

**European Regulators Group
for Electricity and Gas**
Rue le Titien 28
B-1000 BRUSSELS

E-mail to: balancing-integration@ergeg.org

CC to asta.sihvonen-punkka@emvi.fi and
tahir.kapetanovic@e-control.at

Brussels, 3rd August 2006
AMG/EdH/nh

Dear Madam,
Dear Sir,

We noted with interest the ERGEG consultation paper on guidelines of good practice for electricity balancing market integration and we much appreciate the opportunity to participate in this public consultation and to provide comments. We are currently finalising a position paper which addresses both cross-border intra-day and cross-border balancing markets. We intend to present the paper to the Florence Forum in the autumn of this year.

As outlined in our Oslo Declaration, integration of intra-day and balancing markets is crucial to any further development of electricity markets. The ERGEG draft document is a valuable analytical paper which highlights the challenges lying ahead for the integration of such markets and raises a number of questions that need to be addressed. However, at this stage we consider this draft more a discussion paper than guidelines since the basic framework and the way forward still need to be tackled. Indeed, we believe that further work and a **clear indication from ERGEG of the way forward are needed.**

Whilst balancing is key to the further integration of electricity markets, we feel that an important link in the sequential approach is missing. We believe that liquidity should initially be created in the forward and day-ahead markets and as this is developing, the process should be extended to intra-day markets, which will in turn create momentum for bringing together balancing markets. Day-ahead OTC- and exchange-based markets are becoming increasingly liquid, allowing them to function as reliable reference for financially settled products on the long-term markets. It is now essential in our view that **regulators focus first and foremost on developing and integrating intra-day markets. Developing appropriate, well functioning and liquid intra-day markets, including across borders, will enable market participants to trade and close their position to the largest extent on the intra-day markets as close to delivery as possible.** This will result in only limited volumes being left to balancing markets, which can then be used to keep the system physically in balance. In addition, regulators should ensure that there is sufficient harmonization of existing balancing markets across Europe. If creation of intra-day markets and sufficient harmonization are not taken as a priority, it will prove impossible to integrate balancing markets. Therefore, we feel that the last section (Section 8 “Options for the Integration of Balancing Markets”), leaving three options open, requires further in-depth discussion, in particular in relation to the statements about reservation of cross-border capacity on which we will elaborate later on in this letter.

Maximisation of commercial available cross-border transmission capacity is a crucial issue to increase the level of cross-border trading, meaning that reservation of cross-border capacity must be considered with great care. In our view, **cross-border intra-day and balancing markets can develop and be well functioning without implying specific reservation of capacity** for balancing purposes (as suggested in Section 5 of the ERGEG draft under the heading “Acquisition of transmission capacity for balancing purposes”). We therefore have **concerns over ERGEG’s proposal** to opt for such cross-border transmission capacity reservation and our arguments are as follows:

- Article 6(3) of the Electricity Cross-Border Regulation 1228/2003 states that TSOs are obliged to maximise the capacity they offer to the market, a principle which we fully support. TSOs should not be allowed to reserve transmission capacity for balancing purposes, as this would not result in the most efficient usage of the available capacity.
- Transmission capacity is a scarce resource and must be allocated on a non-discriminatory basis to ensure the most efficient usage. It is very difficult **to determine the balance between alternative uses for transmission capacity** as it requires transparent and non-discriminatory pricing. Currently, this is not possible as products without a nomination deadline are not defined and are thus not tradable. Indeed, transmission rights for reserve and balancing products have a different nomination deadline as currently allocated long-term and day-ahead capacity rights and therefore have a different value.
- If transmission rights appropriate for reserve and balancing purposes are defined, TSOs and regulators would have to ensure that such transmission capacity was available to all market participants in a non-discriminatory and transparent way. If TSOs wanted to make use of such a product, they would have to participate as buyers on the capacity market, organised by themselves, and compete with other interested market participants.

Furthermore, the issue of **firmness of capacity** is not addressed by the ERGEG guidelines. We believe that it is very important for further integration of European markets that market participants can rely on the fact that transmission capacity they have procured from TSOs via market based mechanisms is firm and provides an effective hedge between buys and sells in neighbouring markets.¹

All the issues described above will be addressed in further detail in the upcoming EURELECTRIC Position Paper and notably the series of actions we believe are needed to trigger progress in both cross-border intraday and cross-border balancing markets.

We have highlighted below some further specific comments on the guidelines which we would like to see considered in the consultation process:

- a. We would like to urge ERGEG to also address the issue of **balancing criteria** which are to be applied by TSOs in a control area. It should however be stressed that the level of the used criteria should be set at an appropriate level in order not to require larger than necessary balancing resources, i.e. a balance has to be found between efficiency of the balancing mechanism and security of supply.

¹ Firmness could also be guaranteed either via integrated balancing markets or via cross-border intra-day markets. Indeed, once the intra-day market has proven its efficiency, TSOs should then have the right to be a market participant on the cross-border intra-day market in order to buy back capacity they oversold previously, provided there is proper regulation, market monitoring and transparency on their trading activities. This would necessitate sufficient harmonisation of the roles and procedures of TSOs across borders and strong and seamless co-operation between the involved TSOs of a regional market.

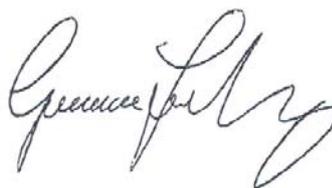
- b. We also question why **automatically activated power reserves** (primary and secondary reserves) are excluded from the ERGEG draft as stated in the background paragraph of Section 1. In many markets, secondary control energy constitutes a huge proportion of the balancing of the control area, with the manually activated share sometimes being relatively low. Therefore, we point out again that the scope of the ERGEG draft guidelines should include the automatically activated power reserves.
- c. In **Section 5 on “Efficiency and competition”** reference is made to the possible harmonisation of payment schemes for capacity payments. We believe that it is necessary to carry out a thorough analysis of the different situations before proposing the ways and means of delivering harmonisation.
- d. With regard to the **“Fundamental features” in Section 3**, we believe that it is necessary to clearly define the term “balancing power”. We understand this term to mean “procurement of reserved generation capacity for balancing purposes”, but not the procurement of the energy itself. The market based methods referred to in this Section for the procurement of “balancing power” would also benefit from further clarification.
- e. Concerning the selection of bids as addressed in **bullet point 3 in Section 5 “Operation of balancing mechanism and market”**, we strongly support ERGEG’s view that a deviation from the merit order can be accepted only if it is necessary to maintain system security or if it can be justified in accordance with **pre-defined criteria**. It should however be pointed out that one of the reasons for such an overruling in an integrated balancing market might be congestion between or even within control areas. In the case of congestion between control areas, there should be a split of the imbalance price between those areas. In the case of congestion within a control area, the bids used for solving the internal congestion should not influence the imbalance settlement price for the balancing responsible parties.

We hope that these comments prove useful and look forward to our continued dialogue. We are at your disposal to discuss any points you may consider relevant in the follow-up of your work.

With best regards,



Tony COCKER
Co- Chairman, WG Wholesale
Markets & Trading



Gunnar LUNDBERG
Chairman, WG Wholesale
Markets & Trading

Encl.: EURELECTRIC comments' table

EURELECTRIC comments

No	Chapter / Section	Comment		
1.	General + Section 8	EURELECTRIC calls ERGEG for <u>further work on their paper</u> and <u>a clear indication of the way forward</u> (including on the options for the integration of balancing markets).		
2.	General	ERGEG should focus first and foremost on <u>developing and integrating intra-day markets</u> and improving their functioning. Balancing market integration is only a further step.		
3.	General	Intra-day markets, including across border, should be developed for market <u>participants to trade and close their position to the largest extent possible on the intra-day markets</u> as close to delivery as possible. This will result in limited volumes being left to balancing markets.		
4.	Section 5, subsection “Acquisition ...”	<u>Reservation of cross-border capacity</u> must be considered with great care, as in EURELECTRIC’s view cross-border intra-day and balancing markets can develop and be well functioning without implying reservation of capacity (EURELECTRIC sets out in 3 bullet points the issues to be considered concerning the reservation of cross-border capacity)		
5.	General	The issue of <u>firmness of capacity</u> should be addressed in the ERGEG guidelines as this is an important factor for further integration of European markets.		
6.	General	The issue of <u>balancing criteria</u> which are to be applied by TSOs in a control area should be addressed in the ERGEG guidelines, whereby striking a balance between efficiency of the balancing mechanism and security of supply.		
7.	General + Section 1	EURELECTRIC questions why <u>automatically activated power reserves</u> (primary and secondary reserves) are excluded from the guidelines and asks for inclusion.		
8.	Section 5, subsection “Efficiency and competition”	EURELECTRIC believes it necessary to carry out a <u>thorough analysis of the different payment schemes for capacity payments</u> before proposing ways and means of delivering harmonisation.		
9.	Section 3, subsection “Fundamental features”	EURELECTRIC asks for a <u>clear definition of balancing power</u> which is understood as “procurement of reserved generation capacity for balancing purposes”.		
10.	Section 5, subsection “Operation ...”, bullet point 3	EURELECTRIC supports ERGEG view that a deviation from the merit order should only be possible following pre-defined criteria; congestion between or within control areas can constitute such a criteria.		