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RTE consultation on rules for balancing mechanism and balancing responsible parties

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The European Federation of Energy Traders (EFET)[1] welcomes the opportunity to comment on the RTE draft new rules for balancing mechanism and balancing responsible parties.

While EFET has no specific concerns on the majority of the amendments proposed by RTE, we believe that **the proposal on the financial security framework** contains some drastic measures and therefore deserves much more fine-tuning and consultation.

We fully support the objective of RTE to manage its counterpart risks and to prevent fraudulent activity. However, we believe that the proposal as it stands does not tackle these objectives in the most efficient way, while exposing all market participants to significant operational hazards and potentially disrupting the orderly functioning of the market.

As we have understood it, the reform revolves around two main mechanisms:

Bank guarantees linked to the annual power average of the Perimeter Extraction (Points C4.and C6. of Section 2 of the rules):

- The bank guarantee levels remain unchanged compared to the existing rules, except that a new step is added after EUR 3.2M at EUR 5M.
- Each bank guarantee level (from EUR 0 to EUR 5M) is linked to a maximum level of exposure on BRP, Injection and Withdrawal fees and all financial flows

[1] The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent, sustainable and liquid wholesale markets, unhindered by national borders or other undue obstacles. We currently represent more than 100 energy trading companies, active in over 28 European countries. For more information, visit our website at www.efet.org.

linked to RTE's "Ajustement-Ecart" account. Once the maximum level of exposure (outstanding invoices plus amounts to be paid on delivered power) has been reached, the BRP will be required to increase its financial cover (with a cash deposit option within 10 working days as a transitory measure, with a bank guarantee equivalent to the next threshold within a month).

- This obligation as it stands, would remain unchanged if the BRP's current exposure falls back under the level authorised by its original bank guarantee level.
- In case of non-compliance with this obligation, the BRP would not be authorised to take any net selling position if no cash has been deposited within 2 days or if the bank guarantee is not increased.
- Non-physical BRPs risk facing a ban from participating in the Balancing mechanism in case of non-compliance.

Limitation of the net short position of BRPs on a daily basis (Points C.3.3.1.3 to C.3.3.1.5 of Section 3 of the rules):

- The bank guarantee level also determines a maximum net selling position.
- The daily assessment takes into account all futures and spot transactions on EEX and EPEX Spot, assessed at the end of D-1 and OTC nominations ("NEB").
- Once the threshold is breached, RTE will curtail **all** selling transactions registered for the day and the BRP will need to rebalance itself on the intraday market.
- RTE foresees a phased implementation of this measure (see Point B.4 of Section 3 of the rules), whereby for the first six months, RTE will only notify BRPs that they are exceeding their maximum authorised amount of daily net selling volumes. After this period, RTE proposes to take curtailment actions and to conduct an impact assessment.

While EFET understands the rationale behind the reform, it appears to us as not robust enough against operational errors and likely to impact all market participants (including those that are not in breach of any requirement), while not necessarily limiting the potential of fraud where it really lies.

The bank guarantee requirement or their level are not challenged by EFET. However, the design of the overall process should be better focused on its primary purposes (ability to react quickly to limit the potential of fraud and efficient management of RTE's counterpart risks), while also reinforcing its operational robustness, limiting its management costs and avoiding false alarms or unnecessary burden.

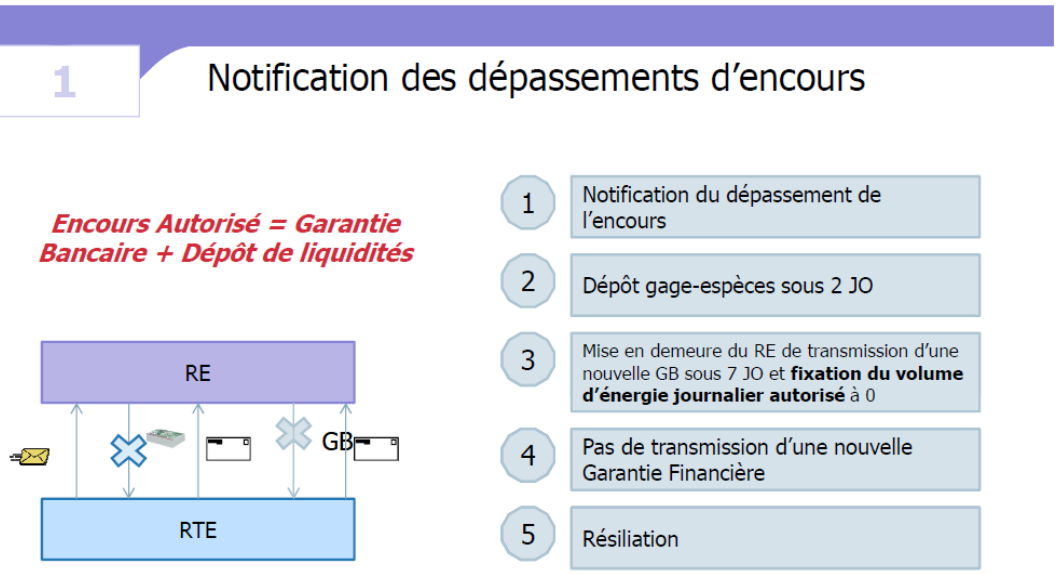
For this purpose we believe that some additional fine-tuning of the proposal is necessary, as suggested below.

- First of all, EFET proposes to better define the first level categories where the potential of fraud is likely to start and in order to allow for faster reactions in case of unplanned activity. This could be done through a minimum level of bank guarantee and "Encours autorisé" already in the first category (thus also avoiding to provide a "free credit" signal) and also with a more progressive scale (such as with an additional level of EUR 100,000 Bank Guarantee with EUR 10,000 "Encours autorisé"). This would ensure that each level of activity is correctly covered by a financial guarantee (without a bank guarantee no outstanding negative imbalance should therefore be authorised). We believe that this approach would better allow to tackle the risk of fraud where it lies, i.e. small scale, non-asset backed sudden fraudulent trading, while ensuring a more progressive and proportionate management of RTE's counterpart risks.

- Also in order to ensure a more precise and fluid management of the real risks RTE should take into account all the elements of the BRP perimeter (including imports and exports and intraday activity, potentially on the following day if intraday calculations are not available) and also when possible all reliable information directly provided by BRPs to refine its estimates concerning consumption units, especially during periods of changes in the consumption pattern.

- In the long-term, RTE should also consider put in place call-margining to allow more flexibility in the system.

- Concerning the operational process which will be triggered in case of insufficient financial guarantee, there should be much more flexibility for coming back to the normal process, for avoiding false alarms and for avoiding the ultimate stage of unilateral termination of the contract:



- In particular we consider that the proposed process should be stopped (especially in positions 3, 4 and 5) if the calculations made in the following days after the first notification indicate that the BRP is back under the level authorised by its original bank guarantee level. This would allow to eliminate some potential false alarms or to take into account the remedial actions taken in intraday by the BRP before real time, after the threshold was overpassed in day-ahead (potentially due to an unexpected position in day-ahead).

- We also propose that the first notification (in 1) should include an automatic acknowledgement of receipt and should allow for 3 days for the cash deposit and also that the energy volume should not be set to zero in 3 but rather decreased to a third of its value. This measure would better allow to avoid cascading defaults while seriously decreasing the risks for RTE. In the same way there should probably be a suspension (or energy volume put to zero) in 5 before the final termination is decided (the termination might indeed require some additional legal or regulatory steps). These measures would allow for a more progressive and robust management of problematic situations.

- In addition to all this some automatic pre-warning notification should also be implemented (via email), such as when 80% or 90% of the authorised amount is "consumed".

EFET believes that the limitation of the net short position of BRPs on a daily basis is very questionable and would also potentially put the market as a whole at risk.

- Since transactions exceeding the threshold would be curtailed, not only the contravening BRP but also its counterparties would be affected. This risk would not be manageable for non-contravening BRPs (this would induce some additional risks to transact with some counterparts and would also raise

some legal challenges on the EFET contracts). Market participants are also concerned about potential snowball effects that could potentially occur quickly.

- Also, the RTE calculation of BRPs position considers futures and spot transactions on EEX and D-1 EPEX Spot as firm, thus introducing a bias against forward OTC transactions and rendering them non-firm in practice, which is, to our judgement, an excessive measure. Also the continuous intraday market segment of EpexSpot is not considered and we consider (as for the financial guarantee) that this "limitation process" should be stopped when the estimated net short position falls back within the authorised limits during the following days. This would allow for eliminating errors or erroneous forecast, by taking into account the planned or remedial actions taken in intraday by the BRP before real time.

- Also the proposed calculation does not correctly take into account generation schedules communicated by asset-backed BRPs to the TSO. This should be considered in the calculation of the asset-backed BRPs, particularly based on historical statistics or with some unavailability discount if justified in order to reflect the reality of historical unplanned outages.

In any case, should these measures be approved, we believe that some additional analysis and discussions with market participants would be needed and that the impact assessment proposed by RTE should be conducted after the phase-in period of six months without activating the curtailment provisions.

EFET therefore encourages for some further discussions on these elements, which are of particular importance.

We remain in the meantime at your disposal for more explanations if needed.