

ERGEG REGIONAL INITIATIVES PROGRESS REPORT

A EURELECTRIC Response Paper

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EURELECTRIC RESPONSE TO THE ERGEG REGIONAL INITIATIVES PROGRESS REPORT

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EURELECTRIC response paper to the ERGEG Regional Initiatives Progress Report

B.1. From your point of view, what is the main achievement of the Electricity Regional Initiatives process?

EURELECTRIC strongly supports the development of regional markets in Europe and sees them as a realistic intermediary step towards the single EU electricity market. ERGEG Regional Initiatives have brought a positive contribution - despite their voluntary nature - to the implementation of the Congestion Management Guidelines into the regions, one of the main achievements of the ERI being the establishment of auction offices..

At the same time, it is important to notice that the degree of market integration varies significantly across regions and the gap between most advanced regions and the ones lagging behind has increased over time. Therefore success of the ERI can only be assessed looking at each region separately. EURELECTRIC recognises that better progress has been achieved in regions where the idea of market integration received governmental support.

To ensure progress in all regions, along with coherence and convergence towards the single EU market, an overarching framework with clear targets, deadlines and responsibilities is necessary. Such framework should inter alia integrate feedback from the most successful Initiatives. Once that has been agreed and defined by all key stakeholders, work should commence on its implementation. EU Institutions, who are politically responsible for the goal of an integrated Pan-European market, should ensure high-level coordination and monitoring of the process.

Attention should also be put to other issues, which are impacting real market integration such as regulated end users tariffs and other national protectionist measures so that the coupling of wholesale markets can also be followed with progress in these related matters.

B.2. What should be the framework conditions for having flow-based capacity calculation based on a common grid model implemented in practice?

The flow-based (FB) method, which must be applied across an entire (at least synchronous) region in the same fashion, naturally requires strong cooperation among TSOs and would therefore contribute to the objective of regional integration. With this method, TSOs should adopt on a regional basis the same standards for calculating grid capacity in each control zone, the same procedures and assumptions and the same regional grid model.

Establishment of a European-wide common grid model (EU-CGM) will require the same level of information and coordination between TSOs with regard to

- reliability assessment based on the EU-CGM
- security analysis (capacity assessment) based on the EU-CGM
- curative redispatch measures based on a EU-CGM to guarantee firmness.

Border capacities (BCs) and Power Transfer Distribution Factors (PTDFs) should not be set bilaterally by neighbouring TSOs, as is now the case for NTC/ATC values, but should be discussed and agreed regionally by a competent regional entity under effective supervision or at least detailed monitoring by the competent regulatory bodies. This appears to be the effective way of ensuring compliance with the agreed operational standards, guaranteeing the transparency and credibility of the grid calculations for all market participants and thus leading to optimal gains in economic welfare.

The exact structure and powers of this regional entity should be worked out by the competent regulatory authorities and TSOs in collaboration with market participants. It could for example take the form of a regional capacity allocation office. Without an integrated operational setup, FB method will not deliver sufficient value-added to the system operation.

Issues related to the legal responsibility for grid security that would arise from the creation of such a centralised authority would also need to be addressed by the competent regulatory authorities and the TSOs.

In this context, we also want to refer to the question B.4 about the transparency requirements that are necessary to make flow-based calculation successfully implemented together with flow-based allocation.

EURELECTRIC welcomes the establishment of an Ad Hoc Advisory Group (AHAG) of stakeholders, decided at the last Florence Forum, which will monitor concrete projects and provide guidance for the elaboration of the framework guidelines and the network codes. In particular, EURELECTRIC welcomes the project to develop a European capacity calculation concept based on a common grid model and flow based calculation, where clear benefits can be demonstrated.

Given the innovative characteristic of the FB method and the highly meshed European network, it is recommended that this method only becomes operational after extensive shadow tests.

B.3. What do you believe should be the short- and long-term goals for a regional approach to capacity allocation?

EURELECTRIC believes that the below listed goals will help drive a coordinated and integrated wholesale markets. To achieve them, strong political support and closer Member States' involvement are key enablers.

These goals (2010-2015) are as follows:

- Introduce market coupling within and between the regions for all physical cross-border capacity on the basis of the above mentioned governance model and following on an implementation roadmap
- Ensure implicit continuous allocation of intra-day capacity via the implementation of a continuous European cross-border intra-day platform
- Introduce a 'TSO-TSO with common merit order' model to integrate cross border balancing markets.

In order to achieve these goals, it will be crucial to:

- Reach consensus over a target model for the EU capacity allocation and congestion management framework between all major stakeholders, to be applied in a consistent manner between and across the regions so as to create a level-playing field (2010)
- Increase coordination between different projects and regions on the EU/interregional level in order to avoid overlap and to ensure consistency with the agreed target model
- Ensure close and robust cooperation between TSOs and Power Exchanges, which primarily depends on agreement on the governance framework and definition of new functions, roles and responsibilities against the background of the adoption of the 3rd Energy Package.

Attention should also be paid to current impediments to liquid wholesale markets such as the continuation of end-users regulated tariffs and the existence of import/export bans on certain interconnectors.

B.4. Do you consider transparency requirements for capacity calculation sufficient? If not, what do you need additional data/information for?

No, we note that most of TSOs do not provide sufficient information to market parties on **how** the capacities are calculated. To ensure transparency and market's trust in the values defined by TSOs they should clearly explain how assumptions are made, how different drivers/factors are included in the calculation and how final results are calculated.

Market parties also do not get the necessary feedback from TSOs, which would enable them to understand the **results** (i.e. the offered capacity to the market, both inside markets and cross-border). It is also fundamental that in the case of pilot projects related to flow-based calculation and allocation processes, these projects are run in a way that will help build trust in the market. It would be advisable in this case to offer the market a potentially simplified model allowing them to get familiar with the mechanism and to understand the end results and underlying assumptions. This should ideally be done on an ex-ante basis or -as a minimum – on an ex-post basis. Clarification of the details will entail an interactive debate between TSOs and market parties, and will lead to an improved calculation process.

Due to this lack of transparency market parties often have the impression that capacity amounts offered to the market are too conservative and that margins are larger than what is required for network security margins. In some regional markets, there are also concerns over growing security margins whilst the capacity offered to the market is declining. There also concerns that TSOs are not sharing sufficient data between themselves, which as result limits usage of potential extra capacity.

We have frequently verified that calculation methods and results across the borders are asymmetric and therefore believe that TSOs should provide full transparency on the way they make their calculation.

There is overall a striking difference between the information on capacity data (transparency on fundamental network data), which has improved over the years and the still poor information which is persisting on capacity calculation.

B.5. What practical steps should be taken at an interregional level to ensure an efficient and harmonised approach to capacity allocation in the 1) long-term; 2) day-ahead; and 3) intraday markets?

Long term

We believe that the best way to ensure efficiency and harmonisation in the development of long-term capacity markets is to agree at the EU level some key requirements, which will then be applied by regulators and TSOs at regional level.

Some of the basic features of an EU wide target model have been already agreed within the PCG work as presented at the December Florence Forum in Rome and should serve as guiding principles to coordinate the work within and between the regions. Detailed specifications of the target model defined at the EU level together with a concrete implementation roadmap will improve the regional markets and help drive an inter-regional process converging towards a single integrated EU market.

We believe that these above mentioned topics are instrumental in bringing wholesale markets together, thereby creating large and liquid spot markets where spot prices can be seen as the reference price. In addition to this, attention should also be paid to making concrete steps towards physically/financially firm transmission rights (via for example TSO incentives) based on a harmonised definition of force majeure. EURELECTRIC in this respect fully supports the conclusions of the PCG. We believe that the current 'use-it-or lose it' mechanism should be promptly replaced with use-it-or-sell-it principle on all borders where capacity rights are allocated physically.

Day-ahead

In our opinion, agreement on the EU-wide target model will be key to making progress in DA market coupling projects. EURELECTRIC fully supports Single Price Coupling all over Europe as the target model (as agreed in the PCG project).

The further work on the target model should comprise two major elements:

- Development of a single matching algorithm that will enable establishment of prices and volumes across all borders between the “PX market areas” and/or bidding areas compatible with capacity calculation.
- Agreement on a governance model that will clearly elaborate functions and responsibilities of power exchanges and TSOs. Market stakeholders should be consulted and market parties’ needs should be taken into account when making the final choice between various alternatives of governance arrangements. To facilitate involvement of market parties in the process, a permanent follow-up function via an advisory board or similar should be envisaged.

When it comes to implementation, EURELECTRIC recognises that stakeholders should reach agreement on a pragmatic and feasible sequential approach, as it will be difficult to proceed with market coupling in several regions at once. One of the possible natural sequence has been outlined in the PCG proposal for a DA roadmap.

Intraday

EURELECTRIC welcomes the outcome of the PCG project where consensus on Implicit continuous allocation (continuous trading) as target model for the intraday timeframe was reached.

The implementation of the target model will include establishment of common principles, development of centralized capacity management and shared order book function as well as step-wise regional spread-out. Similar to DA, it will require coordination between regions and agreement on a pragmatic and feasible sequential approach.

In our view, agreement on a target model for all three timeframes can be achieved independently of each other due to limited interdependencies between these timeframes.

B.6. What are the future challenges in ensuring that allocation mechanisms across all timeframes can work together?

Due to the fact that electricity markets have been historically national and very diverse (in terms of industry structure, generation mix, market model features, etc.), regional integration has been and remains very challenging.

However, in our opinion it is now crucial to use the momentum created in the PCG project and to develop an overall consensus on the target model for the EU-wide capacity allocation and congestion management for different timeframes. Without a clear EU-wide target model, it will be difficult to coordinate between regional market developments and make the next step towards inter-regional integration and ultimately an EU-wide electricity market.

EURELECTRIC recognises the value of bottom-up initiatives in achieving a single electricity market. In doing so, it is essential to ensure that regions develop in a consistent manner. This requires in our view that these local/regional initiatives (in particular those which are recent) are closely coordinated and monitored in order to make them compliant with the target model. Should it not be the case, necessary pragmatic steps should be identified and planned to align them up with the target model.

In our view, the ERGEG Ad Hoc Advisory Group (AHAG) established at the last Florence Forum should have a role in coordinating and monitoring these existing initiatives as well as advising new initiatives on their consistency and appropriateness in relation to the target model.

EURELECTRIC believes that AHAG will also be able to effectively contribute to interregional coordination by giving advice to ERI regarding the planning and coordination of market coupling projects.

EURELECTRIC strongly supports the need to reach agreement between all major stakeholders on a roadmap with clear milestones and deadlines. The roadmap should be based on a realistic view reflecting a possible natural path of market integration, in which most advanced regions merge first and the less developed regions join them in the next phase.

The agreement on a possible roadmap for Day-Ahead reached in the PCG project has been a positive experience and similar agreements should be reached for Intra-Day and Forward.

B.7. Do you consider that achievements by different regions towards a harmonised set of rules at regional level for long-term capacity allocation merit further work or should there be more emphasis put on inter-regional harmonisation (considering that this may impede short-term regional progress)?

We believe that progress should be made in parallel inside the regions and between regions.

Some basic steps can be taken at regional level to improve the efficiency of long term capacity allocation and do not have to be coordinated at a wider scale. This can be done for example by introducing the use it or sell it principle, ensuring (financial) firmness, coordinating long term auctions inside regions (through common auction offices) and establishing secondary markets. A common platform for trading transparently these capacities is wishful.

Harmonisation of products (multi annual, annual, quarterly, monthly, etc.), auction rules and procedures inside regions and between regions are crucial to speed up market integration: this process has to be made consistent EU-wide, be based on best practices already in place in certain regions and further evolve towards one single agreed EU model.

The more regional markets will progress, the more they will have to converge towards a common target model, which in the meantime will have to be defined at the EU level. With regard to this point, we believe that some important points have already been agreed among all stakeholders within the PCG work and the final target model can be further defined in more details during the next 6-12 months. The features of this agreed EU target model will have to guide any future development of regional models either through voluntary implementation or through the implementation of binding network codes, which will later include the specifications of the target model.

B.8. Do you think that extending the geographical scope of existing auction offices is advisable/feasible?

With regard to extending the geographical scope of existing auction offices, a pragmatic approach should be followed to ensure at the same time quick implementation and effective market integration. Practically this will imply coordination of tasks between existing auction offices without creating new structures/entities or overlapping functions/responsibilities if the relevant entities already exist. It will thus avoid unnecessarily high management costs.

Tasks of Central Auction Offices should also be extended: some auction offices are only involved in the allocation process, while others are involved in the capacity calculation or the nomination process. In the final stage all these activities (including secondary market of capacity rights, intermediate for market coupling, intermediate for cross-border intraday process etc) should fall within the remits of the central auction office.

We also believe that the process has to be coherent with the progressive coupling of regions. If a region expands, the existing auction office can extend its activities to the additional markets/price areas, if the borders of these new markets are regulated by central auction office.

As a general recommendation for existing and future auction offices, EURELECTRIC calls for progressive harmonisation of offices structures and auction rules. As the recent Commission study on the regional initiatives concludes, if different models of auction offices are in place, this would create obstacles to further integration of regional markets. Stronger steering by relevant authorities is required to achieve further progress.

We are indeed convinced that a step-wise integration of the central auction offices towards one European auction office (at the latest by 2015) would enhance the harmonisation process of allocation rules, and also lead to a harmonisation of the IT platforms making market operations more efficient.

B.9. Do you agree with price market coupling as the target model for day-ahead capacity allocation?

EURELECTRIC fully supports price coupling as the target model for day-ahead capacity allocation. This will be facilitated through the development of a common grid model as it will contribute to maximizing NTC values available to the market and implementing loop flows controls as well as information exchange between TSOs.

For further EURELECTRIC comments on this issue, see our response to B4.

B.10. How important do you consider further development of cross-border balancing solutions? Which model do you consider appropriate and efficient?

Integration of balancing markets across Europe will be instrumental in accommodating renewable power into the grid.

EURELECTRIC supports the agreement on a high-level target model that has been reached in the PCG project, namely the TSO-TSO with common merit order (with TSO-BSP, multi-TSO-TSO as intermediate steps) and believes that further work on defining the detailed features of the target model should be continued.

In our view, the target model should in principle support the cross-border capacity allocation in the most efficient sequence, exclude any capacity charges (as only remaining capacity left from previous timeframes should be used for cross border balancing) as well as be based on marginal pricing for balancing energy.

We also support a pragmatic approach towards integration of cross border balancing markets. Integration should start with pilot projects, harmonisation of gate closures and technical characteristics. Effects of integration of cross border balancing markets should be studied using the experiences of the pilot projects. The impact of the cross-border balancing markets on optimisation of social welfare as well as contribution to security of supply should be carefully analysed. We also recognise that development of cross-border intraday market will positively contribute to efficient functioning of balancing markets.

B.11. Do you share ERGEG's view that significant progress in transparency has been reached thanks to the ERGEG Regional Initiatives? What steps should be taken in order to enhance transparency further?

We believe that progress on the European level has been positive though limited. Electricity generators have contributed to this by engaging in voluntary disclosure of relevant production data within the framework of the ERI. The regional initiatives have thus achieved some important progress with the drafting of the Transparency reports (based on 2006 Guidelines for Good Practice) and their adoption in some regions.

We call for lead regulators of the other regions to enforce the rules agreed at regional level as a first step towards a common EU approach with a list of transparency requirements agreed among all stakeholders. However, a binding process is still lacking at the EU level to ensure harmonisation of rules in all regions and a level-playing field for all generators.

In relation to this fundamental data on market transparency, EURELECTRIC therefore believes that this issue needs to be handled promptly in the form of a legally binding instrument (eg. new legislation or revision of the existing congestion management guidelines). We believe that this is the intent of the comprehensive approach, which the Commission is in the process of elaborating

We also believe that it is of paramount importance to avoid duplicating administrative costs on operators due to different regulation levels: provisions on transparency and exchange of information should therefore be harmonised on European level and should lead to coherent arrangements that minimise administrative and bureaucratic burden operators.

In this context, there could also be room for network codes strictly based on detailed framework guidelines prepared by ERGEG/ACER and associated network codes developed by ENTSO-E, which describe information exchange and publication requirements together with other technical aspects.



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