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Explanatory note to the South West Europe TSOs  
proposal for a methodology for splitting long-term cross-  
zonal capacity in accordance with Article 16 of  
Commission Regulation (EU) 2016/1719 of 26  
September 2016 establishing a guideline on forward  
capacity allocation

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DISCLAIMER: the study in this explanatory note is a preliminary study and further analyses will be done comparing in depth market spreads in day-ahead timeframe with auction prices in long-term timeframes.

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## 1. Introduction

This document is the explanatory note to the Long-term cross-zonal capacity splitting methodology for SWE Region in accordance with article 16 of Commission Regulation (EU) 2016/1719 of 26 September 2016 establishing a guideline on forward capacity allocation.

The TSOs of the South West Europe Region, in this explanatory note, justify the adequacy of the proposed split shares in the methodology.

## 2. Justification of the adequacy of the split of the long-term cross-zonal capacity

The long-term transmission rights are to be understood as risk-edging products for the market spread volatility risk. In the form of ‘options’, either PTR with UIOSI, or FTR, the transmission rights are differentiated by each direction of flow in the interconnection.

Therefore, the spot value of a directional transmission right is the market spread in this direction, i.e., only positive market spread and zero if market spread is negative. In the limit, the auction price of transmission rights in a specific timeframe (yearly, monthly, etc.) should reflect the average of the positive market spread in this direction for this timeframe.

In order to justify the adequacy of the split shares in a bidding zone border, a comparison of auction prices with respect to positive market spreads, based on historical data, can be performed to show if historical volumes of allocated capacity are enough to be used for edging the market spread volatility risk. This analysis will be performed each year, based on Article 4.7 of the methodology, to revise, if necessary, the split shares in each bidding zone border.

TSOs of the South West Europe Region have performed some analysis of prices in both bidding zone border of SWE Region with historical data, that are explained in the paragraphs below.

### Portugal – Spain bidding zone border

Due to the Portugal – Spain bidding zone border have entered in SAP since year 2019 and the current split shares are in force from that date, the analysis of prices are referred only to year 2019.

For each timeframe allocation in this bidding zone border (yearly, quarterly and monthly) and for each direction, it has been compared the auction price and the average positive market spread. The results are summarized in the table below.

Timeframe	Direction	Split share in 2019	Auction Price	Average Market Spread
Yearly	PT > ES	15%	0,08	0,009
Quarterly		15%	0,08	0,001
			0,09	0,005
			0,02	0,002
			0,01	0,030
Monthly		15%	0,06	0,004
			0,04	0,000
			0,10	0,000
			0,07	0,015
			0,05	0,001
			0,06	0,000
			0,11	0,005
			0,05	0,000
			0,04	0,000
			0,06	0,008
0,04	0,064			
0,02	0,016			
Yearly	ES > PT	15%	0,12	0,211
Quarterly		15%	0,11	0,595
			0,21	0,214
			0,22	0,011
			0,22	0,017
Monthly		15%	0,17	0,708
			0,18	0,706
			0,27	0,382
			-	0,263
			-	0,358
			0,17	0,017
			0,15	0,004
			0,09	0,001
	0,15		0,028	
0,25	0,045			
0,19	0,000			
0,12	0,002			

Based on these results, the current split shares for the Portugal – Spain bidding zone border for both directions are considered still not enough for the volume of capacity that market participants are demanding at the transmission rights auctions and the split shares should be increased.

Additionally, in coordination with the Long-Term Capacity Calculation Methodology, the split shares have been increased to reflect the modification on the transmission reliability margin used in the calculation of the capacity for each allocation timeframe.

## France – Spain bidding zone border

For the France – Spain bidding zone border, the analysis of prices is based on the historical data of years 2018 and 2019.

For each timeframe allocation in this bidding zone border (yearly and monthly) and for each direction, it has been compared the auction price and the positive market spread with hourly resolution. A percentage indicating how many times the auction price is higher than positive market spread has been obtained. The results are summarized in the table below.

Timeframe	Direction	Split share for 2018 and 2019	Auction Price > Market Spread
Yearly	FR > ES	33%	94,8%
Monthly		33%	91,5%
Yearly	ES > FR	33%	41%
Monthly		33%	39,5%

Based on these results, the current split shares for the France – Spain bidding zone border in the France to Spain direction are considered not enough for the volume of capacity that market participants are demanding at the transmission rights auctions and the split shares should be increased in this direction. For Spain to France direction the current split shares can be considered enough for market participant demand, as the occurrence of auction prices being higher than market spread is close to 50%.

However, in coordination with the Long-Term Capacity Calculation Methodology, the split shares in both directions have been increased to reflect the modification on the transmission reliability margin used in the calculation of the capacity for each allocation timeframe.