

NEMOs consultation on the Harmonised minimum and maximum price limits for single day-ahead and intraday coupling



EFET response – 2 December 2016

The European Federation of Energy Traders (EFET) is committed to improving the integration of European wholesale energy markets and took an active part in contributing to the drafting and improvement of the CACM Regulation until its adoption. We welcome the consultation of the NEMOs on the adoption of specific methodologies for single day-ahead and intraday coupling. We will focus our comments below on the part on the harmonised minimum and maximum price limits proposal according to Art. 41 and 54 of the CACM Regulation.

1. Do you find that the proposal addresses all the relevant objectives and issues that it should?

As a general note, we believe that the proposal of the NEMOs lacks ambition. The proposal presented by the NEMOs features at best the status quo, but could also mean a step back if, e.g., min/max intraday price limits would be aligned on the day-ahead price limits. In any case, the proposal falls short of the objective set in the CACM Regulation, i.e. that **harmonised price limits should take account of the value of lost load (VoLL)**.

We remind the NEMOs of the importance of free formation of prices in the wholesale electricity market¹. One of the basic elements to ensure this is to **avoid that regulatory or technical caps limit market participants' bidding behaviour directly or indirectly**, which can have negative effects on the market similar to that of administrative interventions (e.g., the adequacy patch in the flow based market coupling algorithm).

¹ EFET Discussion Paper on the free formation of prices in the European wholesale electricity market, June 2016, available at:

http://www.efet.org/Cms_Data/Contents/EFET/Folders/Documents/EnergyMarkets/ElectPosPapers/~contents/GH299HP5MPZQ5T5/EFET_Free-formation-of-prices-power-market.pdf.

At the very least, we would have expected a clear roadmap for min/max prices in day-ahead and intraday to reflect the VoLL. There is also no clear explanation in the consultation document why the NEMOs wish to keep min/max prices at the current level, or even lower that level in the case of intraday. Even if it is not publicly stated in the consultation document, we suspect that the question of the cost of collateral in case of higher min/max prices was one of the reasons that led the NEMOs to present this unambitious proposal. **The proposal should provide a view on the estimated impact on the cost of the collateral in case of higher price caps**, including the consideration that with higher price caps, market participants themselves may take actions to shield themselves from higher potential spikes (e.g. less must-buy or must-sell bids). From a market participant standpoint, we do not expect such hurdles in terms of cost of trading that would, for instance, limit market entry for smaller market participants, if min/max price limits were raised, possibly gradually, towards the VoLL.

Further, **the permanent exemption clause of section 6.1 seriously undermines the very purpose of the methodology proposal**, by granting an indefinite derogation that is in no way foreseen in the CACM Regulation. Indefinite derogations should not be allowed; we therefore consider that NEMOs should clarify how and by whom the derogation period will be set, and how the sunset clause for derogations will work out.

2. In the proposal being consulted upon two different levels are indicated as possible price limits to apply in the Single Intra Day Coupling (SIDC), one like proposed for Single Day Ahead Coupling (SDAC) and one with a wider range. The reason being that SIDC, contrary to SDAC (Implicit Auction), is based on continuous trading and matching of individual orders based on a continually, for each Bidding Zone, visible best bid/ask spread and accordingly there is no clear relevance for limits other than on technical grounds. On that basis we have these specific questions linked to the price limits to be applied:

- Do you have any opinion about if the price limits set for Single Day Ahead Coupling (SDAC) and Single Intra Day Coupling (SIDC) should be identical or different?*

Having identical price limits for both day-ahead and intraday is all the more questionable the lower the limits are. The closer to delivery, the higher the cap should be in order to ensure that the market appropriately reflect the expectation of the cost of imbalances – which itself should be left to reflect up to the VoLL.

If the min/max price limits in both day-ahead and intraday reflect the VoLL, then they can of course be identical.

- *Do you have any opinions about the limits proposed for SDAC? If you disagree with the proposed limits what would you deem as more appropriate limits and can you elaborate on why?*

As mentioned in our answer to Q1, Art. 41 of the CACM Regulation foresees that the proposal for min/max price limits on day-ahead should take account of the estimated value of lost load. This is not the case in the current proposal, which only enacts the current practice.

At the same time it is evident that **a price cap of 3,000 EUR/MWh for SADC is too low**. Indeed,

- This value has already been reached in a few instances in the past and thus has already suppressed day-ahead market prices.
- Secondly, it is safe to assume that current overcapacity will be reduced following the closing and/or mothballing of some of the existing capacity. Thus, scarcity will be more likely to appear, for example in evening hours (no PV), with low wind and high demand.
- Finally, it is important to note that the SADC price cap not only suppresses market prices when the day-ahead price actually reaches this cap. They also continuously suppress prices on the forward markets, because forward prices reflect expected spot prices. Any potential capping of spot prices thus suppresses forward prices.

It is difficult for EFET to make a concrete proposal on the SADC price cap. If it is assumed that real-time or imbalance prices cannot be higher than, for example, 20,000 EUR/MWh, then it is clear that a cap higher than 20,000 EUR/MWh is pointless. A high cap of 20,000 EUR/MWh could however have drawbacks if collateral requirements would increase in a linear fashion with the price cap. Such consequences and possible alternative solutions are not described in the consultation document.

Hence, and pending further analysis on the impact of amended price limits on the required collateral, we believe that **a price cap for SADC somewhere between 5,000 and 15,000 EUR/MWh could be balanced proposal**. **A price floor of -3,000 EUR/MWh for SADC seems low enough** and should not restrict free formation of prices.

- *Do you have any opinion about either of the options (A: +3000/-500; B:+9999/-9999) proposed as limits for SIDC? If you disagree with both sets of proposed limits what would you deem as more appropriate limits and can you elaborate on why?*

First, **we would like to question the application of a price cap to continuous intraday trading**. While we understand the technical need for a price cap in SDAC, we fail to see how this is technically required for the future XBID-based SIDC which is not auction-based.

This first reflection aside, we do not see the rationale for aligning the min/max price limits for intraday on those of the day-ahead timeframe. This would be a step backwards compared to the current caps and floors. At the same time, **EFET sees no reason not to apply a price limit higher than 9,999 EUR/MWh for SIDC.**

Price formation in the power market (including the day-ahead and intraday timeframes) is based on expected real-time prices (or imbalance prices). In case of actual physical scarcity (with involuntary load shedding), the imbalance price will have to be set at a value that reflects the VoLL. Unfortunately, it is still unclear what values will actually be used. Therefore the NEMOs are now forced to apply a best guess on these values. At the same time, there are studies on this issue available. In particular, EFET wants to refer to a recent UK study (“The Value of Lost Load (VoLL) for Electricity in Great Britain”, July 2013) where Ofgem and DECC indicated a peak winter workday VoLL of 10,289 GBP/MWh for domestic users and 35,488 GBP/MWh for SME users based on willingness-to-accept. Ofgem and DECC calculated a weighted-average VoLL figure of 16,940 GBP/MWh (about 21,700 EUR/MWh) for peak winter workdays in GB.

Based on this study EFET suggests that NEMOs use the value of 20,000 Euro/MWh and would set **the price limit for SIDC at 20,000 EUR/MWh, if any. A price floor of -9,999 EUR/MWh for SIDC seems low enough** and should not restrict the free formation of prices.

3. Do you have any suggestions on how to over time tackle the required need to consider the limits in relation to Value of Lost Load (VOLL)?

- *Further, do you have a suggestion on how to in relation to price limits tackle the fact that there is no uniform VOLL across the EU?*

We call for pragmatism in the definition of the VoLL. Today, we have no experience on what the exact value of the VoLL but we could take a proxy. The limit should be high enough to allow all market participants to express their willingness to buy/sell and hence allow a free formation of prices.

Would new studies be made available in the future and new VoLL values be applied for imbalance price setting, we expect the NEMOs to re-assess the price limits accordingly.

4. While the Proposal clearly says that harmonised limits shall apply for SDAC and SIDC respectively it also allows for derogations based on two options, namely (a) an agreement between relevant NEMOs and TSOs and approval by NRAs (Article 6.1), or (b) temporary derogations decided upon by the All NEMO Committee (Article 6.3), and for both options it may be valid in single Member States, Bidding Zones and regions or the whole SIDC or SDAC geographic scope if due consideration is made of the impact on the objectives of the regulation.

- What is your view on the derogation option in Article 6.1?

Art. 41 and 54 of the CACM Regulation do not foresee the possibility of an exemption. This fundamentally defeats the purpose of these articles, especially if the derogation may be granted indefinitely.

If an exemption is to be tolerated temporarily within any particular bidding zone then at a minimum it should be subject to:

- Justification on grounds of non-practicability rather than convenience or preference
- Sign-off by NRAs responsible for surrounding bidding zones
- Imposition of a sunset clause

- What is your view on the temporary derogation option in Article 6.3?

This temporary exemption is not also not foreseen in Art. 41 and 54 of the CACM Regulation. However, **because of its temporary nature, the provision could be acceptable until the price limits for both day-ahead and intraday correctly take account of the VoLL.**

In any case, the wording of section 6.3 should at least be amended as follows: '*In exceptional circumstances, where in the judgement of the NEMO Committee there is a **significant** risk that the Harmonised Maximum and Minimum Clearing Price Limits will be **repeatedly** reached, the NEMO Committee may decide for a temporary period of time to apply Temporary Maximum and Minimum Clearing Price Limits.*'

Further clarity would be welcome in the rules concerning the threshold as of which a risk that the harmonised price limit could be reached is formalised (e.g. when prices reach a certain percentage of the price limit), the level or percentage of the temporary price limit increase/decrease compared to the harmonised price limit, and the standard period for temporary exemptions before the price limit return to their original level.

The NEMOs should also make sure that market participants are consulted on the detailed decision making process in the NEMO Committee that would lead to such measures being taken.

- *What is your view in general about possible existence of derogations, and do you find that, when such decisions are made, the measures proposed to ensure consideration of overall objectives are sufficient?*

See our points below in response to Q4 and our answer to Q1.

5. Do you have other specific feedback on this Min-Max Proposal?

Regarding sections 6.4 and 6.5, it seems that there is a high likelihood that the assessment process for a review of the permanent limit would be based on the same considerations as the temporary change, i.e. a “significant risk that the min/max prices will be repeatedly reached”.

Applying the same conditions as for the temporary lift of caps/floors misses the point that **the mere existence of min/max prices that do not reflect VoLL do influence market participants’ expectations and naturally limit the possibility of prices reaching the limits.** We refer to our answers to Q1 on this point. The methodology should clarify the conditions that would trigger a review of the price limits, as per our proposal for the temporary exemption in our answer to Q4.

We also request that the **periodic assessment of section 6.5 is turned into an actual review of the min/max price limits to ensure that the VoLL is reflected to in the day-ahead and intraday min/max price limits.**