

## **TSOs consultation on a methodology to further specify and harmonise imbalance settlement**



### **EFET response – 28 September 2018**

We thank the TSOs for the opportunity to comment on their draft proposal of a methodology for the harmonisation of imbalance settlement, and ENTSO-E for the workshops they organised on 23 March and 20/21 June 2018, as well as the webinar of 19 September 2018 to provide insights into the TSO approach to this methodology.

#### *Raising the ambition in the implementation of Electricity Balancing Guideline*

Generally, EFET remains concerned about the level of ambition of the proposal which we deem far too low in terms of true harmonisation. The presentation made by the TSOs at the Electricity Balancing Stakeholder Group (EBSG) meeting of 3 September 2018 shows that individual TSOs have fundamentally diverging intentions when it comes to the implementation of this methodology. Because the elements and volumes to be considered by each TSO to set the imbalance price are not restricted in this methodology, and because it does not detail how the various element should be combined by individual TSOs, we do not expect a true harmonisation of imbalance settlement either at a regional or pan-European level once the methodology is applied.

#### *Ensuring the consistence and relevance of the imbalance settlement price*

The TSOs' proposal mentions a number of "main components" TSOs can choose from to set the imbalance price in their control area. This list neither explains how the various components could be combined, nor excludes the possibility to include "minor components" in the imbalance price, or for which proportion. This will result in different constructions of the imbalance price for each control area.

This is a fundamental flaw in the methodology: if BSPs are to compete on a level-playing field across borders in the provision of balancing services to TSOs, BRPs should also face the same risks with regard to imbalance settlement. Moreover the imbalance price is the basis for price formation in all market segments (including the

day-ahead and forward markets). Market prices on these market segments reflect an expectation of the imbalance price. Harmonisation of the method for determination of the imbalance price is truly the corner stone of the EB GL, without which not only competition between BSPs on the common balancing platform will be skewed, but also cross-border trade in general will be distorted. Without proper harmonisation of imbalance settlement across control areas, a true single EU power market will not become reality.

*Making sure imbalance settlement price is set according to the right purpose*

The imbalance price needs to correctly reflect the value of energy in real time and the cost of balancing the system to incentivise BRPs to be in balance or help the system restore its balance. However, we strongly object to the possibility of arbitrary incentivising components (including scarcity components) being used in imbalance pricing, especially if they differ from one Member State to the other. Such arbitrary components act as penalties and are likely to create counter-incentives and thus trigger inefficient behaviour by BRPs. For example, BRPs might be incentivised to hold back reserve, or to control their portfolio steering towards a small over-supply.

Such incentive/scarcity components should also not result in a revenue stream for TSOs, their financial neutrality in balancing activities being one of the core principles of imbalance settlement according to the EB GL.

*Beyond the Guideline, avoiding market fragmentation*

Also, though these elements are part of the terms and methodologies to be developed and approved at national level, the proposal under consultation fails to an actual, harmonised methodology for the imbalance settlement, including the treatment of additional elements related to BRPs' balancing responsibility, such as penalties for imbalances (beyond the imbalance settlement price).

Unfortunately, the current proposal actually goes in the direction of more divergence instead of convergence. Technically, it even allows for different processes to be applied in price zones with multiple control areas/TSOs such as Germany. We are very worried that the TSOs' proposal includes the legal possibility for further fragmentation of markets where it should work towards further harmonisation.

Harmonisation should also apply to central dispatching models to the greatest extent possible.

*Ensuring transparency in real-time around system state and imbalance price*

Furthermore, we would have hoped that the new rules, once implemented, would give market participants more transparency concerning to the state of the systems and the formation of the imbalance price compared to the current situation. Making real-time price and system information publicly available would allow market participants to truly respond to or support the system balance – a key goal as highlighted in the explanatory document by the TSOs. Such transparency could be provided by the TSOs individually for their respective control areas, for each grid control cooperation area as well as for every cross border connection.

## Specific comments

### Article 1:

#### **Article 1.2(a): The proposal will not apply to periods for which market activities have been suspended.**

The Network Code dealing with market suspension is the Emergency and Restoration (E&R) Code. A reference to it should be included here. However, as there is no clear rule in the E&R Code concerning the imbalance settlement in cases of market suspension, we believe that this methodology proposal should include principles for imbalance settlement in case of market suspension.

The subject of market suspension (the conditions for market suspension and restart, as well the question of which price(s) applies during the suspension) was discussed in MESC meetings back in 2016 (meetings of May and September 2016). Back then, the MESC advised that rules for imbalance pricing in times of market suspension should be included in this proposal. Settlement of imbalances must continue according to proper market rules also in times of extreme tight systems or periods of scarcity driven load-shedding. Only in case of even more extreme situations, like a system black-out or a system restoration after a black-out, settlement based on market rules may be suspended. In our view, it must be ensured that in case of brown-outs caused by scarcity, the imbalance price is set at least at a level of the assessed VoLL or at a higher level if the last imbalance price already surpassed that VoLL. The latter is important to avoid that the VoLL could act as a de facto price cap. Such considerations are correctly mentioned in the explanatory document (page 13), however they are not reflected in the proposal.

### Article 2:

No comment.

### Article 3:

#### **Article 3.1(b): The imbalance adjustment [will include] all volumes activated by each connecting TSO for that ISP for purposes other than balancing, that are assigned to the concerned BRP.**

The article needs clarification: the current formulation of the article, stating that the imbalance adjustment will include also volumes activated for other purposes than balancing introduces a confusion whether these volumes will be corrected by the TSO or put under the responsibility of the BRP.

We believe that TSO actions affecting the balancing position of BRPs should not result in additional imbalances for which BRPs should be responsible. For example, if a congestion action is requested, the resulting imbalance for a BRP that performs this action should be neutralised by the TSO; in practice this means that the imbalance is 'taken over' by the TSO, who then has to correct it by a counter-balancing action.

**Article 3.4: The applied imbalance adjustment shall be reported by the TSO to the concerned BRP without delay and shall be finalised not later than set by national terms and conditions.**

The reporting of the imbalance adjustment to the concerned BRP should be subject to a clear and harmonised deadline and not be left for determination by national terms and conditions. This deadline should be based on existing best (i.e. fastest) practice among the TSOs for imbalance adjustment reporting, at the very least as a target with a precise timeline for TSOs to align on the harmonised deadline. Continuing to apply varying timeframes across different market areas requires market participants to maintain different operational processes and hinders new market entries.

Furthermore, TSOs should jointly tackle the harmonisation of the final imbalance calculations. Receiving such updates a quarter or a half-year following the concerning ISP is a financial liability and operational burden placed on the BRPs.

#### Article 4:

**Article 4.1: BRPs shall have one single final position equal to the sum of its external and internal commercial trade schedules.**

EFET strongly supports the common use of a single position for BRPs. This is an important harmonisation step towards a level-playing field.

**Article 4.1(b): TSOs currently applying the calculation of two positions per BRP shall change to apply the calculation of single position per BRP not later than the implementation of [the 15-minute ISP].**

To our understanding, this paragraph seems to make a link between the implementation of the 15-minute ISP and the calculation of one position per BRP. However, no such link is mentioned in the EBGL. The implementation of a single position should coincide with the implementation timing of the ISH proposal. Should individual TSO consider this unfeasible, individual derogations could be requested.

**Article 4.2: The imbalance for each BRP over each ISP shall be calculated for each imbalance area by the connecting TSO.**

This paragraph, combined with the definition of “imbalance area” in Article 2(11) EBGL, is tautological: the methodology says that the calculation of a single BRP position happens per imbalance area, while Article 2(11) EBGL says that ‘imbalance area’ means the area in which an imbalance is calculated.

The methodology hence lacks a clear designation of the geographical level at which the imbalance calculation happens. The relevant area for BRPs is the bidding zone, since this is the area considered by BRPs in the previous market timeframes. The methodology should make clear that a single position **per bidding zone** (not per control area for instance), needs to be calculated for each BRP.

**Article 4.3: The calculated imbalance over each ISP for each imbalance area shall be reported by the TSO to the concerned BRP without delay and shall be finalised not later than set by national terms and conditions. (And articles 4.4 and 4.5).**

Once again, the proposal provides a fallback mechanism to the deadlines set by national terms and conditions regarding the timeframe by when each BRP is informed about the calculated imbalance per ISP for each imbalance area (Article 4.4) and the net allocated volume (Article 4.5). These timelines should be harmonised by the TSOs.

Article 5:

#### **General comment on Article 5.1:**

Article 5 should be the cornerstone of the ISH methodology proposal. If BSPs are to compete on a level-playing field across borders in the provision of balancing services to TSOs, BRPs should also face the same risks with regard to imbalance settlement. Moreover the imbalance price is the basis for price formation in all market segments (including the day-ahead and forward markets). The market prices on these market segments reflect an expectation of the imbalance price.

The harmonisation at European level of the principles and method for determination of the imbalance price is truly at the core of the EB GL objectives. Indeed:

- Recital (5) EBGL: This Regulation establishes **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.
- Article 1.1 EBGL: This Regulation lays down a detailed guideline on electricity balancing including the establishment of **common principles for the procurement and the settlement** of frequency containment reserves, frequency restoration reserves and replacement reserves [...].
- Article 44.1(d) and (g) EBGL: The settlement processes shall [...] **facilitate harmonisation of imbalance settlement mechanisms [and] support competition among market participants.**

Without the harmonisation of these principles and method for imbalance settlement, competition between BSPs on the common balancing platform will be skewed, but also cross-border trade in general will be distorted. Without proper harmonisation of imbalance settlement process across control areas, a truly single EU power market cannot be obtained.

Article 52(2) EBGL gives room to come up with a far more ambitious proposal than what the TSOs present us today. Indeed, the TSOs are expected to “further specify and harmonise **at least**” a number of elements listed in the article. Instead, the current proposal consists in a list of elements, not much further specified than in the EB GL, and clearly no methodology.

The TSOs should harmonise the imbalance price methodology across Europe. In the uncongested case, whether the marginal bid for determining the balancing energy price is set by a local or a foreign BSP shouldn't matter (as the overall welfare is increased), the imbalance price should be based on this cross-zonal price. An additional benefit of applying a harmonised imbalance price methodology is that it takes away the complexity related to the volume determination (whether this should be based on requested or activated TSO volumes), as the volume that is used for the price calculation is equal to the activated volume in the entire region that is considered.

**Article 5.1: Each TSO may use one or more of the following prices as main component for calculating the imbalance price [...]**

### **Main vs. minor components**

While the formulation of the article appears at first to restrict the elements which the TSOs can use for the calculation of the imbalance price (with the formulation "may use only"), article 5.1 refers to the "main components", which effectively leaves ample room to TSOs to include other components in the calculation. It was confirmed during the workshop organised at ENTSO-E on 20/21 June that despite the confusing wording of the methodology, the list of components of article 5.1 should not be considered exhaustive.

We do not see, beyond the elements listed as "main components" in Article 5.1, which other elements could reflect "the real time value of energy", as requested in the principles for imbalance settlement of Art. 44.1(b) EB GL. Should the TSOs have specific elements in mind that contribute to making the imbalance price reflect the real time value of energy, then these should be further clarified and included in Article 5. Without clarification of potential additional elements, and a justification that they fit with the principles of Article 44 EB GL, we see no reason for the methodology to leave an open door to the inclusion of further elements in the imbalance price.

Should the ISH proposal maintain the possibility to include other elements than those listed in Article 5.1, then a solution to what constitutes a main or a minor component would need to be found, as there is currently no explicit threshold on what constitutes a main or minor component. This leaves the door wide open to individual TSOs interpreting how much 'minor' components can weigh in the imbalance price calculation. Lacking an explicit methodology – as mentioned in the previous comments – at least an explicit delineation should be made. This could be, e.g., set at 10% of the overall imbalance costs on a monthly basis.

### **Combination of main components**

The methodology does not provide details on how to combine the elements listed in Art. 5.1, which will lead TSOs to apply vastly different approaches to set the imbalance price at national level. The objective should be to achieve similar price dynamics for similar imbalances all over Europe.

Bearing in mind our comments on point (d) – which we propose to delete, see below – if the ISH proposal intends to put forward a methodology rather than only a list of components, it needs to specify how the elements of points (a), (b) and (c) will be



combined. We propose to combine them based on the MWh volumes considered in each of the processes (avoided activation, balancing energy activation and intended exchanges).

**Article 5.1(b/c): Requested vs. activated volumes**

The FRR component is based on requested volumes, while the RR component is based on activated volumes. This difference is neither explained nor clear. As the volumes used for the calculation – mentioned in paragraph 3 – are all based on requested volumes, this deviation for RR should be either clearly explained or brought in line with the requirement for FRR.

**Article 5.1(d): In case a TSO identifies the need for stronger incentives in scarcity situations, the TSO may propose to its relevant regulatory authority to apply a scarcity or an incentive component in imbalance pricing.**

EFET strongly objects to the inclusion of Article 5.1(d). Art. 44.1(b) EBGL states that the imbalance settlement price should reflect the “real time value of energy”. The real time value of energy naturally takes account of the risk of scarcity. Therefore, if properly set according to the EB GL principles, the imbalance settlement price mechanism should de facto provide an adequate price in situations of scarcity. As a result, Art. 5.2 is either redundant, or would serve as a deterrent to setting the imbalance settlement price properly.

In addition, if implemented in a non-coordinated way, such additional components would lead to different imbalance price behaviour with similar imbalance volumes in the different control areas. Their use should be harmonised through the definition of an imbalance price methodology, instead of listing the major components as currently proposed.

Only in case of a scarcity caused brown-out (load shedding), the value of that intervention must be reflected in the imbalance price. For that reason, it must be checked whether for these periods the imbalance price would remain below (an assessment of) the VoLL and in such case the imbalance price must be increased to the VoLL.

**Article 5.3: Each TSO may only use the following volumes for calculating the imbalance price [...]**

The methodology does not provide details on how to combine the different elements listed in Art. 5.2, which could lead TSOs to apply vastly different approaches in terms of the volumes considered to set the imbalance price at national level.

Once again, this important leeway given to TSOs is a fundamental flaw in the methodology: if BSPs are to compete on a level-playing field across borders in the provision of balancing services to TSOs, BRPs should also face the same risks with regard to imbalance settlement. This is truly the corner stone of the EB GL, without which competition between BSPs on the common balancing platform will be discriminatory.

Article 6:

**Article 6.1: Each TSO shall calculate the value of avoided activation from frequency restoration reserves or replacement reserves for each ISP during which there has been no activation of balancing energy in either direction for the imbalance price area.**

The article stipulates that TSOs shall calculate the value of avoided activation, but it does not lay down in sufficient detail how it should be calculated.

Furthermore, the application of the value of avoided activation and the delineation from the price for the intended exchange for imbalance netting remains unclear. Applying imbalance netting is actually just doing this – avoiding the activation (or actually the request) of balancing energy bids. The corresponding value is then always relevant for the calculation of the imbalance price, in order to correctly reflect the real-time value of energy; not just in situations without additional activation of balancing energy.

**Article 6.3(a): the connecting TSO will calculate the value of avoided activation**

It is not clear why a connecting TSO needs the value of avoided activation for the calculation of the imbalance price. The imbalance price should be based on the requested volumes of balancing energy, and thus only relevant for the requesting TSO.

When calculating the value of avoided activation according to merit order information it is important to consider the activated balancing energy bids. The value of avoided activation is then determined from the subsequent bids that were not activated. In the same way, the value of avoided activation will also become relevant for balancing energy pricing. The activated balancing energy bids should be remunerated according to the marginal price of the last required bid, regardless of the bid having been activated or avoided.

Article 7:

**Article 7.1: Each TSO shall implement the use of single imbalance pricing for all imbalances not later than application of the ISP of 15 minutes.**

The link between the single imbalance price and the harmonisation of the 15-minute ISP is not made in the EBGL. Therefore, such an explicit link and general derogation of the requirement to implement the single imbalance price should not be proposed by this ISH proposal. The implementation of the single imbalance price should be at the time of the implementation of this ISH proposal – i.e. 18 months after its approval by NRAs. If TSOs see valid reasons that such implementation is not feasible, an individual derogation should be requested to the national NRA with a possibility for market participants to comment on this request via a public consultation.



Article 8:

**General comment on Article 8:**

Article 52.2(d) EB GL foresees that **all TSOs** shall establish “the definition of conditions and **methodology** for applying dual imbalance pricing”. Art. 8 of the ISH proposal instead establishes the conditions under which TSOs may apply dual pricing, and leaves the responsibility of establishing the methodology to apply dual pricing to each of these individual TSOs. This is not in line with either the letter or spirit of Art. 52 EB GL.

**Article 8(1)(b): Each TSO may propose to its relevant regulatory authority the application and methodology of dual pricing for a given imbalance area for any ISP in which [...] the TSO requests activation of both positive and negative balancing energy from frequency restoration reserves or replacement reserves for that given ISP.**

It is unclear whether in this case the dual pricing is only allowed during ISPs with up- and downward activations, or in general. In the latter case, it would allow a general application of dual pricing by all TSOs as every TSO at some point is confronted with activations in both directions during one ISP. The application of dual pricing in case of activations in both directions during one ISP should therefore be more circumscribed and only allowed if the use of a single imbalance price leads to demonstrable problematic issues.

For calculating the imbalance price for an ISP with TSO requests for positive and negative balancing energy, Article 55.6 EB GL foresees that “in the event that both positive and negative balancing energy from frequency reserves or replacement reserves have been activated during the same imbalance settlement period, the imbalance settlement price shall be determined for positive imbalance and negative imbalance based on at least one of the principles pursuant to paragraphs 4 and 5”, i.e. the imbalance price for either the positive or the negative imbalance. We believe that the methodology should clearly state that the price of the predominant balancing direction should be used to set the imbalance price.

The condition of counter-activated positive and negative balancing energy during one ISP in Article 8.1(b) is the common situation in some countries (e.g. Germany, Austria) for most of the time. Hence, dual pricing would permanently be applied, which is not acceptable. We therefore suggest removing Article 8.1(b). And with the same reasoning Article 8.1 (d)(iii) with very similar content should be removed.

**Article 8.1(c): Each TSO may propose to its relevant regulatory authority the application and methodology of dual pricing for a given imbalance area for any ISP in which [...] the net sum of all imbalances in an imbalance area and where applicable, HV-DC that are not attributable to any BRP does not indicate a clear direction for that given ISP and therefore does not justify to set an incentive to one certain direction for that given ISP. The threshold for what is considered a clear indication of the direction shall be proposed by TSO and approved by the NRA in the national terms and conditions for BRPs.**

The lack of a clear imbalance direction should not be a reason to apply dual pricing. BRPs should not be punished by artificially strong imbalance prices because the netted imbalance volume is small. If there is no clear imbalance direction, there is no high imbalance need for the TSO and no associated high imbalance energy procurement cost for the TSO. The imbalance price should simply reflect this for all BRPs.

**Article 8.1(d): Each TSO may propose to its relevant regulatory authority the application and methodology of dual pricing for a given imbalance area for any ISP [if] the specificities of the local electricity market or imbalance price area (such as in a small- scale market size, with a low number of BRPs causing the majority of the imbalances) require dual pricing in order to provide proper incentives to BRPs to be in balance.**

The cases listed in article 8.1(d) should be exhaustive. Art. 52.2(d)(i) EB GL requires that all TSOs specify and harmonise the conditions to deviate from the single pricing rule and apply dual pricing. A series of examples cannot be considered specific and harmonised conditions.

Besides, Art. 52.2(d)(ii) EB GL requires all TSOs to develop a methodology for applying dual pricing. The methodology under consultation only comprises elements related to the conditions relating to deviating from the single pricing rule, not for the application of dual pricing.

The EBGL Article 52(2)(d)(i) states that the conditions may be proposed by a TSO to its relevant regulatory authority. The proposal is therefore only applicable to the imbalance pricing if the TSO chooses to do so and after a regulatory authority approval. The national NRA should avoid any attempt to reform or influence the national TSO.

Moreover it is questionable whether the example given (a small market with a low number of BRPs) is justified as a reason to propose dual pricing. Also in such a market the imbalance price must reflect the value of electricity correctly, which by definition should be one, single price. Applying dual pricing, thus theoretically creates a market inefficiency. Such inefficiencies need sound justification and to be disclosed not only to the relevant NRA but also to market participants.

Applying single pricing is preferred, because if you help the system you should get the credits for this. Whether dual pricing to avoid balancing energy oscillations as described in the explanatory documents, should be investigated first, and be weighed against the opportunity losses by BRPs. It should be noted that situations where a

single price can turn into a dual price, based in a TSO activation in the last minute of an ISP, poses a serious financial risk to a BRP, an argument which is not mentioned nor discussed in this context.

**Article 8.1(e): Each TSO may propose to its relevant regulatory authority the application and methodology of dual pricing for a given imbalance area for any ISP in which [...] the costs of balancing energy used to balance the system (excluding the balancing capacity) are entirely to be covered by the BRPs which cause the imbalances the single pricing method may not provide enough resources or may results in a deficit.**

This provision should be removed. The overriding objective must be to set the imbalance price at the value of electricity and to implement single pricing, so that the correctly set imbalance price can correctly do its work in steering the market. Cost recovery is a secondary objective and should not override the main principles.

**Article 8.2: In case of application of dual pricing for a given ISP and a given imbalance area pursuant condition (b) or (c), the TSO shall calculate an imbalance price in one direction according to its methodology for calculating a single imbalance price for that ISP and that imbalance area; its methodology to calculate the imbalance price for the other direction shall not use any main components other than in accordance with this proposal Article 5.**

The calculation methodology for both directions should be the same. It is therefore not clear why there are different explanations for the calculation methodology for the dominant direction and for the other direction. Both should adhere to the general requirements of the imbalance price calculation.

Article 9:

**Article 9.2: Each TSOs shall implement the Articles of the imbalance settlement harmonisation proposal, relevant to their dispatching model, self-dispatching or central dispatching, in accordance with Article 52(4) of the EBGL, no later than eighteen months after approval by all relevant regulatory authorities.**

Reference is made to Art. 52(4) EBGL, requiring the implementation of the ISH proposal 18 months after approval by NRAs. However, key elements such as the single imbalance position and single imbalance price calculations are pushed back to the harmonization of the ISP towards 15 minutes. The EBGL makes no such link, and it could even be considered against the spirit of the EBGL. If derogations for the implementation of certain elements of the ISH are required for well-founded reasons, this should be possible. However, the ISH should not allow for blanket exemptions but rather take the ISH implementation deadline as the default implementation requirement for all elements it contains.

Article 10:

No comment.