



- Consultation response -

## **Europex consultation response: Methodology for a co-optimised allocation process of cross zonal capacity for the exchange of balancing capacity or sharing of reserves**

Brussels, 30 July 2019 | Europex is pleased to contribute to the consultation on the '*All TSOs' proposal for a methodology for a co-optimised allocation process of cross zonal capacity for the exchange of balancing capacity or sharing of reserves in accordance with Article 40 EB GL.*' The primary parts of the response are included below.

**Please add here your feedback related to Articles 1 and 2 'Subject matter and scope' and 'Definitions and interpretation'**

Europex fully supports the use of market-based mechanisms to ensure the most efficient allocation of cross-zonal capacity, in particular in the day-ahead, intraday and balancing timeframes. This will also contribute to enhancing security of supply.

As a matter of principle, Europex opposes any pre-reservation of capacity for the balancing timeframe. Doing so risks the permanent withdrawal of transmission capacity from free competitive markets, e.g. the SDAC and SIDC timeframes, and would therefore lead to significant economic inefficiencies. Cross-zonal capacity reservation for cross-zonal balancing exchanges must remain an exceptional measure and be limited in size and proportional to the overall cross-zonal capacity allocation in accordance with the actual balancing needs. Moreover, according to the recently revised Electricity Regulation 2019/943, TSOs shall make the maximum level of cross- and intra-zonal transmission capacity available for trading while respecting a minimum of safety standards of secure network operation.

Any co-optimisation process should be carefully designed to maximise social welfare and to avoid any negative impact on the SDAC and SIDC timeframes. It must also allow for a maximum usage and efficient allocation of cross-zonal capacity, clearly following and respecting the principles set out in the Clean Energy for all Europeans package.

Against this background, Europex would like to express several strong reservations with regard to the present proposal and to Articles 1 and 2 in particular:

- Europex is sincerely concerned that the proposal to allocate CZC for the exchange of balancing capacity or the sharing of reserves does not include a clear definition of the roles and responsibilities of specific parties. Yet, the allocation of roles and responsibilities is a crucial element to understand the methodology, given the complexity of the topic and the number of parties who may be involved.
- As a result of the above, market participants are likely to lose trading opportunities, thereby also undermining the efficiency and well-functioning of day-ahead and intraday markets.
- The cost of co-optimisation should be assessed against the transition costs linked to the SDAC evolution. Indeed, a thorough cost/benefit analysis ought to be performed to evaluate the potential gain or loss from such a co-optimisation process, also given its higher level of complexity.
- As set out in section 4.2.5 of the explanatory document to the proposal, there are challenges stemming from the non-convex welfare optimisation problem between the capacity and day-ahead markets. Since the day-ahead and balancing capacity bids are competing for cross zonal capacity as a scarce resource, co-optimisation should only be applied if welfare is indeed increased during the allocation of CZC.
- There are several risks that the co-optimisation approach induces by impacting day-ahead market processes, i.e. consequences of the implementation that have not been properly considered. The co-optimisation should only be applied if the identified issues are solved. Europex, as a matter of principle, opposes any pre-reservation of capacities for the balancing timeframe, as doing so risks the permanent withdrawal of transmission capacity from free competitive markets, e.g. the SDAC and SIDC timeframes, and would therefore lead to significant economic inefficiencies.
- Besides co-optimisation, the Electricity Balancing Guideline (EBGL) defines two additional approaches to sharing reserves and exchanging balancing capacity: a *market-based allocation* and an *economic efficiency analysis*. There is currently no information available about whether any of the TSOs is planning to use the proposed co-optimised allocation process or in which region this process is to be included.
- Indeed, at the last ENTSO-E co-optimisation stakeholder workshop on 6 June 2019, it was stated that no TSO was intending to apply this method. For us, this raises the question of how and why further analysis of this method should be conducted.

- Furthermore, there is a lack of information on the other two types of processes, i.e. *market-based allocation* and the *economic efficiency analysis*. Therefore, it is impossible to evaluate the impact on the existing markets and to provide a constructive comparison between the proposed methodologies.

**Please add here your feedback related to Article 3 ‘Principles of balancing capacity cooperation’**

According to Article 3 of the current proposal, CZC can be allocated separately for upward and downward activation or jointly in case of an exemption. The methodology should clarify how TSO balancing needs and market offers are to be compared with SDAC for a co-optimisation of CZC in both cases. Regarding joint capacity balancing procurement between upward and downward capacity, it is unclear whether the bids are split when they are to be compared with SDAC bids, or whether there is another method.

**Please add here your feedback related to Article 5 ‘Timeframe of co-optimised allocation process’**

In Article 5.1.b., it is not clear why the notification to market participants of selected balancing capacity bids should be done after the SDAC result notification.

In Article 5.2.c., the verb “convert” should be replaced by an expression that more clearly indicates that orders are aggregated to create supply and demand curves.

For more clarity, it should be indicated:

- how a TSO’s demand would be affected on the buy or sell side, depending on the direction upwards or downwards, and /or;
- how upward and downward offers are incorporated in separate or commonly aggregated buy or sell curves.

**Please add here your feedback related to Article 6 ‘Process to define the maximum volume of allocated cross zonal capacity for the exchange of balancing capacity or sharing of reserves’**

As stated before, there should be no (i.e. 0%) pre-reservation of CZC for balancing before the SDAC and SIDC markets. This is also reflected in the Framework Guidelines on Electricity Balancing which are very clear that cross-zonal capacity reservation for balancing exchanges is indeed an exceptional measure: “The Network Code on Electricity Balancing shall require that any decision on cross-border transmission capacity reservation for balancing is taken on a case-by-case basis, by relevant NRAs supported by a full cost-benefit analysis and market consultation, in a transparent, non-discriminatory, fair and objective manner.”

**Please add here your feedback related to Article 7 ‘Determination of the actual market value of cross zonal capacity for the exchange of energy’**

From a general point of view, the description appears to be correct. However, it remains unclear whether the overall welfare optimisation in the price coupling algorithm for SDAC is done for all BZs, CZ ICs and time units of the given SDAC auction combined. The latter is distinctly different from the case for “the actual market value of cross zonal capacity for the exchange of balancing capacity or sharing of reserves”, because the given co-optimisation model would likely only be applied by a single or a few BZs and CZ ICs that are part of the SDAC.

Furthermore, it is important to specify whether “marginal pricing” is applied to all orders in SDAC and if co-optimisation, or any of the other applicable models, for the “exchange of balancing capacity” would instead apply ‘pay as bid’. This would directly impact the price formation in SDAC and possibly introduce significant risks of undue speculation and indirect hoarding (of CZ capacity). Also, even if “marginal pricing” was to be applied for co-optimisation, there is a severe risk of reduced efficiency and undue speculation, among others, because orders in SDAC are truly firm, i.e. lead to financial settlement of contracted volumes and physical scheduling obligations (e.g. BRP positions), whereas in most cases not all the orders selected for the “exchange of balancing capacity” will actually be used for balancing.

**Please add here your feedback related to Article 8 ‘Determination of the actual market value of cross zonal capacity for the exchange of balancing capacity or sharing of reserves’**

While the general high level description appears to be largely correct, it is unclear what the basis for the demand elasticity would be, e.g. the shape of the TSOs’ buy orders on a BZ (control/scheduling area) level which would determine which part of the overall “balancing capacity” would be acquired via CZ capacity allocation. It needs to be recognised that regardless whether TSOs were to place such orders price-dependent or price-independent they would in many cases risk strongly influencing the price formation in the SDAC and subsequent SIDC markets. This in itself is a serious concern in relation to the co-optimisation model and needs to be considered before any further steps are taken.

**Please add here your feedback related to Article 10 ‘Firmness regime of cross zonal capacity’**

According to Article 38(9) of the EBGL and Article 10(2) *“when CZC allocated for the exchange of balancing capacity or sharing of reserves has not been used for the associated exchange of balancing energy, it shall be released for the exchange of balancing energy with shorter activation times or for operating the imbalance netting process.”* The allocated CZC that has not been used for the associated exchange of balancing energy should be released to all the markets that are still open at the given timeframes and not only to the exchange of balancing energy with shorter activation times. It is

unclear when this occurs and if the SIDC market is still in operation. If the SIDC market is still open, it is obvious that the CZC should not be used for the exchange of balancing energy. Instead, the capacity should be given back to the SIDC market. After gate closure of the SIDC, the CZC that remains unused may be released for the imbalance netting process.

**Please add here your feedback related to Article 11 ‘Pricing of cross zonal capacity’**

Article 11.3 is not applicable the flow based model. This should be clarified.

It is difficult to understand what definition of “uncongested area” is applied in Article 11.2 if X% of cross-zonal capacity (CZC) is used for SDAC and Y% for balancing based on the co-optimisation model and the total of X% plus Y% is 100% of CZC. In other words, this puts into question the claim that the CZ price for the exchange of balancing capacity in this case should be set to zero (0). Put differently, it is not clearly explained in the co-optimisation methodology when there would be only partial usage of CZ capacity for SDAC and none at all or only limited CZ capacity allocated for the exchange of balancing capacity and accordingly some CZ capacity left for the SIDC. This certainly deserves additional clarification.

**19. Please add here your feedback related to Article 13 ‘Publication’**

In order to forecast prices, it is necessary that the TSOs publish their needs for the exchange of balancing capacity or sharing of reserves in quantity and volumes before the SDAC takes place. Otherwise, it is not possible for market participants to forecast prices and submit orders in an efficient manner.

**About**

Europex is a not-for-profit association of European energy exchanges with 27 members. It represents the interests of exchange-based wholesale electricity, gas and environmental markets, focuses on developments of the European regulatory framework for wholesale energy trading and provides a discussion platform at European level.

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