

Subject: FEBEG comments on CREG's public consultation on ELIA's objectives in the context of the incentive to promote balance in the system

Date: 3 July 2020

FEBEG thanks CREG for the organization of a public consultation on the objectives to be achieved by Elia Transmission Belgium SA in 2021 in the context of the incentive to promote the balance of the system referred to in Article 27 of the tariff methodology ¹. Please find hereafter the comments of FEBEG in the framework of this consultation. The comments and suggestions of FEBEG are not confidential.

Background

In order to promote the balance of the electricity system, and after consulting Elia, the CREG decides the conditions for granting a financial incentive of € 2,500,000 to the realization, during the year 2021, of following seven objectives (or projects) within the given deadlines:

1. Establishment of a framework for the development of scenarios for Elia's prospective studies, in consultation with market players
2. Prediction of the "System Imbalance" and study of its provision to market players
3. Analysis of the conditions necessary for the development of a "technology neutral" framework for the use of so-called limited-coordination units (in the framework of participation to ancillary services)
4. Review of existing baseline methodologies and analysis of evolutions or developments of new methodologies
5. Analysis and modernisation of the schedules that enable the designation of multiple BRP's for a single connection point
6. Development of a new methodology for the daily predictions of the volume of non-contracted aFRR and mFRR balancing energy bids which are available within the LCF Block
7. Scarcity pricing

General Remark

FEBEG specifically wishes to underline its deep concerns regarding the proposed approach and timing mentioned in the incentive related to Scarcity Pricing.

FEBEG would also like to highlight that Scarcity Pricing will not solve the adequacy issues and that the introduction of Scarcity Pricing in Belgium alone (and not in parallel in neighbouring countries) has dangerous consequences for the level playing field of market participants and entails risks of market distortion.

¹ <https://www.creg.be/fr/consultations-publiques/les-objectifs-a-atteindre-par-la-sa-elia-transmission-belgium-en-2021-dans>

<https://www.creg.be/nl/openbare-raadplegingen/de-doelstellingen-die-nv-elia-transmission-belgium-2021-moet-behalen-het>

Detailed remarks

1. Establishment of a framework for the development of scenarios for Elia's prospective studies, in consultation with market players

FEBEG would like to stress that the involvement of market players is key for developing scenarios for prospective studies. Indeed, these scenarios should be in line with the necessity of an energy transition to a low-carbon economy and the contribution of the electricity sector to the upcoming smart sector integration at European level. This transition will require huge investments by market players in the electricity sector (generation, storage and demand response), but also in other sectors (transport, industry, agriculture) and activities (renewable and decarbonized gases, energy efficiency, etc.). FEBEG therefore believes that ensuring the relevance of any prospective scenario requires the appropriate framework for "co-creation" and an active participation of market players.

FEBEG is strongly committed to contribute to such exercises that will help the electricity and gas sectors to contribute to the long-term decarbonization objectives.

2. Prediction of the "System Imbalance" and study of its provision to market players

We support the study on this subject, with the envisaged three phases. We are interested in the results of such a study and the reliability that can be obtained. We also wonder if the result of such a prediction model could be used for setting clear and transparent rules for the activation of mFRR, which is a request that has been voiced by FEBEG on several occasions.

3. Analysis of the conditions necessary for the development of a "technology neutral" framework for the use of so-called limited-coordination units

We have our reserves on the usefulness of such a study, this is something which has been assessed in 2019 after the end of 'Slow R3 non-CIPU', which was created for the winter 2018-2019. The conclusion in 2019 was that it is not useful to prolong such a product. If such a study would be pursued, it would be good to compare possible benefits with the costs an implementation of such a product would bring.

4. Review of existing baseline methodologies and analysis of evolutions or developments of new methodologies

We support further analysis and reflection on this subject. We think it is useful to assess best practices in Belgium and neighbouring countries and to benchmark what is currently done versus new insights of TSO and market actors. We therefore support this study.

5. Analysis and modernisation of the schedules that enable the designation of multiple BRP's for a single connection point

We are not opposed to this proposal, as it could unlock new possibilities for market actors, but we however fear increased complexity regarding communication processes and settlement that would need to be implemented. We recommend that these impacts are part of the study as well.

6. Development of a new methodology for the daily predictions of the volume of non-contracted aFRR and mFRR balancing energy bids which are available within the LCF Block

We believe that there is a potential mismatch or inconsistency between on one hand the discussion in the context of offshore integration (in which BRPs are increasingly being asked to balance their portfolio and have the means to do so) and on the other hand the use of non-contractual flexibility to cover Elia's reserve requirements. The same issue exists in the MARI/PICASSO design in which BRP/BSP cannot change their explicit bids 20–25minutes before real time (which could be interpreted as the TSO having priority on this flexibility). If the same non-contracted means are to cover the BRP's needs and the TSO's needs, it must be avoided unambiguously that this leads to a double use, where in the end the BRP will be penalized. We will be very attentive to these elements in the study.

7. Scarcity pricing

Overall remarks on scarcity pricing principles and potential impact on energy market functioning

FEPEG is a strong supporter of measures to improve the functioning of short-term electricity markets, as currently being implemented through the European Guidelines CACM and EBGL, as well as the recast European Electricity Regulation. These measures will improve the market functioning and make the short-term price signals more market driven. However, FEPEG has consistently argued that **well-functioning short-term markets improve economic signals for flexible capacity, but do not provide any investment signal that is required to ensure long-term adequacy**. One should not oppose short-term market improvements (scarcity pricing) and long-term aspects (adequacy). Moreover, they should not be discussed sequentially but parallelly given the different industrial constraints linked to operations and investments.

Concerning the existence of this incentive in the list of objectives to be reached by Elia in 2021, it should be clarified what issue ~~the~~ **scarcity pricings** aims to tackle. As it **does not provide any structural investment signal**, such a mechanism will therefore not trigger any investment required to meet the adequacy standards. On the other hand, if the scarcity pricing aims to further improve market signals for flexible capacity, it should be noted that multiple measures are currently already being implemented to improve such signalling, such as Pay-as-Cleared/Marginal Pricing for balancing products and improved Intraday markets, as well as improving market access for Demand Response.

It is also not clear to which extent the scarcity pricing on a tense Belgian network will back-propagate on an interconnected EOM market. FEPEG considers that a clear analysis should be made how scarcity pricing could impact and shape the Belgian and European electricity market. Looking exclusively at the national market should really be avoided given the very high interconnectivity of the Belgian market with other European ones, and this at different timeframes (forward, day-ahead, intra-day, real-time).

Finally, it should also be noted that the study made by Elia (published on 10 December 2018) regarding scarcity pricing raises important concerns on the viability of a scarcity pricing measures in the Belgian context. The lack of a real-time reserve market significantly reduces the impact scarcity pricing can have in a Belgian – and even European – context. As such, it is highly questionable whether scarcity pricing can realistically become an effective measure to further enhance the measures already currently under implementation.

FEBEG considers that marginal pricing in the balancing context (for pricing balancing energy as for settling imbalance), if correctly implemented, is sufficient to meet the objective of imbalance settlement price which is to make sure BRPs are balanced, or where relevant and where allowed, adjust their position in real time to help the system. Pricing elements that are added to the imbalance price reduce the visibility the BRPs need, distort the price signal deviating from the pure marginal approach and preclude a true level playing field amongst EU countries that are about to link their balancing markets through Balancing Capacity Cooperation and participation to European Balancing platforms.

FEBEG therefore regrets the recent ACER decision on the pricing of aFRR which will apply the marginal pricing mechanism to the optimization period (4 seconds) rather than to the ISP (15 minutes).

Issues related to the timing and approach mentioned in the incentive towards Elia

In its draft decision, CREG indicates that it will take a decision on the implementation of the scarcity pricing mechanism at the end of 2020. **FEBEG wonders on which current legal basis CREG would be allowed to make such decision unilaterally.** According to FEBEG, the Belgian Authorities should be involved on the decision-making process.

Concerning **the timing proposed by the CREG** in its draft decision for the implementation of the scarcity pricing mechanism, FEBEG considers it **is not realistic**. CREG drives Elia to implement scarcity pricing by 01/01/22, which is very ambitious. This is particularly true when considering that some market concepts – such as a real-time reserve market – are currently missing to properly implement a scarcity pricing mechanism.

The design and the implementation paths will probably not be ready by 2022 when considering the needed amendments and impacts on T&C BRP, the tariffs or the Federal Grid code.

In the frame of Belgium’s implementation plan, FEBEG takes note of the EC’s request to consider adapting the market rules related to price formation in moments of scarcity by 2022. FEBEG understands that the CREG would like to mirror the EC request somehow in the proposed list of incentives for 2021.

However, FEBEG would like to stress that if a scarcity pricing scheme would be developed in Belgium, a few key principles should be duly respected in any case:

1. Enhanced market-parties involvement given the needed rules adaptations for a proper implementation of the scarcity pricing, the impact on BSP and BRP will be very important. It is therefore crucial to involve the market parties soon enough in the design and implementation process.
2. Full transparency and replicability of the inputs, applied formula and outputs: Market parties should be able to anticipate any activation of the “scarcity patch” and estimate its effect on the imbalance price.
3. Real scarcity cost and level playing field: the formula should reflect the cost of scarcity in real time, be considered in a regional setting to avoid market distortions and competitiveness issues for Belgian consumers (households and industries)

Respecting these principles imply that the implementation timeline has to be decorrelated from the implementation timeline of the capacity market, as investment decisions have to be taken by market parties in 2021 to ensure that the adequacy criteria is ensured by 2025.

Existing mechanisms and alpha component

FEBEG suggests to review existing mechanisms such as the current setting of the alpha component in the calculation of the imbalance price at the same time. As a reminder, we hereafter list FEBEG's position concerning this alpha component (price adder):

Distortion of the price signal

Indeed, article 44.1(b) Electricity Balancing Guideline (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 EBGL principles, the imbalance settlement price mechanism should de facto provide an adequate price in situations of scarcity. As a result, adding an administrative component would be distortive since it would reduce the ability of imbalance prices to effectively reflect the real time value of the energy and would jeopardize the proper signalling function of an efficient imbalance settlement price. It would create counter-incentives and thus trigger inefficient behaviour by BRPs.

Distortion of the level playing field between countries

In addition, since the imbalance settlement harmonization proposal recently proposed by ENTSO-E did not provide any harmonized methodology for such an administrative scarcity component, FEBEG is concerned to see national uncoordinated adders to be developed. The EBGL foresees an integrated balancing market. Implementing such administrative component in a non-coordinated way would lead to different imbalance price behaviour with similar imbalance volumes in the different control areas. This would be a threat to level playing field in the European electricity markets.

Contradictory to measures to reduce the occurrence of price spikes

The Pricing Proposal currently under consultation by ENTSO-E introduces the new concept of a Balancing Energy Pricing Period (BEPP). One of the objectives to introduce the BEPP is to reduce the occurrence of price spikes. FEBEG questions why on the one hand measures are being formulated to suppress the real-time value of energy, while on the other hand 'incentivizing components' such as the alpha component are necessary to artificially increase the imbalance settlement price. It would be more efficient, more market-based and more transparent to avoid all such artificial interventions into the balancing prices and instead allow the market to function properly.