

## Definition of Financial Transmission Options

The Convergence CM model allows and provides incentives for existing rights holders to translate their contracts into financial transmission options (FTOs) that gives the rights holder the option but not the obligation to schedule from bus to bus (or traded from hub to hub) without being responsible for congestion costs. The FTO is a financial instrument. Its value is equal to the product of the quantity scheduled times the difference in cost between one location and another. If unused, it expires valueless. We have not decided if it needs to be used for a particular injection withdrawal combination, which may be difficult to implement, or if it can be used against a set of injection and withdrawals, which may have revenue adequacy problems.

Once the bus to bus FTO's have been issued or purchased, any customer can trade or purchase Hub to Hub rights. Hubs are delivery or receipt points where this is active trading, much like Mid C, COB or PV. Hub-to-Hub FTO's are primarily made available from existing rights holders in the secondary market. There is likely to be a requirement for the RTO to validate any segmentation of FTO's to determine if the resale causes extra costs.

- The principle product traded on exchanges would be hub-to-hub FTOs
- Residual congestion would be charged to schedules based on the nodal dispatch model, rather than uplifted. This has a number of implications:
  - a) It would substantially reduce the problem of uplift due to poor definitions of zones and flowpaths associated with the Stage 1 model. Hedges purchased on the secondary market would be from hub to hub only (i.e., would not cover "intrazonal" or source and sink to hub congestion).
  - b) While it would be impossible to obtain a 100% hedge on the secondary market, most hedges will be 95+%, which should be within the margin of error for a product purchased up to two years ahead of time.
  - c) It would provide better dispatch signals during times when the mismatch between the commercial and operational models is sizable.