

**Approval by Energitilsynet and
Energimarknadsinspektionen**

of

**Energinet's and Svenska Kraftnät's proposal for
arrangements to ensure cross-zonal risk hedging
opportunities in accordance with article 30 of the
Commission regulation (EU) 2016/1719 of 26
September 2016 establishing a guideline on forward
capacity allocation**

3 May 2018

I. Introduction and legal context

This document elaborates an agreement between Energimarknadsinspektionen (“Ei”) and Energitilsynet (“DERA”) on 3 May 2018, on Energinet’s and Svenska Kraftnät’s proposal for arrangements to ensure cross-zonal risk hedging opportunities in accordance with article 30 of the Commission regulation (EU) 2016/1719 of 26 September 2016 establishing a guideline on forward capacity allocation (“Regulation 2016/1719”).

This document is intended to constitute the basis on which Ei and DERA will each subsequently make national decisions pursuant to approve the proposal. The legal provisions relevant to the submission and approval of the proposal, and this regulatory authority agreed opinion, can be found in Articles 3, 4 and 30 of Regulation 2016/1719. They are set out below for reference:

Article 3 of Regulation 2016/1719:

This Regulation aims at:

- (a) promoting effective long-term cross-zonal trade with long-term cross-zonal hedging opportunities for market participants;*
- (b) optimising the calculation and allocation of long-term cross-zonal capacity;*
- (c) providing non-discriminatory access to long-term cross-zonal capacity;*
- (d) ensuring fair and non-discriminatory treatment of TSOs, the Agency, regulatory authorities and market participants;*
- (e) respecting the need for a fair and orderly forward capacity allocation and orderly price formation;*
- (f) ensuring and enhancing the transparency and reliability of information on forward capacity allocation;*
- (g) contributing to the efficient long-term operation and development of the electricity transmission system and electricity sector in the Union.*

Article 4 of Regulation 2016/1719:

- 7. TSOs responsible for establishing the terms and conditions or methodologies in accordance with this Regulation shall publish them on the internet after approval by the competent regulatory authorities or, if no such approval is required, after their establishment, except where such information is considered as confidential in accordance with Article 7.*

Article 30 of Regulation 2016/1719:

- 1. TSOs on a bidding zone border shall issue long-term transmission rights unless the competent regulatory authorities of the bidding zone border have adopted coordinated decisions not to issue long-term transmission rights on the bidding zone border. When adopting their decisions, the competent regulatory authorities of the bidding zone border shall consult the regulatory authorities of the relevant capacity calculation region and take due account of their opinions.*
- 2. Where long-term transmission rights do not exist on a bidding zone border at the entry into force of this Regulation, the competent regulatory authorities of the bidding zone border shall adopt coordinated decisions on the introduction of long-term transmission rights no later than six months after the entry into force of this Regulation.*
- 3. ..*
- 4. ..*

5. *In case the assessment referred to in paragraph 3 shows that there are insufficient hedging opportunities in one or more bidding zones, the competent regulatory authorities shall request the relevant TSOs:
 - (a) *to issue long-term transmission rights; or*
 - (b) *to make sure that other long-term cross-zonal hedging products are made available to support the functioning of wholesale electricity markets.**
6. *In case the competent regulatory authorities choose to issue a request as referred to in paragraph 5(b), the relevant TSOs shall develop the necessary arrangements and submit them to the competent regulatory authorities' approval no later than six months after the request by the competent regulatory authorities. Those necessary arrangements shall be implemented no later than six months after approval by the competent regulatory authorities. The competent regulatory authorities may extend the implementation time upon request from the relevant TSOs by a period of no more than 6 months.*
7. *Where regulatory authorities decide that long-term transmission rights shall not be issued by the respective TSOs or that other long-term cross-zonal hedging products shall be made available by the respective TSOs, Articles 16, 28, 29, 31 to 57, 59 and 61 shall not apply to the TSOs of the bidding zone borders.*
8. *Upon a joint request of the TSOs on a bidding zone border or at their own initiative, and at least every 4 years, the competent regulatory authorities of the bidding zone border shall perform, in cooperation with the Agency, an assessment pursuant to paragraphs 3 to 5.*

Regulation 2016/1719 went into force on the 17 October 2016.

II. Background

Pursuant to article 30, TSOs on a bidding zone border shall issue long-term transmission rights unless the competent regulatory authorities of the bidding zone border have adopted coordinated decisions not to issue long-term transmission rights on the bidding zone border.

On all the Swedish-Danish bidding zone borders, transmission rights did not exist on these borders upon entry into force of Regulation 2016/1719. The competent regulatory authorities, Ei and DERA, therefore carried out in a coordinated manner an assessment of hedging opportunities in the concerned bidding zones in accordance with article 30(3).

The Danish assessment showed that there were insufficient hedging opportunities in DK1 and DK2. Thus, Ei and DERA coordinated decisions to request the relevant TSOs, Svenska Kraftnät and Energinet to make sure that other long-term cross-zonal hedging products are made available to support the functioning of the wholesale electricity markets.

Energinet and Svenska Kraftnät have coordinated the necessary arrangements and on 17 November 2017 the proposal was sent to Ei and DERA for approval. This was within the deadline stated in article 30(6) of Regulation 2016/1719.

III. The proposal

The main elements of the proposal are:

- Long term transmission rights on the DK1-DK2, DK1-DE, and DK2-DE bidding zone borders are to be made available with the objective to improve hedging opportunities in DK1 and DK2.
- Energinet and Svenska Kraftnät have evaluated alternatives to long-term transmission rights. In summary, long-term transmission rights have been chosen due to the following conclusion from TSOs' explanatory document:
 - Known setup
 - Flexible solution
 - Lowest risk of over implementation
 - Most cost efficient
 - Ensures TSOs live up to obligation to ensure hedging possibilities
 - Connecting illiquid DK markets to very liquid DE market
 - Trust in TSOs are not affected like with the EPAD products
 - No risk of splitting EPAD products on more exchanges as with the Market Maker product
- The TSOs shall publish the arrangements to ensure hedging opportunities without undue delay after regulatory approval.
- The implementation of the arrangements will be done no later than six months after regulatory approval.

The Energinet and Svenska Kraftnät proposal has not been subject to formal consultation by the TSOs, but the TSOs have jointly held a workshop 12 September 2017, where several ideas were debated with market participants. DERA has held a national Danish consultation from 30 November 2017 to 8 January 2018, the input from this will be debated in DERA's national decision.

IV. Regulatory Authorities position

Ei and DERA find that Energinet and Svenska Kraftnät have followed all formal requirements in article 30 of Regulation 2016/1719.

When assessing the proposal from the TSOs, Ei and DERA have taken into account that article 30(5)(b) does not specify “*other long-term cross-zonal hedging products*”. In fact, the only basis for determining “*other long-term cross-zonal hedging products*” is, in particular, pursuant to the objective of article 30, that the proposed measures shall ensure efficient hedging opportunities in the bidding zones where there has been found to be insufficient hedging opportunities as well as the objectives in article 3 of Regulation 2016/1719.

Ei and DERA also consider that the goal of ensuring efficient hedging opportunities in the Danish bidding zones can be achieved by incorporating and applying all borders to a bidding zone, and not just one bidding zone border.

Therefore, the NRAs assess the proposal with regards to how the proposed measures:

1. support the functioning of wholesale electricity markets (ensure efficient hedging opportunities),
2. promote effective long-term cross-zonal trade with long-term cross-zonal hedging opportunities for market participants,
3. provide non-discriminatory access to long-term cross-zonal capacity,
4. ensure fair and non-discriminatory treatment of TSOs, the Agency, regulatory authorities and market participants, and
5. contribute to the efficient long-term operation and development of the electricity transmission system and electricity sector in the Union.

It should be noted that Energinet and Svenska Kraftnät are not formally proposing – with this proposal – to increase the capacity on DK1-DE, DK2-DE and DK1-DK2 bidding zone borders. The proposal should be seen in the context of the CCR Hansa TSOs’ proposal to shift from physical transmission rights to financial transmission rights on DK1-DE and DK2-DE bidding zone borders.

The CCR Hansa TSOs expect that this shift could enable them to offer more capacity to the market. However, the precise amount of long-term capacity offered to the market is subject to forthcoming proposals from CCR Hansa and CCR Nordic in accordance with article 10 of Regulation 2016/1719. These proposals are expected to be submitted for approval in January 2019. Therefore, the proposal discussed here should be seen in a wider context.

Increasing the capacity on long-term transmission rights towards Germany or between the Danish zones will give market participants the possibility to hedge price differences between Danish and German DA prices. A market participant can enter into a German forward contract together with LTRs towards Germany. German forward contracts have reference to the German DA price. The LTRs pay out the difference between German and Danish DA prices. Therefore, with this combination, an EPAD is not needed, and the much more liquid German forward market is used instead. Limited capacity on the German – Danish borders need not be a problem, since e.g. a Danish producer and consumer could enter into a bilateral agreement on a fixed price. So, not all transactions need to refer to exchange traded forward products.

It should be noted that the proposal is not expected to enhance EPAD liquidity for the Danish bidding zones. Energinet and Svenska Kraftnät write that “*Long-term transmission rights will not as with the EPAD products increase the EPADs directly in the market. This is on the other hand also not the aim*”

of the TSOs. The TSOs shall ensure arrangement that increases the risk hedging opportunities in the two Danish markets.”

In summary, Ei and DERA are of the opinion that Svenska Kraftnät and Energinet are proposing a pragmatic solution that increases the likelihood that hedging opportunities in DK1 and DK2 are improved.

Furthermore, Ei and DERA emphasize that article 30(8) states that the competent regulatory authorities shall perform an assessment of the liquidity in the bidding zones at least every 4 years. Thus, the effect of the proposed measures will be subject to an assessment within at least 4 years.

V. Conclusions

Ei and DERA have assessed, consulted and coordinated and closely cooperated to reach an agreement that the proposal for arrangements to ensure cross-zonal risk hedging opportunities in accordance with Regulation 2016/1719 article 30(6) meet the requirements of Regulation 2016/1719 and as such can be approved.

The necessary arrangements proposed by the TSOs shall be implemented no later than six months after the approval by Ei and DERA in accordance with article 30(6) of Regulation 2016/1719.

Following national decisions taken by Ei and DERA, Svenska Kraftnät and Energinet will be required to publish the methods on the internet in line with article 4(13) of Regulation 2016/1719.