

EFET response to European Commission Consultation to establish the priority list of network codes



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The European Federation of Energy Traders (EFET)¹ would like to thank the European Commission for the opportunity to comment on the priorities for the development of network codes and guidelines for the period 2020-2023 and beyond.

Priorities for electricity

With respect to electricity, we shall focus on the proposal for a Network Code on Demand-Side Flexibility. We acknowledge that the importance of demand-side flexibility, but also of flexible capacity more generally (e.g. storage, generation), will increase with the growth of intermittent renewable energy sources. Growing electrification (e.g. e-mobility) will also put new demands on the grid, with flexible capacity playing an important role in addressing local congestions.

We fully support the involvement of new market participants such as active consumers and independent aggregators in the wholesale electricity market. In our view, the EU internal energy market legislation, particularly with the completion of the Clean Energy Package, provides a comprehensive framework, laying down the key principles for their successful development and effective market engagement. The framework requires non-discriminatory access, level playing field and transparency for all market participants in all market segments, and the development of effective price signals, which is essential for building a robust business case and developing new business models and services.

We are conscious that demand-side flexibility still has a significant untapped potential. We see two main reasons for this. First, the market is not valuing energy at a level that would incentivise demand response. Indeed, current prices of electricity at the

¹ The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open transparent, sustainable and liquid wholesale markets, unhindered by national borders or other undue obstacles. We currently represent more than 100 energy trading companies, active in over 28 European countries. For more information, visit our website at www.efet.org

wholesale level do not correspond to the level at which all types of demand-side response would make economic sense for the moment. Further, the continuation of regulated prices at retail level also impedes the reactivity of domestic customers to energy prices. Second, a number of regulatory barriers exist in EU Member States, stemming mainly from national regulations in fields of national competence, or being the result of incorrect implementation of the EU target model.

At this stage, however, we do not see a need for a dedicated Network Code on Demand-Side Flexibility, as we have not identified significant gaps in the EU framework that would necessitate the development of such an instrument. A code dedicated to demand-side flexibility, alongside the Market Guidelines applicable to all market participants, may impact the level-playing field with other providers of flexible capacity, which would reduce efficiency and increase costs for consumers. It may also lead to overlaps with existing rules, which would run against the Commission's objectives to simplify and streamline regulation.

Instead, we would recommend assessing carefully whether existing barriers to the development of flexible capacity are due to inefficient implementation of existing regulations, or specific national-level rules present in some jurisdictions. Where some elements of the existing EU legislative framework are not tailored to allow demand-side flexibility to develop to its full potential, these rules should be amended to ensure non-discrimination.

The proposal of the European Commission states that a new Demand-Side Flexibility Network Code would aim to:

- Create a transparent and non-discriminatory flexibility market where the distribution and transmission system operators can procure flexibility products to solve congestion in their grid; and
- Facilitate market access and operation of new market players, such as active consumers and independent aggregators, thanks to transparency and harmonisation of the pre-qualification rules and standardisation of flexibility products.

We analyse both of these objectives in turn.

- **Procurement of congestion management services**

The EU energy market framework covers all market segments (forward, day-ahead, intraday and balancing markets), and providers of flexible capacity (be it from demand-side response, storage, or generation) should be able to engage in any timeframe. This means that market participants, irrespective of technology, should be free to maximise revenues by choosing where to offer their capacity and any barriers to this end on a national level need to be removed.

Furthermore, Art. 13 of the Electricity Regulation (Regulation (EU) 2019/943) maintains that congestion management services shall also be open to all generation technologies and all energy storage and demand response, and shall be procured in a market-based manner. This lays down a framework for a transparent and non-discriminatory market for congestion management services (or a 'flexibility market,'

see footnote 2). Capacity is valued at the market and flexibility, as a defining property of capacity,² is also rewarded accordingly and priced through existing or newly developed energy products.

One aspect, however, would need to be clarified going forward. As congestion management is becoming increasingly important, especially at the level of distribution system operators, it would be particularly important to understand if and how market participants would be allowed to choose between offering in the energy market or for congestion management. Until now, we had seen congestion management as a complement to the energy market, not an alternative market. The recast Electricity Regulation sketches a different future, but significant differences of views exist at national level on the implementation of the new model for market-based congestion management. Clarification in the Electricity Regulation as to the precise target model for congestion management would be required. If European authorities target a real market for congestion management, this new approach would have to be compatible with the spirit of convergence of wholesale markets of the past 15 years in Europe, where the same resources can participate in different market segments while complying with wholesale market integrity rules (i.e. REMIT).

A level-playing field between those connected at the distribution level and those connected at the transmission level would also need to be ensured.

- **Facilitating access to the energy market for new participants**

Facilitating the participation of new market participants, in particular those able to offer flexible capacity, is essential for achieving our decarbonisation objectives in a cost-efficient manner. In fact, there are markets where we can already see some growth in demand-side flexibility participation, for instance (e.g. France, Great Britain, Ireland, Germany, Finland, Belgium and the Netherlands).³

The main reason for their limited participation in the market so far is that the business case is still not very strong: current prices of electricity at the wholesale level do not correspond to the level at which all types of demand-side response make economic sense for the moment. However, this is likely to evolve in view of the changing system needs and a growing demand for a more fair, competitive environment.

A number of regulatory barriers also create challenges for both new and existing market participants. In particular, ancillary services remain an important value stream for demand-side flexibility providers, with the situation differing among jurisdictions. Pre-qualification requirements for the participation of demand-side flexibility in markets or products should ensure that balanced quality standards and requirements are put in place, to be followed by all market participants without any undue limitation or discrimination. Minimum bid size requirements in some platforms restricting the

² Flexibility is a property of the capacity, not a separate product, and it is misleading to speak of separate 'flexibility markets.' With respect to the first stated objective of a potential Demand-Side Flexibility Network Code in the consultation document, we understand the creation of a 'transparent and non-discriminatory flexibility market' to mean a market where TSOs and DSOs can procure congestion management services.

³ SmartEn's EU Market Monitor for Demand Side Flexibility, https://smarten.eu/wp-content/uploads/2020/03/EU_Market_Monitor_2019_1-23_1page.pdf

participation of smaller demand-side flexibility providers shall be accompanied by transparent and equal rules governing the pooling of all kind of resources. These are issues that require attention on a national level and need to be aligned with the non-discrimination principles embedded in EU legislation.

Regarding product standardisation, flexible capacity is priced through existing energy products and there is reasonable transparency around the pricing of these products. At the wholesale level, market participants are free to shape their products on the OTC market. Should the standardised products in Single Day-Ahead Coupling (SDAC), Single Intraday Coupling (SIDC) or on the common balancing energy activation platforms be a hurdle to the participation of demand-response to the market, then the debate about reviewing these products (shape, size, etc.) should be carried out in the context of the Guideline on Capacity Allocation and Congestion Management (CACM, Regulation (EU) 1222/2015) and the Electricity Balancing Guideline (EBGL, Regulation (EU) 2017/2195) and their implementation projects. A comprehensive assessment of the need for some standardisation may be in order to alleviate concerns around potential market fragmentation and products tailored to certain types of capacity.

In our understanding, a number of challenges to the growth of demand-side response stem from national level requirements, particularly related to the structure and functioning of the retail market. Independent aggregators could energise markets and increase the value for customers by discovering new ways of delivering flexibility, but the contractual relation between suppliers and customers and the ability of independent aggregators to engage with customers must be properly defined to set out a robust and fair regulatory framework (e.g. detailed rules governing balancing responsibility). Unlocking opportunities for new business models to develop is related to ensuring freedom of contractual relations,⁴ non-discriminatory data access for service providers and the availability of appropriate infrastructure (i.e. smart meters roll-out). The removal of price caps, availability of dynamic pricing (by restricting regulated tariffs solely to cases of energy poverty) and cost-reflective network charges are also essential for the development of effective price signals (both for consumers and new market participants), which could support viable new business cases.

We would urge for the removal of national level requirements that constitute barriers to innovation, but would see this as a matter for national level reform aiming to deliver a transparent and competitive environment where new business models and services can flourish.

Priorities for gas

On the priorities regarding gas network rules, we believe that accomplishing the desired level of harmonisation may require some additional reinforcements to existing network codes and guidelines. We believe that it would be particularly important for an internal market for gas to revise the Network Code on Harmonised Transmission Tariff

⁴ Here it is important to stress that standardisation of retail supply contracts should be avoided as it risks stifling innovation.

Structures for Gas (NC TAR, Regulation (EU) 2017/460), so that it can address some of the major challenges that the gas sector is or will be facing in the coming years. These include:

- Reduced gas throughput and capacity bookings, otherwise leading to constant tariff increases and potential asset stranding.
- Tariffs applicable to renewable, decarbonised and low-carbon gases injection into the gas networks and the potential issue of cross-subsidisation.
- Applicability of the tariff methodologies to dedicated hydrogen networks and or blended gas networks.
- Inclusion of guidelines for the implementation of hub mergers in the wholesale gas markets. Clear criteria and standards procedures (consultations, investment and welfare analysis, congestion management mechanisms) should be provided to ensure the design of market mergers will increase efficiency and cross-border trading. European regulators and transmission system operators (TSOs) should also conduct joint analysis on cross-border impacts of merging hubs in their respective jurisdictions.
- The recent experience of the implementation of NC TAR has shown the need for the introduction of clear provisions seeking to prevent cross-subsidies between domestic and cross-border consumers. The inclusion of cross-border impact assessments in tariff setting involving relevant National Regulatory Authorities (NRAs) and TSOs is crucial to avoid any potential cross-subsidy between network users.
- Implementation of guidelines for the provision of flexibility services in the gas market. For example, the introduction of common rules/guidelines for market-based mechanisms to solve short-term congestions. Common rules across EU jurisdictions would facilitate the harmonisation of these services and the participation of cross-border flexibility providers in national schemes.

We also take this opportunity to signal the disappointingly low impact of the ACER opinions on national tariff-setting methodologies. We note that the extensive work of the Agency often identifies a number of major flaws, especially in connection with cost orientation of applied reference price methodologies (RPMs) in different national tariffs, yet it is rarely taken into account by the relevant authorities. EFET believes that it would be prudent to oblige NRAs and/or TSOs to react to ACER's opinions and provide additional clarity on the issues of potential non-compliance. An extended and reinforced mandate of ACER would benefit the harmonisation process of the regulatory frameworks for gas across Europe.

EFET would like to highlight that EU legislation also needs to provide more clarity on the applicability of the Network Codes to hydrogen and blended gas transmission networks in general. This also applies to the mandate of recognised authorities in the field of renewable and low-carbon gases. More clarity in this respect would help to ensure that the interoperability of different parts of the European gas system remains intact. A harmonised approach at the early stages will also be crucial for the cost-effectiveness of the future development of both gas and electricity networks, particularly in view of the envisaged sector integration.