
**EURELECTRIC Response to
EREG Consultation
“Draft Revised Guidelines of Good
Practice for Electricity Balancing Markets
Integration” (GGP – EBMI)**

SG Balancing & Intra-day Markets



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Guidelines of Good Practice for Electricity Balancing Markets
Integration” (GGP – EBMI)**

This paper has been prepared by the SG Balancing & Intra-day markets.

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EURELECTRIC Response to ERGEG Consultation “Draft Revised Guidelines of Good Practice for Electricity Balancing Markets Integration” (GGP – EBMI)

Introduction

EURELECTRIC welcomes the ERGEG Consultation and recognises it as a step forward towards the development of cross-border reserve and balancing markets within the context of the adoption of the third energy package. Consultation facilitates an early start of the interim period and is a way for market stakeholders to contribute to all major aspects of the cross-border balancing.

We believe that the launch of a workshop on the GGP for Electricity Reserve and Balancing Markets (as proposed in the Florence Forum in November 2008) after this consultation will bring additional benefits with regard to the quality of the final guidelines. Stakeholders should be given an opportunity to exchange views and ideas on this highly complex topic in an open and direct dialogue with the regulators.

1. General comments

EURELECTRIC considers that the framework of the draft good practice guidelines is well outlined and the issues addressed in the consultation are highly relevant. We strongly support the ERGEG’s views as to the three major benefits of reserve and balancing market integration:

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

However, EURELECTRIC would like to point out a number of comments to be considered in finalising ERGEG draft guidelines:

- **The objective laid down in the third energy package of creating regional markets requires in our view a much clearer stance in favour of integrating reserve and balancing markets.** While the guidelines merely leave this option open, they should have set out the steps and measures conducive to cross-border harmonised balancing markets. EURELECTRIC therefore strongly calls for the harmonisation of cross-border reserve and balancing markets underpinned with firm obligations placed upon TSOs to cooperate and harmonise their practices and standards. Regional operation centres dealing with balancing and reserve functions for two or more control areas would be more beneficial than cooperation and harmonisation. These centres could then be used to incorporate other system operation tasks that would lead to Regional Independent Operators¹. However, as these have not emerged yet the response in this paper is related to the situation where TSOs operate their own control area.
- **As details are as important as principles. In particular, in the area of reserve and balancing markets EURELECTRIC stresses the need to clarify concepts and definitions** (for example, automatically-activated/manually-activated vs. primary/secondary/tertiary reserves, interconnectors without congestion). Should this remain unaddressed, it is likely that the guidelines would unintentionally lead to diverging interpretations, thereby causing delay and hindering harmonisation of cross-border balancing markets.
- **Implementation steps towards developing cross-border reserve and balancing markets are intrinsically linked to progress on intra-day markets.** Therefore EURELECTRIC calls for organising the ERGEG workshop on cross border intra-day markets within a reasonable time from now. The workshop held in the CWE region shows that there is a clear support in favour of a fast implementation of a continuous trading platform with a centralised order book (COB) and that the regulators can play a leading role in this process.
- The guidelines explicitly handle cross-border issues. We think that it should be made clear that the guidelines generally apply to issues between control areas (there could be more in one country) and also apply where internal congestions lead to different price zones.

¹ See EURELECTRIC Discussion Paper: Towards Regional Independent Operators: a main driver for successful market integration

2. Specific comments

EURELECTRIC specific comments are related to:

- Key principles for efficient Electricity Balancing Markets and their Integration
- Revised Guidelines of Good Practice for Electricity Balancing Markets Integration.

For transparency reasons our comments are presented in line with the structure of the ERGEG consultation paper.

2.1 Comments on the Key Principles for efficient Electricity Balancing Markets and their Integration

Governance and institutional arrangements

EURELECTRIC supports ERGEG's view that coordination is strongly needed when dealing with cross-border reserve and balancing regulation. We believe, however, that this cross-border balancing services "regulatory gap", as well as relevant terms and conditions, for the provision of cross-border balancing services should be addressed by ACER. It is the Agency that has to be assigned with the competence to oversee or enforce any breach of rules, resolve conflicts or disputes as well as to approve or veto modifications to balancing market rules.

Operational security

EURELECTRIC believes that definition of security roles and responsibilities are very important and, therefore, need to be defined. At the same time, we believe that the issue of operational security responsibility should also be addressed from the point of market integration. TSOs should be obliged to enter into TSO-TSO agreements on a (sub)regional level in order to comply with the security need by sharing reserves, thereby increasing the stability and the reliability of the whole system. This should not undermine the market-based approach as described below.

Market based mechanisms

EURELECTRIC strongly advocates using market-based mechanisms in procuring reserve and balancing needs. In this context, we agree with the principle that any deviation from the merit order shall only be accepted when it is necessary to maintain system security. However, we want to stress here that such deviations should not influence the balancing settlement price if it is due to an internal congestion.

Effective competition

EURELECTRIC fully supports the removal of all types of entry barriers for new entrants in reserve and balancing markets. Apart from the barriers related to bids' placing and selection, we consider long term capacity reservation contracts as one of the major entry barriers to reserve markets. Removing this impediment (by reducing the duration of commitments) will allow more players to join the reserve and balancing mechanisms.

We also want to contribute to clarifying ERGEG's argument with regard to possibilities for certain players to exercise market power. Balancing market is characterised in general by relatively small volumes and high price volatility. At the same time, it is, on average, very difficult to consistently exercise market power as the number of participants able to supply small volumes needed for balancing is quite large; such a situation would be enhanced by the development of well functioning cross-border balancing markets. Moreover, a clear distinction has to be made when there is congestion: whenever a local problem arises, it has to be treated as congestion and its settlement price should not influence balancing settlement prices.

TSOs' qualification and technical requirements of the services should be as harmonised as possible. However, overly strict TSOs requirements may limit the number of players able to participate in the balancing market, thus hindering competition.

Impact on cross-border trade

EURELECTRIC agrees with the principle of maximising available capacity of the interconnections available to market players. We support the idea that cross-border balancing shall not lead to "undue" withdrawal of interconnection capacity from market players, nor shall it limit opportunities for cross-border trade.

We actually do not see any reason to withdraw interconnection capacity for cross-border balancing from the market. We therefore think that the term "undue" is not appropriate in that sentence.

EURELECTRIC believes that no capacity should be reserved either for intra-day cross-border trade, or for cross-border balancing purposes, when calculating day-ahead capacity. Only remaining capacity should be used for this purpose.

Incentives for balance responsible parties to be balanced

The obligation to be balanced is especially important in the electricity industry as a result of imbalances in real time influence system security. BRPs should be incentivised to be in balance. EURELECTRIC supports that marginal pricing should be market reflective and this will, by itself, provide the right incentives: there is no need for additional fees or penalties when a player is in imbalance.

Transparency

EURELECTRIC has no specific comments.

Market monitoring

EURELECTRIC has no specific comments.

Pragmatic approach

While generally supporting the idea of making reserve and balancing markets in different markets compatible as a first step in a process of evolution of reserve and balancing markets integration, EURELECTRIC calls for expanding the concept of “compatibility” of balancing mechanisms. This can include, for example, “harmonisation” of prequalification processes, as suggested in our Position Paper “Towards Market Integration of Reserve and Balancing Markets”².

Generation units (for primary, secondary, tertiary) and load units (for secondary and tertiary) that will be used for providing balancing services need an individual technical prequalification, which includes the capability of the installation of the provider (load and generation) and the communication lines (especially for secondary and tertiary reserves).

EURELECTRIC believes that progress in integrating reserve and balancing markets can be achieved through pilot projects in potentially dynamic regions (merging neighbouring control areas with similar balancing features). The short term target should be to establish ancillary services offices for procurement of balancing energy that are responsible for adjacent control areas or a region. To do so, it should be ensured that a specific market belongs to only one (integrated) balancing area at a certain moment in time. However, when congestion in another direction arises, a market can join another balancing region. We realise that this might require additional cooperation between TSOs.

2.2 ERGEG’s Draft Revision of the Guidelines of Good Practice for Electricity Balancing Markets Integration

1. Reservation of interconnection capacity (see 5.1 of ERGEG Guidelines)

EURELECTRIC agrees with the outlined principle that no cross-border capacity for should be reserved for balancing purposes. We believe that cross-border capacity should be allocated in the most efficient sequence³, which reflects the practices and needs of trade, and can be represented as follows:

- a. Long & medium term till day-ahead (no capacity reservation for intra-day or balancing);
- b. Unused net transfer capacity (NTC) for intra-day trade;
- c. Any remaining unused capacity for system reserve and balancing purposes.

Therefore, it is logical for capacity to be allocated starting from the long term and going to the real-time. As such, capacity should not be reserved for balancing purpose prior to the closure of the intra-day market. To ensure implementation of this, there should be no possibility to refer to unexpected flows, as balancing as such is a result of unexpected outcomes.

Moreover, introducing a guideline allowing for capacity reservation on non congested interconnectors is strictly speaking excessive, as capacity reserve as such is needed only in case of risk for congestion and therefore loses its importance on non congested lines.

² EURELECTRIC Position Paper “ Towards Market Integration of Reserves & Balancing Markets”, July 2008

³ This principle applies to all interconnectors except those who were granted an exemption pursuant to Article 7 of the cross-border electricity Regulation.

2. Charge on access to interconnection capacity (see 5.2 of ERGEG Guidelines)

EURELECTRIC believes that both types of interconnectors, regulated and merchant lines, should be covered by these Guidelines of Good Practice for Electricity Balancing Markets Integration. Non-used capacity of the merchant lines should be used for cross-border reserve and balancing purposes as this capacity is no longer available for the market after the gate closure and therefore has no further market value. Zero market value of this unused capacity makes it illogical to introduce pricing for its usage for balancing purposes and furthermore makes it difficult to define a level of prices to be set.

We also see strong benefits for merchant owners in making capacity available for balancing purposes. If such use creates additional grid losses in the merchant cable, TSOs should settle with the cable owners the associated costs.

3. Cross-border procurement of reserve capacity (see 6.1 of ERGEG Guidelines)

As a general point, we want to reiterate the importance of clarifying the term of “interconnectors with no congestion” and also point out that the distinction between automatically-activated vs. manually-activated reserves requires further clarification and alignment with the UCTE definition of primary, secondary and tertiary reserves.

In its Position Paper “Towards Market Integration of Reserves & Balancing Markets” EURELECTRIC used the UCTE classification and therefore considered both primary control and secondary control reserves as automatically-activated reserves and tertiary reserves – as manually-activated reserves.

We believe that the introduced definition of quantity limits for redistribution of primary control reserves through cross-border procurement (“relatively small percentage of control area requirements”) is too discretionary and should be expressed in clearer quantity terms. We also support the idea of setting these limits based on follow-up of the experiences rather than fully leaving it subject to the TSOs decision.

At the same time we want to stress that the limits for cross-border procurement of reserve capacity should not be unnecessarily tight, as it would hinder deriving benefits from reserves sharing. In order to avoid situations of “contracting reserve capacity twice” the TSOs should assess the cross-border capacity situation on day-ahead basis and decide to commonly use any competitive reserve capacity from abroad during the non-congested periods of time, whereby they should be allowed to review their position might physical changes require it.

With respect to three outlined considerations on primary control, we would like to point out to the following aspects:

- In case of the tripping of a plant participating in primary control reserves, the generator is bound to replace the plant with another one or should bare the replacement cost of substituting it with another plant
- Issue of ramping capability is in our view not relevant for primary reserves, but this might need further clarification.
- It is impossible to predict the location of a potential synchronous area split in advance and to take that into account when designing geographical structure of primary control reserves.

4. Cross-border procurement of balancing energy (see 6.2 of ERGEG Guidelines)

The definition of manually-activated balancing energy is not clearly outlined in the paper. We refer here to our view elaborated earlier in the paper on the distinction between on one hand primary/secondary reserves as automatic and on the other hand tertiary reserves as manual.

EURELECTRIC does not support the view that cross-border activation of balancing energy should be limited only to balancing energy related to manually-activated reserves. Against the backdrop of market integration process, the (potentially dynamic) merger of two (adjacent) control areas will allow to use commonly also secondary reserve during the period of time the merger is active and therefore these guidelines should be extended to allow also for cross-border procurement from automatically-activated reserves.

Besides, the benefits of cross-border procurement of balancing energy related to automatically-activated reserves are much bigger, given the high frequency of employing of those reserves compared to the manually-activated ones. The guidelines should not use the word cross-border 'trade' mechanisms, but rather refer to a mechanism to allow cross-border 'competition'. This because the TSOs are the central counterpart where market parties 'compete', but market parties cannot 'trade' amongst themselves.

5. Amount of reserve capacity (see 6.3 of ERGEG Guidelines)

EURELECTRIC has no specific comments.

6. Models for cross-border balancing (see 7 of ERGEG Guidelines)

EURELECTRIC supports the view of solely using the TSO-TSO approach as model for cross-border sharing reserves and balancing due to the very short-term nature of the balancing market. We strongly advocate for all the TSOs in a region to form a regional balancing market merit order taking actual transmission capacities/congestions into account. The TSO-TSO approach also leads to faster integration as a lower level of harmonisation is needed at the start.

The TSO-provider model should be avoided as it would even hamper the progress in harmonisation of balancing related rules and procedures, like gate closures and other technical characteristics.

As the TSO should be a neutral body in the balancing and reserve market it is very important that a high level of transparency of the TSO actions are is obtained.

7. Design of balancing markets (see 8 of ERGEG Guidelines)

EURELECTRIC calls for a much stronger and clearer imperative of harmonisation in balancing markets. We consider harmonisation as the major prerequisite for successful integration process of balancing markets and believe that the present guidelines are not prescriptive enough to effectively promote the integration process.

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.

In a situation where regulation in a relevant (invoicing) period (i.e. 15 minutes) is in one direction, the balancing settlement price is equal to the marginal balancing energy price as called by the TSO. If the TSO uses balancing energy in both directions in one period, two prices will exist: one for downward regulation and one for upward regulation.

Marginal prices provide the fairest and strongest incentives for BRPs to balance their portfolio. Therefore, the imbalance settlement price should be equal to the price of the marginal energy bid used for balancing the systems. This means that the price will be equal to the price of the last called bid in this balancing period. Because the selection will be in accordance with the merit order, this would be the most expensive bid.

Stronger volatility of marginal pricing compared to pay-as-bid pricing actually serves as an effective indicator of structural problems and signal the need for further investment as well as further integration.

The need for harmonisation is also strong with regard to settlement regimes. Preserving different settlement systems in adjacent areas will by definition lead to arbitrage, whilst integration of balancing markets will de facto eliminate market parties' interests to act in such a way. However, lack of harmonisation in settlement should not stop the integration process itself. The Nordic example shows that integration is possible without a harmonised settlement system, although it is not ideal.

We support ERGEG's view that BRPs should be given the right incentives to manage their own balance before entering the balancing market. However, this should not only be in the day-ahead market as stated in the ERGEG paper, but also in the intra-day market, as their positions can be prone to changes between day-ahead and 1 hour ahead point of time. To incentivise BRPs to actively participate in the intra-day market and minimise any imbalances providers of balancing energy should be able to adjust up their bids to the point of the closure of the intra-day market.

EURELECTRIC stresses a need for a clear definition and distinction between "balancing needs" and "congestion needs" as congestion costs should not influence the balancing settlement outcome.

8. Transparency and monitoring (see 9 of ERGEG Guidelines)

EURELECTRIC recommends including one missing item "real time imbalance signal" into the data to be made available.