



Hansa TSOs' methodology proposal for a market-based allocation process of cross-zonal capacity for the exchange of balancing capacity



EFET response – 21 October 2019

The European Federation of Energy Traders (EFET) welcomes the opportunity to provide comments on the Hansa TSOs' proposal of cross-zonal capacity allocation for the exchange of balancing capacity, in accordance with article 41 of the Electricity Balancing Guideline (EB GL).

General comments on capacity reservation by the TSOs for balancing purposes:

Since the early stage of drafting of the Electricity Balancing network code, we have opposed the concept of reservation of cross-border transmission capacity by the TSOs for balancing purposes. Though by the time of the adoption of the EB GL, the concept was rebranded as "cross-zonal allocation of capacity", its effects remain the same.

The cross-border reservation of transmission capacity by the TSOs for balancing purposes poses a serious risk to the availability of cross-border transmission capacity in the preceding trading timeframes. By allocating transmission capacity specifically for use in the balancing timeframe, TSOs remove available capacity from the allocation in the other timeframes, thereby restricting market participants' ability to adjust their positions across borders in the most economically efficient manner, and to contribute to overall system balance.

The use of cross-border transmission capacity is a key element of European market integration in the forward, day-ahead and intraday timeframes. A major objective of integration projects such as the EU Harmonised Allocation Rules for forward transmission rights, as well as single day-ahead and intraday coupling are to improve the access and use of such transmission capacity by the market. Reserving capacity (from the forward timeframe until the intraday market) for use by the TSOs in the balancing timeframe would turn the clock back on those improvements.

General comments on the so-called “market-based” method for capacity reservation by the TSOs for balancing purposes:

First, the so-called “market-based” method for capacity reservation by the TSOs for balancing purposes is based on a tool optimising actual balancing capacity bids with forecasted day-ahead bids. The allocation process is based on the forecasted market value of cross-zonal capacity for energy bids. The comparison with the actual value of balancing capacity bids is therefore reliant on estimations made by TSOs based on values from the past and not for the delivery day under consideration. We therefore consider that the “market-based” designation chosen for this cross-zonal capacity reservation process is incorrect. While this process reduces complexity, notably in terms of the functioning of the Euphemia algorithm, compared to the co-optimisation method according to article 40 EB GL, it is based on a fundamental uncertainty as to the value of cross-zonal capacity in the day-ahead market. Changes in the bidding behaviour of market participants compared to what the TSOs have modelled or are expecting should not be underestimated. Besides, ignoring the intraday market in the cross-zonal capacity reservation process, in practice, forecloses opportunities for market participants to adjust their positions. Ignoring the intraday market, in practice, forecloses opportunities for market participants to adjust their positions in intraday across borders and will lead to changes in the bidding process.

Second, the methodology for calculating the market value of cross-zonal capacity reserved for the exchange of balancing energy or sharing of reserves in the current proposal relies on the selection of “reference days” and possible “adjustment factors”. Neither of the two components is specified further. We therefore strongly doubt that the current proposal is in line with Article 41.1(b) EB GL that explicitly requests a “detailed description on how to determine [...] the forecasted market value of cross-zonal capacity for the exchange of energy”. Referring to concepts of “reference days” and “adjustment factors” and postponing the definition of such elements to the BCC proposals is insufficient.

Third, in the context of the implementation of article 16 of the recast Electricity Regulation approved as part of the Clean Energy Package (Regulation (EU) 2019/943), the TSOs will need to allocate to the market a minimum of 70% transmission capacity respecting operational security limits after deduction of contingencies. As the transmission capacity reserved by the TSOs through the “market-based” allocation process would be used by the TSOs themselves for the exchange of balancing capacity or the sharing of reserves, we would welcome a clear statement by the TSOs that this capacity will not be counted within the minimum 70% threshold.

Finally, article 38.8 of the EB GL requires a regular assessment of the need to reserve capacity for balancing purposes. In line with the spirit of this article, we would have expected a thorough assessment of the need to reserve cross-zonal capacity for balancing purposes in the Hansa region. There was, however, no real discussion or presentation by the Hansa TSOs of the need, benefits and drawbacks of cross-zonal capacity reservation for balancing purposes in general, let alone on the so-called “market-based” approach for such reservation. To date, we remain unconvinced of the necessity of such a market design feature. Contrary to the methodology on capacity reservation for balancing through co-optimisation according to article 40 EB GL, the development of the present methodology for a “market-based” cross-zonal capacity allocation for the exchange of balancing capacity or sharing of reserves proposal

according to article 41 EB GL is not an obligatory requirement. Given the overall lack of justification for cross-zonal capacity reservation for balancing purposes, and the missing impact assessment regarding the effects of a so-called “market-based” cross-zonal capacity allocation for the exchange of balancing capacity or sharing of reserves in particular, **we invite Hansa TSOs to withdraw their proposal altogether.**

Should Hansa TSOs persist to issue this methodology, we invite individual Hansa TSOs and NRAs to refrain from implementing this cross-border capacity reservation process, or any of the two others foreseen by the EB GL (co-optimisation under article 40, and the so-called “economic efficiency” allocation method under article 42).

Comments on individual articles:

- ***Recital 3:*** *The goal of the EBGL is to establish an EU-wide set of technical, operational and market rules to govern the functioning of electricity balancing markets. It sets out rules for the procurement of balancing capacity, the activation of balancing energy and the financial settlement of balance responsible parties. It also requires the development of harmonised methodologies for the allocation of CZC for balancing purposes. Such rules will increase the liquidity of short-term markets by allowing for more cross-zonal trade and for a more efficient use of the existing grid for the purposes of balancing energy.*

This recital gives the false idea that the current methodology development is a requirement of the EB GL. The development of a methodology for the “market-based” allocation of cross-zonal capacity allocation for the exchange of balancing capacity is only a possibility given to the TSOs of each CCM. We request the modification of this first part of the recital.

Further, we fundamentally oppose the statement that the reservation of cross-zonal capacity by the TSOs for balancing purposes would or could, in any way, “increase the liquidity of short-term markets by allowing for more cross-zonal trade”. How could possibly a measure that restricts the availability of capacity ever result in increased liquidity on energy markets and lead to more cross-zonal trade? We are puzzled by how the TSOs could come to such a conclusion and include it in the recital of a legally binding document. We request the deletion of this second part of the recital.

- ***Recital 11:*** *The Hansa MB Methodology contributes and does not in any way hamper the achievement of the objectives of Article 3 of the EBGL. In particular, the Hansa MB Methodology serves the objectives of fostering effective competition, non-discrimination and transparency in balancing markets (Article 3(1)(a) of the EBGL), enhancing efficiency of balancing as well as efficiency of European and national balancing markets (Article 3(1)(b) of the EBGL), integrating balancing markets and promoting the possibilities for exchanges of balancing services while contributing to operational security (Article 3(1)(c) of the EBGL), contributing to the efficient long-term operation and development of*

the electricity transmission system and electricity sector in the Union while facilitating the efficient and consistent functioning of day-ahead, intraday and balancing markets (Article 3(1)(d)) of the EBGL) and ensuring that the procurement of balancing services is fair, objective, transparent and market-based, avoids undue barriers to entry for new entrants, fosters the liquidity of balancing markets while preventing undue distortions within the internal market in electricity (Article 3(1)(e) of the EBGL).

We challenge the assertion of the TSOs that cross-zonal capacity reservation in general, and this methodology for a “market-based” method of cross-zonal capacity reservation, would facilitate “the efficient and consistent functioning of day-ahead, intraday and balancing markets” (article 3.1.d EB GL). By allocating transmission capacity specifically for use in the balancing timeframe, TSOs remove available capacity from the allocation in the other timeframes, thereby restricting market participants’ ability to adjust their positions across borders in the most economically efficient manner, and to contribute to overall system balance.

The TSOs have not provided evidence that the present methodology would actually not violate the principle of article 3.1.d EB GL. At the very least, we would like to see any reference to a positive contribution to the functioning of day-ahead and intraday markets removed from this recital.

- **Recital 15:** *In conclusion, the Hansa MB Methodology contributes to the general objectives of the EBGL to the benefit of all market participants and electricity end consumers.*

This recital concludes, without any proper demonstration, that this methodology is beneficial to all market participants and electricity consumers. We challenge this assertion of the TSOs, and would welcome the publication of the factual analysis we expect them to have performed to come to such a conclusion.

This recital actually calls for TSOs to perform and publish a cost-benefit analysis (CBA) before implementing a balancing capacity cooperation (BCC). The performance of a CBA is actually foreseen in the CORE TSOs’ methodology proposal on the same subject (article 3.1 of the CORE TSOs’ proposal). We request the inclusion of the following requirements in the main body of the Hansa TSOs’ proposal:

- the Hansa TSOs that want to establish a BCC shall share with Hansa TSOs the cost-benefit analysis of such a BCC
- the CBA shall also be distributed to Hansa NRAs and market participants
- the decision to establish a BCC shall be excluded unless the CBA is positive
- the relevant NRAs’ decision to approve or not a BCC shall take account of the results of the CBA

Besides, we miss in this methodology the regular assessment to be performed by TSOs with regard to the continued necessity or not of a BCC according to article 38.8 EB GL. This provision is actually included in the CORE TSOs’ draft methodology for the “economic efficiency” method of cross-zonal capacity reservation for balancing (article 42 EB GL), at the article 3.9 of that methodology. We would like to see a similar provision (complemented with a precise timing for the regularity of the checks

and an obligation to disclose these assessments to the relevant NRAs and market participants).

- **Article 3:** *Market principles of each balancing capacity cooperation in the CCR Hansa applying MB*

The article is missing the following specifications:

- limitation of the BCC to standard balancing capacity products according to article 25.2
- information on the minimum and maximum contracting period
- harmonisation of pricing rules within each BCC

An additional requirement should be formulated in article 3, stating that the calculation of the CZCA must not take longer than selecting bids without using a BCC, which should essentially be a few minutes (if not seconds). With sequential day-ahead procurement of FCR, aFRR and mFRR, market participants will be forced to prepare bids for subsequent markets in less than one hour already. Any additional delay in the publication of accepted bids will certainly result in a loss of efficiency – which otherwise should be included in the CBA.

- **Article 3.2:** *The CZC allocated for the exchange of balancing capacity and/or sharing of reserves per product (either RR, mFRR or aFRR) that will not be used in the relevant timeframe by the Hansa TSOs which allocated it, shall be released to all TSOs of the same timeframe if possible, and at least, shall be released to all TSOs for the exchange of balancing energy with shorter activation times or for operating the imbalance netting process.*

We welcome the clarification that cross-zonal capacity reserved for a specific product that was not used for this process shall be made available again for the exchange of balancing energy by all TSOs of the CCR in the same process or in processes with shorter timeframes, in accordance with article 38.9 EB GL.

This paragraph is, however, partially repeated in article 9.2. Please make sure the text of the methodology does not reiterate the same rules multiple times.

- **Article 4.2:** *The Hansa TSOs of each balancing capacity cooperation shall make the notification at least 3 months before the CZC allocation process enters into operation.*

We ask that the full methodology, including the forecast technique, is also shared with market participants and consulted upon. The forecast technique being at the heart of the MB CZCA, full transparency on the process is required.

Market participants can provide valuable input concerning issues of the market value of cross-zonal capacity and should therefore be included into the assessment of the BCC proposal, which is to be considered in the timeline of communication.

- **Article 5.1:** *This methodology imposes no further limitations on the maximum volume of CZC to be allocated for the exchange of balancing capacity or sharing of reserves according to Article 41(2) of the EBGL.*

It should be clearly stated the 10% are applied over CZCA for all of the balancing processes, not 10% for each of aFRR, mFRR and RR, possibly summing up to 30%.

- **Article 5.2:** *The use of additional limits by each balancing capacity cooperation for the maximum volume of allocated CZC for the exchange of balancing capacity or sharing or reserves shall be set out in the proposal according to article 33(1) of the EBGL.*

We would welcome a clearer wording that individual BCCs can set only a lower threshold than the maximum 10% of available cross-zonal capacity referred to in article 41.2 EB GL.

- **Article 6.5:** *The forecasted market value of CZC for the exchange of energy between two bidding zones in the day-ahead market timeframe shall be calculated for each day-ahead MTU.*

The article enshrines that the value of cross-zonal capacity is only compared between the forecasted DA market value and the value of balancing capacity, without taking account of the value of that capacity in the intraday timeframe. Ignoring the intraday market, in practice, forecloses opportunities for market participants to adjust their positions in intraday across borders. This contradicts some of the most fundamental principles in the EB GL itself:

Recital 12 “The integration of balancing energy markets should facilitate the efficient functioning of the intraday market in order to provide the possibility for market participants to balance themselves as close as possible to real time.”

Article 3.2.e “When applying this Regulation, Member States, relevant regulatory authorities, and system operators shall ensure that the development of the forward, day-ahead and intraday markets is not compromised.”

Article 39.2 EB GL explicitly requests the inclusion of the intraday timeframe into the calculation of the market value for the exchange of energy “where relevant and possible”. Presumably, the relevance is undisputable and even though it is difficult to estimate the value contribution of the intraday timeframe, an estimate of zero is just as arbitrary as any other value but certainly wrong. Furthermore, the reasoning in the Explanatory Document that the traded volumes in the intraday timeframe are small compared to SDAC is questionable, particularly given that intraday trading volumes certainly exceed volumes exchanged for balancing.

- **Article 6.6:** *The forecasted market value of CZC for the exchange of energy between bidding zones shall be calculated as the difference in the day-ahead prices of the corresponding hour in the relevant bidding zones of selected reference days in the congested direction. The forecasted market value of CZC for the exchange of energy is 0EUR/MW in the opposite direction of the congested direction.*

Article 6.6 mentions the application of “reference days” for the assessment of the forecasted market value of CZC. It is unclear how those reference days will be selected, especially when market participants will not be part of the consultation prior to the actual application of the methodology.

In addition, we strongly doubt that the reference to “reference days” without further specification is in line with Article 41.1(b) EB GL that explicitly requests a “detailed description on how to determine [...] the forecasted market value of cross-zonal capacity for the exchange of energy”. Referring to the concept of “reference days” and postponing the definition of such elements to the BCC proposals is insufficient.

- **Article 6.7:** *Any application in a balancing capacity cooperation of adjustment factors to the forecasted value of CZC for the exchange of energy between bidding zones shall be included and justified in the methodology for the establishment of common and harmonized rules and processes for the exchange and procurement of balancing capacity according to article 33(1) of the EBGL.*

Article 6.7 mentions the application of “adjustment factors” that shall be included and justified in the “methodology for the establishment of common and harmonised rules and processes for the exchange and procurement of balancing capacity according to article 33.1 EB GL”. To us, the description of adjustment factors belongs to the MZ CZCA methodology and not to the one related to article 33.1 EB GL:

- The adjustment factors are inherent to the CZC allocation mechanism that is chosen rather than to the methodology defining the BCC.
- Moreover, the concept of sharing of reserves is not covered by the article 33.1

We strongly doubt that the reference to “adjustment factors” without further specification is in line with Article 41.1(b) EB GL that explicitly requests a “detailed description on how to determine [...] the forecasted market value of cross-zonal capacity for the exchange of energy”. Referring to the concept of “adjustment factors” and postponing the definition of such elements to the BCC proposals is insufficient.

- **Article 6.8:** *The Hansa TSOs of each balancing capacity cooperation implementing the Hansa MB Methodology shall monitor and report to the Hansa TSOs the efficiency of the forecasting methodology, including a comparison of the forecasted and actual market values of the CZC for the exchange of energy and take appropriate actions, where needed.*

TSOs should publish the forecasted market values on a continuous basis (with as little of a delay as possible) and not only the efficiency of the forecasted market values as currently set out in this paragraph.

- **Article 7.5:** *In the balancing capacity procurement optimisation process, balancing capacity bid selection together with the CZC allocation are optimised to maximize socioeconomic benefit. The balancing capacity procurement optimisation shall minimise the overall costs of procuring the demanded volume of balancing capacity.*

We understand the reasoning for this objective, but changes in the bidding behaviour of market participants compared to what the TSOs have modelled or are expecting should not be underestimated. This will require time to adapt and alignment with TSOs in order to design it.

As we mentioned in earlier points, ignoring the intraday market, in practice, forecloses opportunities for market participants to adjust their positions and will lead to changes in the bidding process.

- **Article 9.2:** *According to article 38(9) of the EBGL, when CZC allocated for the exchange of balancing capacity or sharing of reserves has not been used for the associated exchange of balancing energy of the product it was allocated for, it shall be released to all TSOs for the associated exchange of balancing energy for the same product if possible, and at least it shall be released to all TSOs for the exchange of balancing energy with shorter activation times or for operating the imbalance netting process.*

We welcome the clarification that cross-zonal capacity reserved for a specific product that was not used for this process shall be made available again for the exchange of balancing energy by all TSOs of the CCR in the same process or in processes with shorter timeframes, in accordance with article 38.9 EB GL.

This paragraph is, however, a partial repetition of article 3.2. Please make sure the text of the methodology does not reiterate the same rules multiple times.

- **Article 9.4:** *Hansa TSOs shall not increase the transmission reliability margin calculated pursuant to article 21 of the CACM Regulation due to the exchange of balancing capacity or sharing of reserves for frequency restoration reserves and replacement reserves.*

We welcome this requirement that the application of cross-border capacity reservation should not increase the day-ahead or intraday reliability margins used by the TSOs.

- **Article 11.3:** *The Hansa TSOs applying market-based allocation process in the CCR Hansa shall publish information on the allocation of CZC for the exchange of balancing capacity or sharing of reserves pursuant to article 38 of the EBGL at the latest 24 hours after the allocation and no later than 6 hours before the use of the allocated CZC, pursuant to article 12(3)(h) of the EBGL.*

If the cross-zonal capacity allocation process for the exchange of balancing energy or sharing of reserves is completed at the time of the balancing capacity procurement process in the case of the “market-based” approach, it is unclear why Hansa TSOs would wait to publish information on allocated cross-zonal capacity for the exchange of balancing energy only six hours before its use. For the sake of transparency, this information should be published together with the results of the capacity procurement process, according to the same timing as laid down in article 11.2.

- **Article 11.5:** *Hansa TSOs that will apply the market-based allocation process in the CCR Hansa shall publish the approved methodologies at least one month before its application pursuant to article 12(3)(j) of the EBGL.*

We believe that one month is too short a timing for a proper communication to and preparation of market participants. We believe that a minimum three-month notice to market participants is necessary for appropriate preparation.

- **Article 11.6:** *Only when subject to approval pursuant to article 18 of the EBGL, a Hansa TSO may withhold the publication of information on offered prices and volumes of balancing capacity if justified for reasons of market abuse concerns and if not detrimental to the effective functioning of the electricity markets. A Hansa TSO shall report such withholdings at least once a year to the relevant regulatory authority in accordance with article 37 of Directive 2009/72/EC and pursuant to article 12(4) of the EBGL.*

It shall never be the task of a TSO to decide whether market abuse has been committed, nor to restrict market design or disclosure of price sensitive information on the basis of a fear of such market abuse materialising.