

26 September 2013

ČEZ, a. s.

Identification number in the EC register:

429600710582-32

ACER

Trg republike 3

1000 Ljubljana

Slovenia

Reply of the CEZ Group to the public consultation on the influence of existing bidding zones on electricity markets

General

We welcome the opportunity to discuss appropriateness of current setting and potential redefinition of bidding zones. Origin and development of electricity markets as well as their liquidity reflects many natural factors. RES supporting schemes have substantially affected development of liberalised market and have caused market distortions. Rapid development of RES, e.g. in Germany, without adequate investments into transmission system leads to relocation of negative effects and related costs on neighbouring TSOs and thus on final customers and consumers in those Member States. One of the resulting effects is limitation of available transmission capacities in the CEE region.

Q&A

1) How appropriate do you consider the measure of redefining zones compared to other measures, such as, continued or possibly increased application of redispatching actions or increased investment in transmission infrastructure to deal with congestion management and/or loop flows related issues? What is the trade-off between these choices and how should the costs attached to each (e.g. redispatching costs) be distributed and recovered?

The most important thing for proper functioning of European wholesale market is existence of sufficient transmission infrastructure enabling trading in all time profiles – forward, day-ahead, intra-day, balancing. In case there is insufficient transmission capacity within a single bidding zone, possible enlargement would lead only to escalation of the problem, not to solution of the problem. On the contrary, making the zones smaller (e.g. in case of DE-AT zone) could help to transparently solve not only proper investment signals but also situation about unplanned flows [1], [2].

The field of cost allocation on redispatching has not been sufficiently resolved so far and therefore we suggest not enlarging bidding zones.

According to our opinion main measure for redefining zones shall fulfil certain minimum criteria of compactness and sustainability of existing bidding zones like:



- number of critical lines inside zones
- market homogeneity (e.g. same market design within the entire bidding zone)
- proportion of cross-zonal capacity reduction (available capacity: total physical capacity on zone border)
- intensity of redispatch inside zones
- physical loop flows influencing neighbouring zones

2) Do you perceive the existing bidding zone configuration to be efficient with respect to overall market efficiency (efficient dispatch of generation and load, liquidity, market power, redispatching costs, etc.) or do you consider that the bidding zone configuration can be improved? Which advantages or disadvantages do you see in having bidding zones of similar size or different size?

From longer term point of view we do not see as a sustainable solution keeping bidding zones that do not have sufficient transmission capacities (DE-AT) and that do not have sufficient tools for redispatching within the zone. Negative impacts of such connection are evident from common positioning documents of TSOs: [1], [2].

Presented assumption “Bigger zones higher liquidity” is tricky. It depends on the quality of grid inside zones. Big zones with a lot of critical lines (congestion) inside, require keeping high production reserve for local congestions. Thus lines’ capacities are not freely traded and are not subject of competition. This leads to lower liquidity and higher market price. Good example of well-functioning multiple bidding zones market is Nordpool.

It is not substantial per se whether bidding zones have similar size or not. There are objective reasons why some of the markets are smaller or greater and there is no reason to artificially enlarge them unless there is sufficient interconnection.

There is one exemption within the CEE region where the bidding zone border differs from borders of particular Member States. One should therefore consider whether it would not be more appropriate to respect borders of Member States instead and implement standard congestion management procedures on all borders, e.g. day-ahead market coupling, implicit continues intraday etc.

3) Do you deem that the current bidding zones configuration allows for an optimal use of existing transmission infrastructure or do you think that existing transmission infrastructure could be used more efficiently and how? Additionally, do you think that the configuration of bidding zones influences the effectiveness of flow-based capacity calculation and allocation?

For capacity calculations it is important to use common transparent grid model that reflects all borders and inner-grid constraints. As far as the CEE region is concerned, individual bidding zones are identical with borders of individual Member States with the exemption of DE-AT profile.

Physical capacity of transmission system is fixed until new line is built. Implicit market coupling increases effective utilization of existing cross-zonal capacities. However, at the moment implicit market coupling is present only



among selected bidding zones. Method of calculation capacity either NTC or Flow Based calculation has minimum differences in additional contribution

Redefining bidding zones will not affect available capacities significantly but it will fairly allocate costs of critical lines inside bidding zones and instead of exporting them to other bidding zones.

4) How are you impacted by the current structure of bidding zones, especially in terms of potential discrimination (e.g. between internal and cross-zonal exchanges, among different categories of market participants, among market participants in different member states, etc.)? In particular, does the bidding zones configuration limit cross-border capacity to be offered for allocation? Does this have an impact on you?

Current practice within the CEE region shows that offer of unlimited transmission capacity on DE-AT profile causes problems to neighbouring TSOs, who are therefore forced to limit available capacities for cross border energy exchange on the remaining profiles within the region.

Practical and real impacts are documented in studies of TSOs in the region: [1], [2].

Reserves for unpredictable flows due to congestion inside DE-AT bidding zone reduce cross-zonal capacities and discriminate producers on the DE-AT zone borders in comparison with producers within the zone. DE-AT border should be in same regime as other borders. If the DE-AT capacity is truly unlimited then implementing implicit market coupling will not affect these producers and the AT and DE price will be coupled continuously.

5) Would a reconfiguration of bidding zones in the presence of EU-wide market coupling significantly influence the liquidity within the day-ahead and intraday market and in which way? What would be the impact on forward market liquidity and what are the available options to ensure or achieve liquidity in the forward market?

The target model for international day-ahead market is an implicit market coupling mechanism based on common grid model and flow based calculation of available capacities that are subsequently at daily market organiser's disposal. This mechanism enables market splitting in case the capacity on particular profile is exhausted due to commercial split of flow. This condition is not fulfilled at the moment on the DE-AT profile.

In case implicit market coupling were introduced on the DE-AT profile, there would be no threat of lowering day-ahead's liquidity because daily markets remain connected through market coupling. Furthermore, we use the hypothesis that liquid forward market can be functional only if case a liquid day-ahead market exists. Because of the fact that the condition of liquid spot market is not threatened and accessibility of transmission capacities will not be worse, this cannot lead to liquidity decrease on forward markets.

6) Are there sufficient possibilities to hedge electricity prices in the long term in the bidding zones you are active in? If not, what changes would be needed to ensure sufficient hedging opportunities? Are the transaction costs related to hedging significant or too high and how could they be reduced?

For hedging purposes it is not important to have one price level and one price zone. There can be more price levels in different zones. For effective hedging



it is important to have high correlation between zones. That is reached by allocating sufficient capacities to cross-zonal borders. In case of low liquidity in one zone, one can hedge in another price zone if sufficient cross-zonal capacity is secured.

7) Do you think that the current bidding zones configuration provides adequate price signals for investment in transmission and generation/consumption? Can you provide any concrete example or experience where price signals were/are inappropriate/appropriate for investment?

According to our opinion, the existence of the common bidding zone DE-AT does not create sufficient investment signals into cross-border DE-AT profile, nor into powerplants' construction.

8) Is market power an important issue in the bidding zones you are active in? If so, how is it reflected and what are the consequences? What would need to be done to mitigate the market power in these zones? Which indicator would you suggest to measure market power taking into account that markets are interconnected?

ČEZ does not have any significant market power in spite of having most of its assets in one bidding zones because the CZ bidding zone is well connected with the neighbouring zones.

9) As the reporting process (Activity 1 and Activity 2) will be followed by a review of bidding zones (Activity 4), stakeholders are also invited to provide some expectations about this process. Specifically, which parameters and assumptions should ENTSO-E consider in the review of bidding zones when defining scenarios (e.g. generation pattern, electricity prices) or alternative bidding zone configurations? Are there other aspects not explicitly considered in the draft CACM network code that should be taken into account and if so how to quantify their influence in terms of costs and benefits?

ENTSO-E should ensure that each Member State applies transparent capacity allocation mechanism and congestion management procedure on its border in harmony with the requirements of the EU legislation (Regulation 714/2009). This requirement is not currently fulfilled on the DE-AT profile. In addition we consider fundamental to carry out cost-benefit analysis for individual alternative scenarios.

10) In the process for redefining bidding zones configuration, what do you think are the most important factors that NRAs should consider? Do you have any other comments related to the questions raised or considerations provided in this consultation document?

NRAs should ensure that each bidding zone is a compact area with sustainable grid with minimal congestion inside the zone, especially no congestion between places of production and places of consumption and with no impact on neighbouring bidding zones coming from congestion inside bidding zone.

NRAs shall decide about redefining of bidding zones if there is:

- high number of critical lines inside the zone or
- high reduction of cross-zonal capacity for market or



- high need of cross-zonal re-dispatch or
- significant loop flows influencing neighbouring zones
- insufficient market homogeneity (e.g. different market design within one bidding zone).

The practice shows that big zones with inner congestions bring complications and redistribution of costs on mitigation of congestion and higher costs for unplanned flows are transferred to neighbouring countries/TSOs – see the case of splitting of Sweden by EC [3] or studies of CEE TSOs [1], [2] Each Member State should apply transparent capacity allocation mechanism and congestion management procedure on its border in harmony with the requirements of EU legislation (Regulation 714/2009). This requirement is not fulfilled on DE-AT profile.

Unrestricted commercial flow between DE-AT leads to trading of such amount of energy in Germany which cannot be transmitted by German grid inside Germany nor further to Austria. This leads to systematic overloading of neighbouring systems where unplanned flows cause additional costs and worsen reliability of operation of transmission systems.

With regards to aforementioned we suggest splitting of common DE-AT bidding zone into two separate zones in which standard mechanism of market coupling/splitting will be applied. According to our opinion such splitting will have positive effect on competition in CWE and CEE regions due to higher transparency and will not have significant impact on liquidity on exchanges due to application of market coupling.

[1] Study of ČEPS, MAVIR, PSE and SEPS – Bidding Zones Definition, March 2012, available from: http://www.ceps.cz/ENG/Media/Tiskove-zpravy/Documents/120326_Position_of_CEPS_MAVIR_PSEO_SEPS-Bidding_Zones_Definition.pdf

[2] Unplanned Flows in the CEE Region, January 2013, available from: http://www.ceps.cz/CZE/Media/Tiskove-zpravy/Documents/German-AustriaMA_Study.pdf

[3] Splitting of Sweden, available from: http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=1_3_9351