

**ACM consultation on the Hansa TSOs' methodology proposal for a market-based allocation process of cross-zonal capacity for the exchange of balancing capacity****EFET response – 17 February 2020**

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

We have carefully scrutinised the differences between the initial version of the TSOs' text, open to consultation back in September 2019, and the final version submitted to NRAs in December. We have also read the TSOs post-consultation report, including their statements and/or justifications in reaction to our and other stakeholder comments to their initial text. Despite some improvements in the methodology proposal, we remain concerned about quite a number of elements in the final text. You will find more details about this and amendment suggestions below. These rely in large parts on our response to the initial consultation of the TSOs on this methodology<sup>1</sup>.

**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

<sup>1</sup> EFET response to the CORE TSOs consultation on a market-based method for the reservation of cross-zonal capacity for balancing purposes, dated 22 October 2019 and available at: [https://efet.org/Files/Documents/EFET\\_EBGL\\_Art41\\_CCR%20Hansa\\_21102019.pdf](https://efet.org/Files/Documents/EFET_EBGL_Art41_CCR%20Hansa_21102019.pdf).

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 balancing capacity cooperation (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 ACM, along other 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 EB Regulation. 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 EB Regulation), enhancing efficiency of balancing as well as efficiency of European and national balancing markets (Article 3(1)(b) of the EB Regulation), integrating balancing markets and promoting the possibilities for exchanges of balancing services while contributing to operational security (Article 3(1)(c) of the EB Regulation), 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 EB Regulation) 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 EB Regulation).*

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 EB Regulation 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.

- **Article 3.2:** *The Hansa TSOs that want to establish a BCC shall publish on the ENTSO-E website the expected costs and benefits of such a BCC.*

We welcome the improvements included by the CORE TSOs in the final methodology proposal. Indeed, article 3.2 now requires that TSOs that want to establish a BCC not

only to carry out a cost-benefit analysis (CBA) and share it with the other TSOs of the CORE region, but also to publish it on the ENTSO-E website so that it becomes available to all CORE NRAs and market participants.

However, we're still missing a number of other requirements to ensure the proper use of the CBA:

- 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

In addition, 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. While TSOs in the consultation report mention that this is included in other parts of the methodology, we see nowhere an explicit requirement for a regular reassessment of the costs and benefits of an established BCC. This provision is actually included in the CORE TSOs' draft methodology for the "economic efficiency" method of cross-zonal capacity reservation for balancing, at the article 3.8 of that methodology. We would like to see a similar provision (complemented with a precise timing for the regularity of the checks – yearly – and an obligation to disclose these assessments on the ENTSO-E website).

- **Article 4.1:** *Each BCC applying the Hansa MB Methodology shall inform all European TSOs through an announcement on the ENTSO-E website.*

We request that Article 4.1 of this is aligned with the formulation of Article 4.1 of the same methodology applicable in the CORE region:

*"In addition to the notification process as referenced to in Article 1.4 of this MB CZCA methodology, all Core TSOs of each BCC within the CCR Core applying this MB CZCA methodology shall inform the Core TSOs and market participants latest by 4 (four) months ahead of the application of this MB CZCA methodology forecast technique consisting of the use of reference periods and adjustment factors to determine the forecasted market value of CZC for the exchange of energy. Core TSOs may provide remarks not later than 3 (three) months ahead of the application. The BCC TSOs shall take the remarks by the Core TSOs properly into account.*

The new wording of the CORE TSOs methodology for the implementation of Article 41 EB GL clearly states that market participants will be informed four months in advance of the application of the MB CZCA, including the forecast technique, the use of reference periods and adjustment factors. We would add a clear requirement that TSOs will consult stakeholders on the implementation of the MB CZCA for each specific BCC, as stated as an intention of the CORE TSOs in their consultation report.

- **Article 5.2:** *The market-based allocation process to allocate CZC for the exchange of balancing capacity and/or sharing of reserves shall include the following steps [...]*

An additional requirement should be formulated 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 6.2:** *Hansa TSOs and Hansa NRAs of each BCC of the CCR Hansa may commonly apply additional lower limits besides the limitations of Article 41(2) of the EB Regulation for the maximum volume of allocated CZC for the exchange of balancing capacity or sharing of reserves within their own BCC.*

We welcome the clarification by TSOs 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 6.4:** *The maximum volume limitations of allocated CZC for the exchange of balancing capacity and/or sharing of reserves shall be applicable for the combined allocation of all balancing capacity products on a certain bidding zone border per direction.*

We welcome the clarification by TSOs that the 10% limit is applied over CZCA for all of the balancing products, not 10% for each of aFRR, mFRR and RR, possibly summing up to 30%.

- **Article 7.5:** *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, where the CZC is calculated in accordance with the Capacity Calculation Methodology for CCR Hansa, following Article 20(2) of the CACM Regulation (EU) 2015/1222.*

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 7.6:** *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 7.6 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 7.8:** *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 EB Regulation.*

Article 7.8 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 7.9:** *The Hansa TSOs of each balancing capacity cooperation implementing the Hansa MB Methodology shall monitor, demonstrate and publish on the ENTSO-E website the efficiency of the forecasting and the appropriateness of the choice of reference periods, and application of adjustment factors and mark-ups on at least a yearly basis,, including a comparison of the forecasted and actual market values of the CZC for the exchange of energy and take appropriate actions, where needed.*

We welcome the addition of a publication requirement on the ENTSO-E website to ensure transparency towards NRAs and market participants. However, we believe that TSOs should also publish the forecasted market values themselves on a continuous basis (with as little of a delay as possible) and not only an analysis of the efficiency of the forecasted market values as currently set out in this paragraph.

- **Article 8.4:** *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 12.3:** *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 EB Regulation as soon as possible but no later than 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 12.2.

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

We thank the Hansa TSOs for the modification of the timeline for publication of the BCC methodology, from 1 month before application (in the initial version of the text) to three months. This will allow proper preparation of market participants to the new processes.

- **Article 11.6:** *Only when subject to approval pursuant to article 18 of the EB Regulation, 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 EB Regulation.*

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.