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EBL comments on Draft revised ERGEG Guidelines of Good Practice for Electricity Balancing Markets Integration (GGP-EBMI)

The development of common European rules and regulations, to secure a common platform for trade and competition in the electricity sector, is of imperative importance. Guidelines are important in order to secure a long term development towards harmonised solutions and pave the way for a European Integrated Market. Hence, EBL¹ welcomes the opportunity to comment on Draft Revised ERGEG Guidelines of Good Practice for Electricity Balancing Markets, which was published on January 15, 2009. We limit our comments to those guidelines which we believe should be amended in order to promote competition in the wholesale and balancing markets, as well as to secure proper investments incentives in both balancing power and cross border capacity.

General comments and conclusions

EBL agrees that balancing market integration is a key issue in the development of the internal electricity market, and we are certain that the importance of this issue will increase significantly in the future. The RES directive and investments in new renewable power generation, especially wind power, will lead to a drastic increase in the proportion of intermitted power generation within the European Community. As a result, future demand for balancing services will be substantial.

EBL considers the framework of the draft good practice guidelines and the issues addressed as highly relevant. We strongly support the need for guidelines and ERGEG's views on the following issues:

- access to a more diversified generation technology mix, thus enabling reduction of the total amount of necessary reserves, minimising balancing costs and increasing efficiency.
- stronger competitive pressure; and
- wider scope for reserves sharing and therefore reduction of the supply interruption risks.

There are several issues that in our view should be considered in finalising the guidelines:

¹ The **Norwegian Electricity Industry Association (EBL)** is the main electricity industry association in Norway representing approximately 260 companies with a yearly production of approximately 123 TWh (99% of the total generation in Norway), suppliers and distributors with 2,1 million network customers (92 % of Norways total network customers). The main purpose of EBL is to deal with industry-related economic and political issues on behalf of its members, to provide a good framework and conditions for the industry in respect to financial, legal and technical issues.

- Unfortunately we believe ERGEG's proposed guidelines in some cases will impede competition in trade and exchange of system- and balancing services throughout Europe. There are few if any technical obstacles of increased exchange of e.g. products for automatic load frequency control – LFC. Existing and upcoming HVDC technology can facilitate cross-border exchange and trade of fast, flexible, and reliable LFC products. If, however, the guidelines are enforced as proposed an efficient exchange and trade of such products will not be possible. As an example Norwegian generators would be directly obstructed from competing with Dutch generators on supply of LFC. If there is no technical reason for not opening up for such solutions the guidelines will represent a formal trade barrier imposed on the market players. In this respect any possible conflicts of interest regarding European competition legislation should be scrutinized.
- The objective of creating regional markets laid down in the third energy package requires integration of reserve and balancing markets. The proposed guidelines, however, leaves this option open. We believe the guidelines should set out concrete steps and measures in order to secure future harmonisation of balancing markets. Firm obligations should be placed upon TSOs to cooperate and harmonise their practices and standards.
- In order to avoid diverging interpretations and implementation delays in harmonisation of cross-border balancing markets, there is in our view a need of increased clarity of concepts and definitions (e.g. automatically activated / manually-activated vs. Primary /secondary / tertiary reserves, relations between intra-day markets and balancing markets, capacity allocation on interconnectors with or without congestion in relation to DC and AC interconnections).
- Solutions and implementation steps concerning cross-border reserve and balancing markets are interlinked with the development and implementation of intra-day markets. In our view Intra-day market solutions are a part of the balancing integration and should be addressed in the proposed guidelines.

When describing the benefits from balancing market integration, ERGEG points out that the integrated market will help the TSO to minimise balancing cost. However, EBL believes that efficient utilisation of resources and sound investments are dependent of “correct” price levels rather than “low” price levels. The main benefit of the integrated market is to secure an efficient utilisation of cross-border capacity, balancing resources, and give the right incentives for future cross-border capacity increases.

Proper incentives for future investments in cross-border transmission capacity and efficient use of existing capacity is important in order to achieve EU energy policy targets regarding implementation of renewable, security of supply and market integration. Although day a-head market development and integration in Europe is increasing, it is important to develop open market solutions for trade and exchange of balancing reserves and ancillary services (primary and secondary reserves). It can be shown that the value of exchange of such reserves can be much higher than the exchange in day ahead, illustrated in figure 1 below.

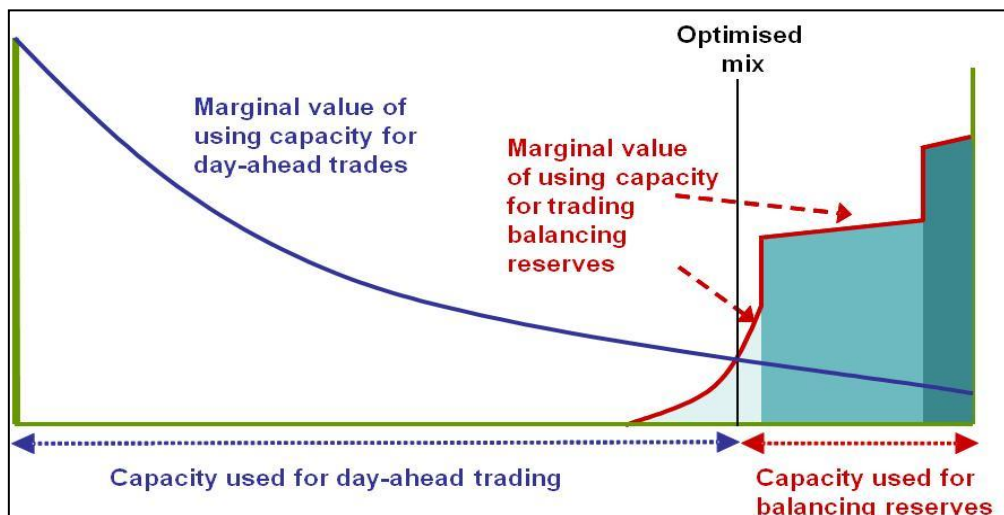


Fig. 1. Efficient use of grid

In our point of view it should be the value of exchangeable products that decides the priority of cross-border capacity use. In cases where exchange of primary/secondary reserves have higher value than tertiary reserves, intra-day trade or day ahead trade, cross-border capacity should be given to the primary/secondary markets (the products giving the highest profitability and highest European social welfare).

The proposed guidelines do not address the differences between AC and DC interconnectors in relation to exchange of balancing services. In this respect there are large differences between the two technologies. Power flows in AC systems follow Kirchoff 's law and are not easily controllable. Power flows on DC interconnectors are on the contrary highly controllable and equals a load or a generator at each point of connection depending of direction of flow. DC interconnectors can therefore more easily be used for automatic balance reserve capacity by use of Automatic Generator Control - AGC and Load Frequency Control – LFC systems. Furthermore DC systems may be designed specifically to cater for loads with a short duration, tailor made for the balancing market.

In systems where intra-day markets are not introduced all balancing mechanisms are controlled by the TSO. Implementation of well functioning intra-day markets will increase competition for balancing services and reduce the need for TSO controlled balancing services (primary, secondary and tertiary reserves). Increased competitive pressure is not only important for reducing the possibilities of market power abuse from generators. Single buyer solutions where the TSO is the only buyer in combination with wide legal rights to control available transmission capacity, order generator governor parameter settings etc. can be detrimental for competition and efficient price formation in the balancing markets. It is therefore important to find solutions that also increase competition between TSOs.

ERGEG's Draft Revision of the Guidelines of Good Practice for Electricity balancing Markets Integration

In the following our comments concerning the specific proposed Guidelines are given.

5. Access to interconnection capacity

5.1 reservation of interconnection capacity

ERGEG proposed Guidelines

No interconnection capacity shall be reserved for cross-border balancing except to cope with unexpected flows resulting from primary control or for interconnections with no congestions.

Comments from EBL

Proposed text alteration:

No interconnection capacity shall be reserved for cross-border balancing unless such reservations can be shown beneficial to the market, subject to public consultation, and published for predefined future periods.

EBL does not agree with the proposed guidelines that limit reservation of interconnection capacity for balancing power to primary control or in situations where there is no congestion. Although we agree that reserving capacity for cross-border balancing on existing interconnectors can reduce competition in wholesale markets when capacity is scarce, capacity reservation for balancing purposes may be a prerequisite for triggering new cross border investments. As an example we would like to refer to the planned cross-border interconnection Skagerrak 4 submarine cable where revenues from balancing services are crucial to the project economy. Capacity reservation (100MW of 600MW) is a prerequisite for the exchange of these balancing services. The value of these reserve capacity exchanges is higher than the forecasted values of day a-head trade on the same capacity (100MW). If

no capacity can be reserved for balancing purposes, this and other projects may be postponed or cancelled. We believe that the proposed guideline could lead to fewer investments, resulting in reduced cross border flows, reduced competition, also in the wholesale markets and reduced European welfare. We urge ERGEG to consider any possible disincentives for investments.

Furthermore, we see no reason why it should not be possible to utilise capacity for balancing purposes in the opposite direction of expected power flows. This will increase revenues from cross border trade, hopefully leading to investments in cross border capacity.

The Norwegian production system is highly flexible and has a large potential for developing even more power and balancing capacity that could be offered to an increasing regulation need in Europe. The DC technology today and in the future offers very flexible, fast and controllable regulation possibilities. It is therefore important that the Guidelines do not reduce the potential economic and technical benefits that this technology and the Norwegian regulation capacity can provide to the European system in the future.

5.2 Charge on access to interconnection capacity

ERGEG proposed Guidelines

When setting up cross-border exchanges of balancing energy after gate closure of day ahead and intraday markets, any charge on access to interconnection capacity for balancing energy shall be prohibited. Only new interconnections exempted under Article 7 of Regulation (EC) 1228/2003 may, upon request, be exempted from this provision.

Comments from EBL

We support ERGEG's position.

6. Contracted reserves

6.1 Cross-border procurement of reserve capacity

ERGEG proposed Guidelines

Cross-border procurement of reserve capacity shall be possible only for primary control reserves or for interconnections with no congestions. Redistribution of primary control reserves through cross-border procurement shall not exceed a relatively small percentage of control area requirements and shall be subject to affected TSOs' approval.

Comments from EBL

Cross-border procurement of reserve capacity could be profitable from a social welfare point of view if reservation of transmission capacity for such purposes is made possible.

As pointed out by ERGEG procured cross-border capacity reserves is subject to grid availability that can only be ensured with reservation day ahead at the latest. If this cannot be done control areas which choose to reserve capacity abroad, must have local means available in case of transmission congestions and TSOs would have to contract reserve capacity twice and unduly withdraw resources from the wholesale market.

Thus cross-border procurement of reserve capacity should be made possible by reservation of cross-border transmission capacity and on interconnections with no congestions.

Redistribution of primary control reserves through cross- border procurement should be evaluated in terms of security of supply needs and not as a general rule be restricted to a relatively small percentage of control area requirements. We support the need for TSOs' approval. However, this

issue should not entirely be left to TSOs decision, but be based on follow-up of experiences and a high degree of transparency and well founded redistribution criteria is therefore important.

6.2 Cross-border procurement of balancing energy

ERGEG proposed Guidelines

TSOs shall implement mechanisms allowing cross-border trade of manually-activated balancing energy as long as system security is not endangered. Those mechanisms shall not discriminate between balancing energy bids and offers from local and neighbouring markets. Adequate procedures for the agreement of exchange schedules shall be set up to allow cross-border exchange of balancing energy.

Comments from EBL

EBL do not support the view that cross border activation of balancing energy should be limited only to balancing energy related to manually-activated reserves. The benefits of cross border procurement of balancing energy related to automatically-activated reserves can be much higher than the manually-activated reserves, due to the high frequency of activation of these reserves compared to the manually-activated ones. Hence, in addition to manually-activated reserves the TSO should be obliged to develop and implement mechanisms that allow cross-border trade of automatic-activated reserves (primary and secondary).

ERGEGs definition of manually-activated balancing energy is not clearly outlined in the paper in regard to the distinction between on one hand primary/secondary reserves as automatic and on the other hand tertiary reserves as manual.

6.3 Amount of reserve capacity

ERGEG proposed Guidelines

The amount of reserve capacity shall be set according to defined security criteria and approved by regulators.

Comments from EBL

EBL support ERGEG's views.

7. Models for cross-border balancing

ERGEG proposed Guidelines

Towards integrating balancing markets, the TSO-TSO approach shall be seen as the preferred solution whereas the TSO-Provider approach may be implemented in case of incompatible gate closure and technical characteristics of balancing services.

Comments from EBL

Keeping system balance is a key responsibility of the TSO. Market participants are therefore through guidelines and codes obliged as far as possible to keep their balance regarding their bids into the market. Introducing e.g. intra- day trade enables the market participants to eliminate most of their

imbalances, hence reducing the TSOs need for buying additional system- and balancing reserve capacity. Balancing markets should therefore not only be considered as a tool which can enable the TSO to maintain balance in a cost efficient manner, but also a mechanism to enable the market participants to keep their own balance. This will increase trade between market participants and reduce the TSO's need for system- and balancing services.

EBL does not agree that the TSO-TSO approach for cross border balancing should be seen as the preferred solution. The TSO-TSO approach does not facilitate efficient utilisation of balancing power capacity, as long as all economic incentives are not directed to the market participants.

Investment and generation incentives must be directed to those who supply balancing power. In order to develop the internal market, this key principle should apply to cross-border balancing trade as well as national markets. Furthermore, market participants should have full access to the integrated balancing market in order to compare the cost of imbalance, charged by the national TSO, to the integrated balancing market price.

We believe that the TSO-Provider approach would facilitate increased competition and a more efficient market. Increased competition leads to a better utilisation of balancing power capacity. We fail to see why this approach only allows trade in one direction if reservation of capacity for trade of such products is allowed. In any circumstance trade in the opposite direction of a given congestion should be possible as it would relieve the congestion.

By utilising automatic control systems (e.g. AGC and LFC) both control flexibility and rapidity could be assured. However, capacity reservation is a prerequisite for trade of primary and secondary reserves.

Obstacles regarding different market rules and IT systems should be addressed in these guidelines in order to harmonise such rules as should ENTSO-Es obligation to develop European grid codes.

8. Design of balancing markets

ERGEG proposed Guidelines

Full harmonisation of balancing markets is not a prerequisite for cross-border balancing. Thus, cross-border balancing implementation should precede definition and implementation of a standard market design.

In a step-wise process, harmonisation of gate closures and technical characteristics of balancing services is not a prerequisite. But increased compatibility would be highly valuable and allow enhanced cross-border balancing exchanges.

The coexistence of different balancing services settlement schemes may be a barrier to cross-border balancing exchanges. Whereas there is a lack of consensus on a preferred scheme, it is clear that in the integrated balancing market settlement must be resolved in a common way.

Comments from EBL

Although we agree that full harmonisation is not a prerequisite for implementing cross-border balancing schemes, we consider harmonisation as a major prerequisite for a successful integration process of balancing markets. The proposed guidelines are in our opinion not prescriptive enough to effectively promote a successful integration in the future. It is therefore

important to harmonise the main framework and design of these markets as far possible at an early stage. There seems to be a slight discrepancy between paragraph 1 and 3 in this respect. In our view there are several issues that should be harmonised before implementation of cross-border balancing markets in order to secure a smooth future harmonisation. Definitions and important market design standards should be in place prior to implementing cross-border markets. If this is not the case future harmonisation could prove difficult. In our opinion the guidelines should point out the most important issues for harmonisation and a concrete step-wise approach towards full harmonisation in the future.

Harmonisation of gate closure should in any case be a top priority regardless of balancing market integration. Harmonised gate closure is a prerequisite for integrating and coupling markets and is a key obstacle in order to develop the internal electricity market.

The ERGEG proposal describes two pricing options regarding balancing service settlement. We consider a price system with the marginal price for upwards and the marginal price for downwards regulation for settlement provides the best incentive for market participants to match their supply and demand. We believe that the pay-as-bid option does not provide needed long term incentives in order to invest in balancing power capacity. As the proportion of intermittent power generation in the European energy-mix will increase in the future, proper incentives for investments must be in place. Economic theory supports that only a marginal pricing option will result in efficient allocation of resources and provide optimal investment incentives. We do not consider marginal pricing to be more sensitive to market power. On the contrary, we believe pay-as-bid pricing may result in reduced transparency, less liquidity and higher prices in the long run.

In order to prevent congestion costs influencing the balancing settlement outcome a clear and distinct definition between “balancing needs” and “congestion needs” should be established.

9. Transparency and monitoring

9.1 Transparency

ERGEG proposed Guidelines

All information required for the effective functioning of the integrated balancing market shall be structured, aggregated appropriately and made available to the public in a format which takes into account the needs of all market players.

Comments from EBL

EBL support the need for a high level of transparency.

9.2 Public data

ERGEG proposed Guidelines

The data published in each control area shall include balancing market rules (including mechanisms to allow cross-border balancing) and lists of data defined below. Information shall be published in the local language and in English.

All of the information published must be kept available at least for two years after the publication of the final update.

Comments from EBL

EBL support ERGEG’s proposal.

9.3 Monitoring by regulators
ERGEG proposed Guidelines
Regulators shall include in their evaluation of congestion management methods, mentioned in Article 1.10 of the amended Congestion Management Guidelines annexed to Regulation (EC) 1228/2003, a chapter on cross-border balancing. This chapter shall evaluate implemented mechanisms and on-going projects. It shall also highlight impediments to implementation and enhancement of cross-border balancing.
Comments from EBL
EBL support ERGEGs proposal.

This concludes our remarks to the consultation document. If there is any need for further clarification regarding our comments do not hesitate to contact us.

Best regards,
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