paper_French%20CRM_11012018.pdf.

Like CRE and many actors of the sector, we also deplore the **introduction of the “70% threshold”** in the provisions of the recast Regulation on capacity calculation. Our combined efforts to convince the European Parliament and Council that a threshold, whichever its value was a bad idea, that it ignored not only network but also economic reality all this obviously failed. For us, the approval of the threshold is the sign of a general frustration at political level of the extremely slow pace of implementation of the Third Package, and particularly of the provisions on capacity calculation. Since 2009, the TSOs have consistently violated Annex 1 of Regulation 714/2009 that prevented discrimination between internal and cross-border transactions, and regulators have not made them accountable for that. Ten years later, Capacity Calculation Methodologies (CCMs) are finally being approved at regional level, and still most of them completely ignore the principles of social welfare optimisation laid out in the ACER Recommendation 02/2016. Collectively, regulators, TSOs and market participants involved in this Third Package implementation process, we bear the responsibility of this lengthy process and of the political response to our lack of reactivity in the completion of the IEM, which took the form of the 70% threshold, a simplistic solution imposed on a complex question.

Now, the context being what it is, we will have to live with this threshold. Whether as of 2020 or gradually until 2025, the threshold will need to be applied. For this, we should make sure that throughout Europe, TSOs implement the recast Regulation in the same manner. Despite lengthy discussions between the three main EU institutions, the text of the recast Regulation is not fully clear on the reference used to apply the threshold, nor on the elements of capacity calculation that need to be taken into account in the 70% or not. With this in mind, EFET started a dialogue with ENTSO-E to ensure that proper guidance is provided to the TSOs for the application of the EU rules. We would welcome the involvement of regulators, including CRE of course, in this exercise. It is important that regulators are well prepared and contribute to the proper and timely application of the threshold. With the adoption of the threshold, we have seen how the lukewarm engagement of some regulators and their leniency towards TSOs' reluctance to apply certain EU rules can backfire, so it is now time to be more rigorous.

Of course the application of the threshold may pose challenges to governments, regulators, TSOs and market participants. The cost of remedial actions to guarantee a high level of cross-border transmission capacity will likely increase. But it will be the occasion to bring more transparency on these costs – many of which are internalised at the moment, if not hidden in some markets, notably in France. It will also be the occasion to also assess the value of increased cross-border trade. And in the end, we may get away from the perspective that has prevailed until now on the question of capacity calculation and the use of remedial actions, i.e. one largely focused on the balance sheet of TSOs rather than on social welfare creation as a whole. Through full transparency on capacity calculation and the use of remedial actions – including the labelling of lines as CNEs in flow-based market coupling or the opaque use of balancing merit orders for congestion management purposes – we may get to a point where regulators would be able to actually apply the ACER Recommendation 02/2016, and possibly convince Member States for the next review of the recast Regulation of a more economically efficient form of capacity calculation than that imposed by the threshold.

Question 2: *Do you share CRE's positive assessment of market design as provided by the current legislation and the way it is applied in France? In your opinion, what are the essential points that the future "gas package" should cover? On these points, which concrete evolutions do you call for, and for which reasons?*

We generally share CRE's positive **assessment of the current market design in France**. The implementation of the EU and French legislative framework in the gas sector has proved more straightforward and scrupulous than in the electricity sector. This is notably to put to the credit of the TSOs – for instance in their inclusive conduct of the zones merger – and CRE itself – in its strong support for a market based solution for storage procurement. The TSOs and CRE created a fruitful environment of dialogue and trust with market participants.

As far as the gas zones merger is concerned, we support the objective to create a national price discovery location, allowing easier access to the French market. The reform was conducted in a constructive manner and perfectly on time. It is however too soon to tell if the balance of infrastructure investments and flow commitments works for the management of summer as well as winter constraints. The reform of storage procurement is very positive, and as shown by the subscriptions for 18/19 and 19/20 storage years, the competitive approach that the Government finally implemented to trust in delivers both on cost efficiency and security of supply.

This rather positive outlook should not make CRE forget about current challenges: we harbour serious concerns with the **review of the gas tariffs in France** just launched by the regulator, notably when it comes to its compliance with the NC TAR and the risks it poses for open interests of market participants. Our biggest concern in this area is that the new transportation tariffs (ATRT 7) will not be finalised and published before the auctions for the next gas year 2019-2020 (as provided by NC TAR). As we noted in our response to the CRE consultation on the evolution of the tariff regulation for infrastructure operators in France⁵, it is of particular concern considering that, if the new tariff period were to commence in April 2020, it exposes the French gas system to higher regulatory uncertainty with respect to ATRT6 tariffs, which may become subject to legal challenges as the general reliability of French gas transmission tariffs would diminish. Transactions have been concluded on the basis of the ATRT6 tariffs and ignoring these open interests in the market would threaten them and the confidence that the market has in the – so far – reliable regulatory framework in France. Moreover, we noticed that the timeframe provided by this consultation document does not seem to meet the deadline set by Article 27, §5 of the NC TAR which states that “the procedure consisting of the final consultation on the reference price methodology [...], the decision by the national regulatory authority [...], the calculation of tariffs on the basis of this decision, and the publication of the tariffs [...] shall be concluded no later than 31 May 2019”.

With the European elections coming up and the start of a new European Commission in the fall, we are indeed likely to see a **new Gas Package** tabled on the European legislative agenda rather fast. Like the Clean Energy Package, it will likely be a

⁵ EFET response to the CRE consultation on tariff regulation applicable to infrastructure operators in France, dated 3 April 2019 and available at: https://efet.org/Files/Documents/Downloads/DRAFT_EFET_CRE%20tariffs%20framework_03042019.pdf.

combination of review/reinforcement of existing market rules and opening towards new areas/technologies of the sector. We are happy to see the Madrid Forum provide input to the European Commission on a number of these new subjects. It is indeed important that the discussion involves European and national policy makers, regulators, TSOs and market participants.

We definitely support studies on the future role of gas, including questions of sector coupling and the integration of renewable and low carbon gases, to see how the gas sector can also contribute to the EU and national environmental objectives on a level-playing field with other technologies. Once this study phase is over, it will be important to reflect on the positive and negative experience of renewable electricity development to avoid undue market interferences and ensure that new projects are assessed based on the full spectrum of their benefits (including environmental), but also their costs. The regulator will have a key role to play to provide full transparency on these initiatives. CRE should also be highly proactive in the process underway to develop a pan-European green gas certificates trading scheme, which would enable such certificates to be tradable and transferable across EU repositories.

We would welcome greater **convergence of gas and power regulation** where it makes technical and economic sense. We see good opportunities for that when it comes to licensing requirements for instance, where the administrative burden on gas trading companies is much heavier than that of their power trading counterparts for no clear reason. In other areas, such as tariffs or the treatment of grid investment, we see how the sector coupling discussion pushes for a convergence of regulation, so that the power and gas sectors can contribute equally to the energy transition. But the regulator will need to tread carefully on those questions, so as not to disrupt abruptly the sector and endanger the viability of companies and system operators.

Question 3: *Do you believe that the Regulation on trans-European energy infrastructures (n ° 347/2013) should be revised? If so, what changes would you recommend?*

The development and proper maintenance of infrastructure is key to the functioning of the internal markets in both electricity and gas. However, this should not result in a blank check for system operators to invest in infrastructure at any cost. At EFET, we have always supported a **reasoned approach to new infrastructure investment**: before investing in new cables or pipelines, system operators ought to make sure that existing infrastructure is used at its economic optimum, and that any new investment is supported by a sound economic analysis. Considering the natural financial interest in growing the asset base on which they are remunerated, regulators have a key role to play in scrutinising any new investment project and challenging system operators when the economic benefits of a project are not apparent.

We have recently seen infrastructure projects proposed by TSOs in France that were not supported economically, most notably the HVDC power cable in the Bay of Biscay, and the STEP gas pipeline project. Both projects aimed at increasing the interconnection between France and the Iberian Peninsula. In the first instance, the current rate of use of the existing France-Spain power interconnection, and the suggestions made by RTE on the incentive regulation for the new HVDC cable (with

very low rates of use) both indicated the lack of necessity – or at the very least the over-dimensioning – of the new project. The Bay of Biscay cable project was nonetheless approved by CRE – albeit with more stringent incentives than what RTE had proposed. Instead, we expected the regulator to challenge the TSOs on both sides of the border on their use of the existing infrastructure, and possibly advise a review of the scale of the project⁶. In the case of the STEP project, a disappointing open season and a negative cost-benefit analysis did not prevent the European Commission to include the prospective new pipeline on the list of PCI projects. But there, we were happy to see the French and Spanish regulators reject the project on the basis of a lack of economic interest for it⁷.

While we note the political push at European level to increase interconnections between Member States – through **the famous 10%, now 15% cross-border interconnection target** – we see regulators as the guarantors of a sane reflection on this question. Having cables in air and pipelines in the ground is not an objective as such. It neither contributes to security of supply, affordability of energy, or sustainability. Appropriately using these cables and pipelines and making them available to the market is what matters. Regulators have a double role to play here: educating decision makers at governmental level about the complexity of the topic; and making sure that the market design, including capacity calculation, issuance and firmness of transmission rights, and transmission tariffs, allows the economically optimal use of existing infrastructure. Only regulators are in a position to do this, to make sure in the end that consumers do not finance unnecessary infrastructure.

As far as a **possible review of Regulation 347/2013** is concerned, it is important to us that projects, even those primarily focusing on ensuring security of power or gas supply, are only included in the PCI list if they are backed by strong commercial interest.

In the process itself to define this PCI list, the final selection of projects on the European Commission side lacks transparency, casting a shadow on the results of the whole process. In the example of the STEP project, a derogatory process was been implemented, with an ad-hoc cost benefit analysis made by an independent consultant. This is challenging the requirement that the European Commission placed on itself that all projects should be analysed on an equal footing, i.e. through the same methodology.

A review of Regulation 347/2013 should include full transparency on the selection process and stringent methodologies, so as to reinstate trust in the whole PCI selection process. Clear and transparent cost benefit analyses must be published, and if these analyses are negative, no socialisation of costs should be granted to these projects.

⁶ For more thoughts on this project, see the EFET response to the CRE consultation on the incentive framework for infrastructure investment projects at the French-Belgian and French-Spanish borders, dated 23 February 2018 and available at:

https://efet.org/Files/Documents/Downloads/EFET_CRE%20consultation%20infra%20incentives_23022018.pdf.

⁷ For more thoughts on this project, see the EFET response to the CRE consultation on the TYNDPs of GRTgaz and TIGF, dated 7 December 2017 and available at:

https://efet.org/Files/Documents/Downloads/EFET%20response%20CRE%20consultation%20TYNDPs_07122017.pdf.