

TSOs proposal for an implementation framework for the exchange of balancing energy from Replacement Reserves

EFET response – 4 April 2018

The European Federation of Energy Traders (EFET¹) thanks the European TSOs for this opportunity to provide feedback on their proposal of an implementation framework for the exchange of balancing energy from Replacement Reserves. Our response to this consultation should be considered in the broader context of our input on the TERRE project at Balancing Stakeholder Group meetings and through consultation responses over the past few years².

Feedback related to the introductory Article 1 and Article 2

Our main concern relates to the objective of Replacement Reserves of “maximization of social welfare”. The objective should be further specified: maximization of social welfare should not be considered only for RR, but in larger scope (of which RR is just a part). The TERRE project can of course contribute to the overall maximization of social welfare, but this should be done by providing a clear signal to the market through cost-efficient procurement of its balancing energy. The Electricity Balancing Guideline (EBGL) clearly reflects this reasoning in its objective of improved cost-efficiency and reduction in system imbalance and costs for society (EBGL Recital 11 and 14). The EBGL does not consider or mention the maximization of social welfare as an objective for the balancing market alone, and thus even less so for an individual balancing process. EFET took note of the explanation provided by TSO at the stakeholder workshop of 19 March 2018, but remain opposed to the current principles. Indeed, considering the RR process in isolation for any calculation of social welfare would be incomplete and would risk creating distortion and de-optimisation in other processes. The main objective of the RR process should thus be brought into line with the EBGL, i.e. the cost-efficient procurement of balancing energy. Should any consideration be given to the maximisation of social welfare, this should be done in a broader approach including other balancing platforms and other market timeframes, in particular the intraday timeframe.

¹ The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent and liquid wholesale markets, unhindered by national borders or other undue obstacles. EFET currently represents more than 100 energy trading companies, active in over 27 European countries. For more information: www.efet.org

² See notably our responses to the TSOs/ENTSO-E consultations on the TERRE project dated 16 August 2017, available at: http://www.efet.org/Files/Documents/Downloads/EFET_TERRE%20consultation_160817.pdf; dated 31 March 2016, available at: http://www.efet.org/Files/Documents/Electricity%20Market/Spot%20and%20short-term%20markets/EFET_TERRE-consultation_31032016.pdf.

Another concern for EFET is the lack of consideration on local aspects of the project. Whilst local implementation is a responsibility of national bodies, we still consider that ensuring level-playing field should be a key concern for the project. Therefore, we recommend that an overall follow up of the local aspects is ensured by the project.

The RRIF is referring to the explanatory document for a list of participating RR TSOs in article 1.1. EFET considers that the binding document should contain all necessary information.

Feedback on Article 3: High-level design of the RR-Platform

Article 3 (1) (a) refers to the process where offers that are deemed 'coherent' with the RR standard products by the connecting TSOs are forwarded to the RR-platform. It is not clear from the text – nor from the explanatory document – what criteria are considered to evaluate whether an offer is coherent with the Standard Product. At the workshop, TSOs explained that 'coherent' meant 'standard product'. We hence recommend clarifying the text to remove any ambiguity.

Feedback on Article 4: The roadmap and timeline for the implementation of the RR-Platform

Article 4 (1) refers to the fulfilment of "further requirements by the GL EB" to consider the RR-Platform to be formally implemented. It is not clear what further requirements by the Guideline are considered relevant for the formal implementation of the RR-Platform. RR TSOs need to clarify what these "further requirements by the GLEB" relate to and which extra conditions they add to the Implementation Framework. If they have all already been included in the Implementation Framework, then the reference could be deleted.

Article 4 (5): the last sentence should read "A TSO may request a derogation from this requirement **to its regulatory authority** (Article 62 GL EB). **The request shall be duly justified according to article 62.5 GL EB.**"

Article 4 (6): the introductory sentence should read "The TERRE project **aims to establish** the main market functioning of the RR-Platform following Article 4 (5) of this RRIF." The RRIF is a binding document, tentative formulations such as "aims to" have no place in it.

Article 4 (6) (c):

- the first sentence should read "The parallel run phase will encompass the participation of the RR TSOs and the national BSPs **if needed**." The involvement of BSPs in the parallel run should not be an option TSOs can do without, even in central dispatch countries.
- in the last sentence, we appreciate the inclusion of a tentative date for the parallel run (Q2 2019). We understand that this date will primarily depend on the date of the NRA approval of the RRIF. Hence, a target date linked to that approval may be more appropriate (e.g. 6 months

after the NRA approval of the RRIF). Also it is important that both BSPs and TSOs gather sufficient experience from the parallel run. Hence we believe that the RRIF should include a requirement for a parallel run of at least 6 months.

Feedback on Article 5: Functions of the RR-Platform

The description of the functions of the platform are very succinct, to say the least.

Article 5 (1) (a) does not include any description of the Activation Optimisation Function (AOF). We remind the TSOs that whatever is in their Explanatory Document is not legally binding, and hence details on the AOF should be included in the RRIF.

In particular, we are worried of the inclusion of a possibility for TSOs to perform counter-activations via the AOF. We generally do not agree to allow counter-activations by TSOs in TERRE, should such counter-activations go beyond what is strictly necessary to meet the balancing needs of a TSO. Counter-activations that clear bids between market participants that are not related to the balancing needs of a TSO exceed the boundaries of the balancing energy procurement process that is the objective of the TERRE platform. As a result, the TERRE platform would become a hybrid market of balancing energy procurement and intraday auction.

In response to stakeholders' concerns with regard to the impact of counter-activations on the intraday market, TSOs purport to have done an "impact assessment" on the matter in the explanatory document accompanying the RRIF. In a couple of paragraph without evidence, the TERRE TSOs conclude that counter-activations will have no impact on the liquidity of intraday market. This assertion omits the point that the TERRE platform would offer market participants a way to trade across borders closer to real-time than the XB ID allows. This should also be seen together with the fact that the TERRE project foresees a BE GCT that is possibly concomitant with the ID XB GCT (see our comments on article 7), which means that the full results of the XB ID may not yet available at BE GCT. This leads to the same result, i.e. that market participants will have to make a choice between participating in the last minutes of the continuous intraday market before XB GCT or submitting offers on the TERRE platform. In this case, the possibility for counter-activations will directly impact the liquidity of XBID (see our response to question 3.5 for more details on the subject).

As mentioned in our comments on article 1 and 2, regarding the overall objective of the TERRE platform, we reiterate our belief that the goal is to minimise activations: balancing mechanisms in general should be designed to fulfil the balancing **needs** of TSOs, and the cost of this should be an incentive towards BRPs to balance their portfolio in previous timeframes, especially the day-ahead/intraday market. The inclusion of counter-activations pollutes the imbalance price with market activities. The TERRE platform design should

focus on allowing TSOs to procure balancing energy as efficiently as possible. Counter-activations, on the other hand, are rather linked to optimising social welfare. While we appreciate TSOs concerns on this matter – which we would have liked to see make their way in other implementation methodologies such as the Capacity Calculation Methodologies of the CACM Guideline³ – we believe that social welfare ought to be assessed beyond the RR process. For us, as long as market participants still have means to optimise social welfare (via the intraday market), such optimisation will happen by letting market participants the opportunity to balance their portfolios as close to real time as possible and by ensuring that TSO actions in the activation of RR are only based on TSO needs, hence fully understandable by the market.

We note the intention of the TSOs in the explanatory document to monitor “the frequency, the volume and the impact of counter- activations on cross-zonal marginal price, URBs, computational time and social welfare during the parallel run phase and a predefined operational period RR-Platform”. We do not agree with this approach: a firm decision not to allow counter-activations should be taken before even the parallel run. We do not believe the question of the merits of counter-activations will be resolved by monitoring that is proposed in the explanatory document. The difficulty with counter-activations is not the frequency of their occurrence, but rather the fundamental market design question of whether or not market deals should take place in a balancing procurement environment. Moreover, as explained previously, we expect an impact on the intraday liquidity as a result of market participants adjusting their bidding behaviour to the choice to make between intraday and TERRE. Such change in behaviour will not occur in the parallel run but only gradually once TERRE goes live. As a result, any result of such an analysis will underestimate the detrimental impacts. EFET therefore asks that TSOs (and thereafter NRAs) make a clear choice on how cross-border intraday markets and the TERRE platform should interact before the TERRE platform goes live.

Finally, the question of counter-activations is largely caused by the proposed ability of TSOs to define their needs in an elastic manner (see our comments on article 11 of the RRIF). This creates a demand-supply curve that is very similar to, e.g., the day-ahead market. If, on the other hand, the TSO imbalance needs would be systematically expressed in a non-elastic manner, the imbalance needs of all TSOs could first be netted and subsequently matched with the upward or downward merit order list. This would make the process faster, more efficient and more transparent.

Feedback on Article 6: Definition of the RR Standard Products

EFET would like to get explanation why the maximum MW quantity of the RR product will be defined at local level in case of indivisible bids. Differences in the ability of BSPs to offer a volume of indivisible bids distort the level-playing

³ See our response to the TSOs proposals of Capacity Calculation Methodologies, last updated on 22 March 2018, available at: http://www.efet.org/Files/Documents/Downloads/EFET_Eurelectric_MPP_Nordenergi-TSOs%20consultation%20CCM_22032018.pdf

field on the RR-Platform. The maximum quantity for indivisible bids should rather be defined at RR-Platform level.

Feedback on Article 7: Gate closure time for RR standard product energy bids

We believe the RRIF should already at this stage set a precise BE GCT for the RR standard product, namely at H-55 minutes. We would strongly disagree with establishing the BE GCT at H-60 minutes. Indeed, as the XB ID GCT is also set at H-60 minutes, BSPs would not be able to take into account the final results of the XBID into their offers for the TERRE platform. As a result, market participants will have to make mutually exclusive choice during the last moments of XBID to bid their capacity either in XBID or in TERRE. This will result in loss of liquidity in one or both markets and would imply a *de facto* move of the ID XB GCT further away from real-time than the current H-60 minutes. This goes at least against the CACM Guideline that foresees an ID XB GCT of H-60 minutes.

A BE GCT for the RR standard product at H-55 minutes would start alleviating these concerns⁴. We remind the TSOs that this compromise would already leave a very short time (5 minutes) to market participants to integrate XBID results in their bidding for RR. A BE GCT for the RR process at most 55 minutes ahead of real time seems to us the minimum non-negotiable standard to ensure that the RR process respects Recital 12, and article 3 of the EB GL.

Should the final RRIF proposal nonetheless not contain a precise timing for the BE GCT, then the governance for the adoption of the final decision on this crucial point should be much clearer. We understand from the workshop of 19 March 2018 that discussions will take place between TSOs and NRAs after the parallel run. We believe that this would constitute a circumvention of article 19 (3) (h) of the EBGL: the precise BE GCT should be in the form of a transparent RR TSOs proposal (with appropriate justification based on the parallel run results), open to stakeholder comments, and formally approved by NRAs.

Feedback on Article 8: TSO energy bid submission gate closure time for RR

No comment.

Feedback on Article 9: Common merit order lists to be organised by the activation optimisation function

⁴ We observe that under Article 8 of the RRIF, the TSO energy bid submission gate has a range of 9 minutes between H-45 minutes and H-36 minutes before real-time. It is not fully clear why a similar range of between 60 minutes and 51 minutes before real-time cannot be considered for the Balancing Energy Gate Closure Time.

Article 9 (4) refers to the submission of energy bids by the connecting TSO to the RR-Platform if they are deemed 'coherent'. We reiterate our concerns mentioned in article 3.

The process does not explicitly refer to any bid filtering of unavailable bids, something that the explanatory document clearly indicates will be part of the RR bid submission process (chapter 11 of the explanatory process). Should there be any bid filtering, a precise description should be provided in the RRIF itself, which is the only binding document of this TSO proposal.

Regarding the flagging of bids as unavailable, while EFET fully understands the related physical constraints behind such restrictions, we believe that solving this through a system of unavailable bids is not the correct way.

Ideally, congestion would be dealt with in a separate mechanism or at least in a way that allows a clear distinction between balancing and congestion actions. This makes the cost of dealing with congestion apparent instead of hiding it through changes in the balancing market outcome. This would facilitate the allocation of costs to congestion management on the one hand, and balancing on the other hand, only the latter having an influence on the imbalance price.

If TSOs insist on using the balancing energy bids of the TERRE platform to manage congestion, it should at least closely mirror how it would be treated in a separate mechanism. This includes:

- sufficient transparency to identify which bids are marked unavailable by TSOs, and
- payment to market participants that suffer opportunity losses

Regarding the first element, the first element of transparency concerns the RRIF itself: the RRIF should explicitly state the reasons for which a bid can be flagged as 'unavailable' for the RR-Platform, something that is currently only being mentioned in the non-binding explanatory document. Second, TSOs should provide appropriate transparency on the bids that have been marked unavailable, so that market participants and regulators can monitor TSO actions and ensure that TSOs apply a clear distinction between balancing and congestion management actions. This is especially pressing in Central Dispatch Systems (CDS) where Integrated Scheduling Process (ISP) bids are converted by the TSO into RR Standard Products. This process makes it especially difficult for market participants to assess to which degree their capacity is offered on the TERRE platform or withheld by the TSO for congestion or margin reasons.

Regarding the second element, it is indeed only fair that market participants that are barred from participating in a balancing process for congestion management reasons are duly compensated by the relevant TSO. In a zonal system, all pre-qualified BSPs within a zone are supposed to be able to respond on a non-discriminatory basis to TSO balancing energy offers. Contrary to balancing, the financial responsibility of which falls onto BRPs, congestion

management is a task of TSOs, who need to bear financial responsibility for it. Should congestion management actions not be transparently identified and affected BSPs not be compensated, then performing congestion management by blocking bids from participation to the RR-Platform would provide TSOs with a free congestion management service, at the expense of BSPs. Compensating BSPs for their opportunity loss when their bids are marked as unavailable is comparable to, e.g., first being activated upwards on the RR Platform and subsequently activated downwards in a congestion mechanism if separate balancing and congestion management mechanisms were used.

The situation is similar for bids made unavailable for local lack of margin. Ideally, TSOs pre-contract sufficient balancing capacity to ensure the necessary balancing margin instead of counting on sufficient capacity being available at any time. If TSOs insist on reserving certain bids in the TERRE platform, the associated BSP incurring an opportunity loss should be remunerated. This is irrespective of whether the BSP is subsequently activated to ensure sufficient local margin or not, as the BSP will in any case not regain the difference between the bid price and the pay-as-cleared price on the TERRE platform.

Such a system has the added value that, if costs are properly allocated, it will not increase the imbalance price. Energy regulators will use their monitoring and sanction powers to ensure that the common balancing/congestion management merit order is not misused by market participants to artificially inflate congestion management expenditures.

Feedback on Article 10: Rules for governance and operation of entity operating the platform and proposed designated entity

We would welcome a stronger commitment of TSOs to properly gather input for and inform market participants of any decisions affecting the functioning of the TERRE project and RR platform. This should be more explicitly stated than in the sibylline “validates analysis and outputs from the expert groups” of article 10 (2) (b) iv.

Feedback on Article 11: Framework for harmonization of terms and conditions

Article 11 (1): we do not agree with the proposal of TSOs to use elastic imbalance needs. By pricing their bids and offers, and putting them on the CMOL together with bids and offers from market parties, TSOs would be directly active on the market. This would be a serious breach of the unbundling principles embedded in EU legislation. In this way, TSOs would be in a position to set the settlement price and impose *de facto* price caps on the market. TSOs would be marketing the energy from their imbalances, instead of procuring balancing energy to deal with their imbalances.

During the workshop of 19 March 2018, the TSOs explained that they see several reasons for which they need elastic demand:

1. TSO want to prevent the price of RR to “spike”, as they are concerned by a lack of liquidity on the RR platform
2. TSO want to cap the price of RR to the level of alternative balancing products, such as specific products
3. TSO want to cap the price of RR to the level of the expected price of mFRR

EFET strongly disagrees with these 3 motivations:

- The fear for low liquidity should not be a motivation to introduce price caps. Explicit or de facto price caps are not only wrong from an economics standpoint, they are also unlawful with regard to the EBGL: In its article 30.2, the Guideline makes it very clear that price limits can only be applied for technical reasons (IT, algorithm), and be reflective of the value of lost load. As mentioned in our paper on the free formation of prices⁵, we believe that energy prices should be allowed to reflect the true value of scarcity during times of system stress and high demand for power; similarly, when energy is in abundance prices should be allowed to reflect the value of displacing that generation and even go negative – which would give signals for storage operators/investments if they are not caused by out of the market reasons. Likewise, the volatility of energy prices, when not induced by flows in the market design – e.g. lack of transparency, excessive reserve margins, or any other distortion to price formation – is a sign that the market reacts appropriately and fast to demand and supply signals.
- Specific products are supposed to be temporary measures, aiming at facilitating the transition from current national balancing market towards an integrated EU balancing market. They do not follow the same transparency and pricing rules. Hence, using them as a benchmark – or even worst, as a price cap – for standard products introduces serious distortions in the future integrated market.
- Capping the purchase price of replacement reserve to the “expected price of tertiary reserve” would imply that TSOs speculate on the evolution of electricity prices. Allowing TSO to perform a speculative activity would simply violate basic though crucial unbundling rules.

We therefore strongly urge NRAs to carefully analyse these elements and reconsider their proposal on this article.

Should the TSOs persist in their proposal to use elastic balancing needs, then the establishment of the volume of the need flexibility should be made fully transparent. The exact cost of procuring a slightly larger or lower volume of balancing energy should not only be benchmarked by the resulting cost of the TERRE outcome, but also by any cost incurred by any subsequent counter-

⁵ The importance of free formation of prices in the European wholesale electricity market, dated 2 June 2016, available at: http://www.efet.org/Files/Documents/Electricity%20Market/General%20market%20design%20and%20governance/EFET_Free-formation-of-prices-power-market.pdf.

activation (if allowed) of other balancing products to correct for this additional volume.

Article 11 (2): we agree with the interconnection controllability as a tool for TSOs to relieve cross-border congestion. However, two important conditions we mentioned previously are not detailed in the RRIF, but should be met:

- Sufficient transparency should be provided for market participants to understand that an interconnection controllability action has been performed and what the result of this action was (constrained versus unconstrained outcome).
- Bids that were not activated due to an interconnection controllability action suffer opportunity loss (difference between bid price and pay-as-cleared market outcome) and should be remunerated for this. Otherwise, TSOs would be under-incentivised to solve the associated congestion.

Article 11 (3): we agree with the TSOs proposal not to apply caps or floors for RR balancing energy offers, and that only technical clearing price limits may apply.

Article 11 (4): we agree with the objective of a decrease in the commercial scheduling step towards 15 minutes at the go-live of the RR platform. BRPs should have a similar ability to self-balance their perimeter as TSOs have to solve any residual imbalances.

Feedback on Article 12: Cost Sharing Principles

No comment.

Feedback on Article 13: Description of the optimisation algorithm

Article 13 (2): As mentioned in our comments to article 1, 2 and 5 of the RRIF, we believe that the overall objective of the TERRE platform is to minimise activations, not maximise social welfare in isolation of the energy market: balancing mechanisms in general should be designed to fulfil the balancing **needs** of TSOs, and the cost of this should be an incentive towards BRPs to balance their portfolio in previous timeframes, especially the day-ahead/intraday market. The TERRE platform design should focus on allowing TSOs to procure balancing energy as efficiently as possible. While we appreciate TSOs concerns on this matter – which, again, we would have liked to see make their way in other implementation methodologies such as the Capacity Calculation Methodologies of the CACM Guideline – we believe that social welfare ought to be assessed beyond the RR process. For us, as long as market participants still have means to optimise social welfare (via the intraday market), such optimisation will happen by letting market participants the opportunity to balance their portfolios as close to real time as possible and by ensuring that TSO actions in the activation of RR are only based on TSO needs, hence fully understandable by the market.

The constraint of Article 13 (3) (a) (“the sum of all injections and withdrawals of RR across all bidding zones must be zero”) is strange given that the first objective of the RR-Platform would be to remedy imbalances. This would seem to require that the RR process result in the net activation of either upward or downward balancing capacity. Even if the TSO balancing needs are included in the injections and withdrawals, it is not obvious that the outcome would be a zero sum if some needs are elastic and therefore not fulfilled. EFET therefore questions the relevance of this constraint, which should at least be rephrased.

Article 13 (5) merely mentions the application of a fall-back procedure, which is however further elaborated in the explanatory document. EFET would consider it relevant that the main features of the fall-back procedure would also be included in the RRIF itself.

Feedback on Article 14: Language

No comment.

General comments on the proposal

First, we would like to remind the TSOs that whatever is in their Explanatory Document is not legally binding. The RRIF lacks the necessary details, especially on the functioning of the RR platform (article 5 of the RRIF).

Second, we regret that despite repeated comments from market participants, the RRIF does not foresee the possibility for BSPs located in control areas where TSOs do not perform the RR process to offer RR energy directly on the platform via a cross-border BSP-TSO option.

On transparency, we once again stress the need for TSOs to commit to properly gathering input for and inform market participants of any decisions affecting the functioning of the TERRE project and RR platform.

Transparency of the TSO actions is also of primary importance. We request that the following data be systematically published:

- Capacity – Price curve
- Information on the cross-border capacity: how much is available/used; which borders were constraining?
- Information on interconnection controllability actions: differences between constrained and unconstrained auction outcomes
- If the formulation of elastic imbalance needs is allowed by the NRAs: bidding structure by each TSO (volume and prices of elastic imbalance needs)

While the harmonisation of national balancing frameworks is not properly speaking in the scope of the RRIF, we remind TSOs of the importance to ensure basic harmonisation of their national framework to allow market participants to compete on a level-playing field. We consider the following three elements as high priority for harmonisation:

- Balancing Energy Deviation Settlement Price, including any additional penalties or market regulation rules
- Imbalance Adjustment
- Removal of national caps and floors to the bidding price (partly addressed in article 11 (3)).

Generally, we are worried about the lack of information on the on-going processes for the local implementation. Market parties need sufficient time to adjust their processes and systems to the new TERRE requirements. This means that for a parallel run in the second half of 2019, the requirements should be available at the latest by Q3 2018. Without a sufficiently long time-horizon for implementation, participation to the parallel run and the TERRE platform from the beginning may not be possible.

Moreover, the requirements of local implementation should be established in consultation with local stakeholders. For this, at least one consultation on the TERRE implementation at the local level should be organised, ideally combined with a more interactive and iterative process of stakeholder feedback. Given the timing ambition for the parallel run and go-live, the urgency for these elements is increasing. We therefore ask the TERRE project team to stress with each individual TSO the importance of such transparency and stakeholder interaction for the smooth implementation of TERRE.