Introduction of the allocation of Financial Transmission Rights (FTRs) Options instead of Physical Transmission Rights with UIOSI (Use It or Sell It) for long term transmission rights on Belgian Borders

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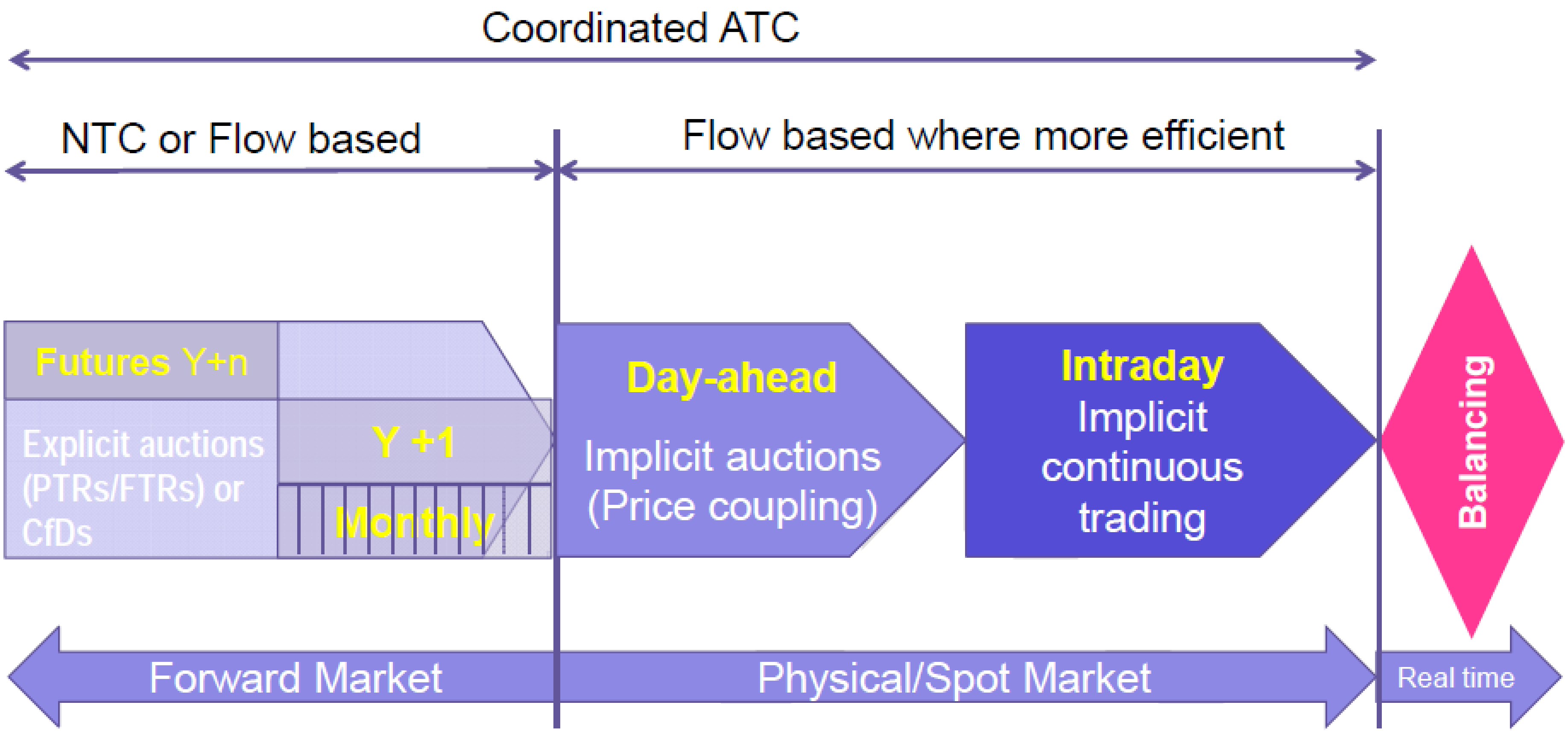
EUROPEAN TARGET MODEL



The European Target Model was designed to provide efficient Cross-Border Congestion Management on forward, Day-ahead and Intra-Day timeframes. It was assumed to be part of a general market design based on energy-only markets in a zonal approach.

WHAT ARE FINANCIAL TRANSMISSION RIGHTS OPTIONS (FTR OPTIONS)?

- Definition based on ENTSO-E's second edition of the Network Code on Forward Capacity Allocation : "Financial Transmission Rights Option means **a right entitling its holder to receive a financial remuneration based on the Day Ahead Market results between two Bidding Zones during a specified period of time in a specific direction."**

- The only feature that is different between FTRs Options and Physical Transmission Rights with Use It Or Sell It (PTRs with UIOSI) **is the elimination of the nomination process** when introducing FTRs Options:

  - <u>PTRs with UIOSI:</u> holder has the option to either nominate in order to use its Long Term Cross Zonal Capacity or to receive a financial income based on the positive (if any) Day Ahead Market price differential

  - <u>FTRs options</u>: holder receives a financial income based on the positive (if any) Day Ahead Market price differential

- With the introduction of FTR Options the link with the underlying physical cross zonal capacity is fully maintained

ADVANTAGE OF FTR OPTIONS

Operational: simplified process (no nomination, matching and capacity adjustments steps) and reduced operational risks

Market

- Because all capacity would be given to DA (no nominations) this would create more liquidity on the spot (potentially leading to: better price formation, better DAMC results and more price convergence).
- Expected increase in competition on Transmission Right markets as it will be easier to enter the market (BRP contract is no longer relevant for this timeframe)
- Reduction of operational risk at TSOs lead to more robust market process for market parties

Flow-Based

- Mitigating the impact of difference in shape of the FB domain with the ATC based long-term rights domain
- FTR options allow an earlier publication of FB parameters (without having to develop an additional publication step "before LT adjustment", as currently added in the context of transparency discussions)

DISADVANTAGES OF FTR OPTIONS

Market

Market participants' must use power exchanges for their physical cross-border transactions

NRA REQUIREMENTS FOR FURTHER IMPROVEMENTS OF THE CWE FLOW BASED METHODOLOGY

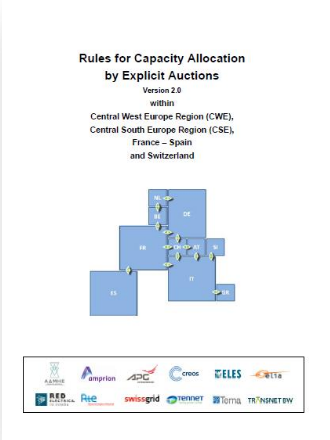
- FTR Option implementation at least at Belgian borders is a requested as one of the methodological improvements by the CWE NRAs in the framework of the approval of the FB implementation :
- **Common Position Paper of CWE NRAs on Flow-Based Market Coupling :** “The implementation of FTR Options, already asked years ago by CWE NRAs, is considered as the enduring solution, at least on the Belgium-France and Belgium-Netherlands borders, for mitigating the impact of difference in shape of the FB domain with the ATC based long-term rights domain.”

EU FINANCIAL REGULATORY FRAMEWORK & CROSS ZONAL CAPACITY PRODUCTS

- The basic element of the European Financial Regulatory Framework is the **definition of a financial instrument** → The Markets in Financial instruments Directive: MIFID I and MIFID II legislations provide this definition of a financial instrument.
- All legal opinions (ENTSO-E, CWE and informal input of several national assessment) indicate that in the framework of MIFID I and II, PTRs with UIOSI and FTRs Options are regarded as the **same products**. **MIFID regulation applies or does NOT apply for both types of LT TR**.
- There are diverging legal opinions regarding the qualification of FTRs Options and PTRs with UIOSI as a financial instrument.
- RECENT DEVELOPMENTS: the **TSO community** (including their allocation offices) would be **exempted from all financial legislation** for all products including FTR options as long as it concerns **trading on the primary market**. The EC have indicated they would integrate this exemption **in their final delegated act on the definition of a financial instrument**, however this will only be confirmed once the delegated act of the EC is finalized and adopted (indicative deadline: Q3-2015). This delegated act needs to be approved by the European Parliament and Council 3 months after submission by the EC (extendable with 3 months). So this issue will be **clarified in the worst case in March 2016** but until then TSOs will assume that no specific action is needed here

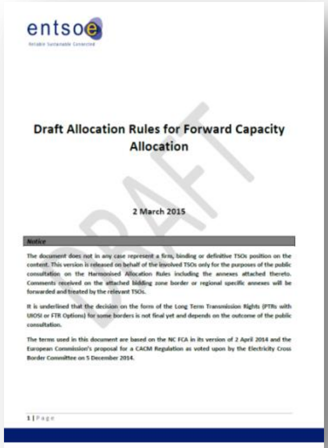
EU HARMONIZED AUCTION RULES (NC FCA) OR INTRODUCING THE POSSIBILITY TO ALLOCATE FTR OPTIONS

- No later than twelve months after the entry into force of NC Forward Capacity Allocation, harmonized allocation rules for LT TR are required.
- Current situation: no single set of harmonised rules for LT TR trading across European bidding zone borders.
- NRA approval of ENTSO-E pilot project “European Harmonized allocation rules – EU HAR” in September-October 2015 in order to become applicable for long term transmission right products with delivery from 1st of January 2016 on (i.e. likely prior to NC FCA entry into force). **The approval by the relevant NRAs implies the introduction of FTR Options on the Belgian borders.**
    - CREG : positive draft decision regarding EU HAR. Draft decision is subject to public consultation (deadline 18 September 2015)
    - CRE : no official decision yet although no blocking points were communicated to RTE, decision is expected beginning October 2015
    - ACM : no official decision yet although no blocking points were communicated to TenneT BV, decision is expected beginning October 2015
    - BNetzA : no official decision yet although no blocking points were communicated to Transnet bw, Tennet GmbH & Amprion , decision is expected end September 2015


Rules for Capacity Allocation
by Explicit Auctions
Version 2.0
within
Central West Europe Region (CWE),
Central South Europe Region (CSE),
France – Spain
and Switzerland

13 borders

41 borders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Draft Allocation Rules for Forward Capacity Allocation

2 March 2015

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