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# Svenska kraftnät's feedback on the report and views on support to the long term hedging market

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# Content

1. Need for TSO intervention
2. Use of congestion income
3. Support to the EPAD market

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# Need for TSO intervention

*"A basic premise for efficient intervention is that missing hedging opportunities are identified as a market failure. If there is no failure, intervention is prone to imply an efficiency loss."*

(Hagman/THEMA, 2015, p. 2)

*"All models come with a cost. Hence, a clear case of market failure should be identified before the TSO is instructed to intervene."*

(Hagman/THEMA, 2015, p. 5)

Svenska kraftnät strongly agrees with the report regarding need to establish that a TSO intervention is necessary before the TSO is asked to, in any way, act in the long term hedging market.

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# TSO intervention implies a cost

- > Shifting the financial risk from market participants to the TSO means socializing the risk to the TSO's customers and ultimately to the end consumers.
- > Additional risk → additional cost → financed by the TSOs customers.
- > If TSO intervention: value for the market significantly higher than the cost.
- > TSO business: Increased transmission capacity → positive impact on market and need for hedging
- > Neighboring interconnectors: measures will significantly impact the Nordic market and involved Nordic TSOs

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# Use of congestion income

> Interventions where the TSO directly take over the risk of market participants will result in a probable cost that is hard to anticipate.

> Auctioning of EPADs/EPAD Combos

> Allocation of Long Term Transmission Rights (LTTR)

Congestion income is the logical counterpart for the TSO.

> However, due to (EC) Regulation 714/2009 regulating the use of congestion income it is not certain that congestion income can be used for the purpose to support the EPAD market.

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# If congestion income cannot be used

- > FCA (art. 58): Costs incurred by TSOs from obligations in the regulation shall be recovered through network tariffs or other appropriate mechanisms.
- > Assuming cost recovery through the network tariff:
  - > No correlation between costs and revenues regarding TSO intervention in long term hedging
  - > Difficulty to assess the impact of LTTRs/EPADs on the TSO income statement
    - > Hard to determine an appropriate network tariff
    - > Likely to have a high volatility in the network tariff
  - > Benefits and costs are applied to different types of TSO customers
- > If Svenska kraftnät cannot use the congestion income for these measures, we will be as any other market participant acting in the market without any underlying asset for the EPADs/LTTRs.



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# If congestion income can be used

- > There is still a probable cost for the TSO to intervene in the market, although it will be in the form of lost congestion income.
- > *Common argument: “But auctioning EPADs or allocating LTTRs is good for the TSO, you are hedging your congestion income!”*
- > No.

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# If congestion income can be used

- > Usually when this counterargument is made it is assumed that the TSO take into account the whole amount of congestion income in the income statement and it therefore affects the network tariff.
  - > This is incorrect!
- > Svenska kraftnät's congestion income:
  - > Congestion income does not directly affect the network tariff, but only through interest rate and depreciation.
  - > Since only a small part of the congestion income affects the income statement – the price risk is only valid for this small part.
- > Hence, Svenska kraftnät has a very limited price risk for the congestion income and a hedge of the congestion income has no significant value.

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# Additional legal aspects

- > Consequences of measures depend on legal framework:
  - > Tendering demands for services, platforms, etc.
  - > State aid
  - > LTTRs and EPADs = financial instruments?
    - > Rules for markets in financial instruments

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# Support of the EPAD market

- > Svenska kraftnät agrees with the report and considers measures that support the existing long term hedging model, i.e. EPADs, as more appropriate than measures involving LTTRs.
  - > The long term market for financial contracts in the system price is fit for purpose.
  - > EPAD contracts is a complement to these contracts and support this design and System price.
  - > Measures involving LTTRs might weaken the existing structure of financial contracts and the System price.
  - > Svenska kraftnät sees a risk that LTTRs will mostly benefit larger market participants since the qualifications to participate in the trade of LTTRs can be substantial due to the European platform for allocation:
    - > Contractual agreements
    - > Collateral demands
    - > IT development
- > Svenska kraftnät believes it is important that the benefits of TSO intervention, if it is needed, is applied to all market participants since the costs will be socialized to all market participants.

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# Summary

1. Need to establish that a TSO intervention is necessary before a TSO is asked to act in the long term hedging market.
2. Important the TSO can use the congestion income as counterpart for measures in the long term hedging market.
3. Support to the EPAD market more appropriate than measures involving LTTRs.

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Thank you!

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