

Swedenergy's answer to ACER's *Public consultation on the influence of existing bidding zones on electricity markets*

General comments

The agency for the Cooperation of Energy Regulators, ACER, has asked for answers on issues concerning the optimal size of a bidding zone.

Swedenergy welcomes the opportunity to assist ACER in the work to achieve a better congestion management in Europe. We see this consultation as one important part. However, in our view, the Technical Report prepared by ENTSO-e is the crucial part of the development in this area. A proper report would outline where the current problems are, where they are alleviated by using cross-zonal capacities rather than congestion management where the bottlenecks occur, and also give some measure of the size of the problem in different areas. In general, Swedenergy endorses the right for national regulatory agencies to decide which measures (market splitting or counter trade) that should be used to handle congestion. However, in our view the most important issue for ACER when dealing with the size of the zones, is to safe guard that the cross-border infrastructure is used efficiently and thus that trade is not impeded by moving internal congestion to the border.

The relative size of bidding zones seems to be of little, if any, relevance in respect to overall *wholesale* market efficiency (i.e., market power is not affected by the size of the zone). However, having internal congestions within an area may imply that demand reactions to price variations can take place in the "wrong" location in respect to the congestion thereby increasing the amount of counter trade or redispatch needed. Additionally, a larger amount of bidding areas if they are reflected in price zones, increase *retail* risk. Thus it is important that the TSOs align with the target model and increase the financial firmness of the underlying transmission grid for example by auctioning financial instruments.

Answers to the questions

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 definition of an “optimal bidding area” is not in contrast to efficient counter trade or cost based re-dispatch. Assuming that congestion is handled where it occurs it is rather two issues that have to be dealt with by the NRA. First, what are the signals to the market that is sent by a particular congestion management method (nb moving problems to the border conceals scarcity and thus signals strengthening of the grid in different areas). The other issue, highlighted by the SvK vs The European Commission is who should pay for the congestion management. If counter trade is needed to avoid suboptimal use of the grid this raises the rather difficult issue of who should pay for this counter trade. This could be alleviated by for example creating regional TSOs.

Additionally, it is important to distinguish between short term and long term congestion management. Transmission investments takes time to establish, and in anticipation of capacity additions the congestions must be managed. The costs related to the short term measures should preferably be attached to the entities bearing the benefits from the measure.

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?

Generally, bidding zones should be closer to the limits of the transmission network and not be constrained by the borders of TSOs. However, to evaluate existing configurations transparency on the state of the transmission grid is necessary. Relevant information for this evaluation should be made available in the Technical Report prepared by ENTSO-E.

The Technical report should bring transparency between actual congestions within a bidding zone, relieved by counter trade or redispatch in the real time market, and expected congestions within zones managed before real time. It is not sufficient to evaluate the amount of counter trade or redispatch as historical figures might be biased in case congestions within a bidding zone have been relieved by restricting the available transmission capacity on the bidding area border.

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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?

Increasing the transparency of congestion management, and thus preventing moving internal congestion to control zone border should by itself increase the use of the European transmission grids. Thus congestion inside a bidding area should be resolved by counter trading or redispatching in the short term time frame i.e. from day ahead gate closure until real time operations. Short run efficient transmission use should be possible within the current configuration. We note that, the technical report prepared by ENTSO-E should be transparent enough to reveal the extent congestions within particular bidding areas have been resolved by restrictions on the bidding area borders.

In the long run ACER should supervise the investigations into merging some bidding areas despite them belonging to different TSOs. Examples of this could be southern Sweden and Eastern Denmark.

The definition of the zones may have lesser impact on the efficiency of the flow-based allocation method than for example the security margins applied within the zones. Thus we would urge ACER to supervise how these security margins are defined, and if possible abuse leads indirectly to moving internal congestion to control area borders.

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?

An efficient congestion management would mean that cross-border exchanges would not be impacted. However, as the current practices are hidden from public view, The Technical Report prepared by ENTSO-is thus crucial to determine the potential extent of discrimination between a TSOs internal customers and cross-zonal customers.

The bidding zone configuration itself does not limit cross border capacity, but rather the practice of not managing a congestion where it occur, e.g. referring to priority access rules. As noted above, reliability margins and the trade capacity between bidding areas should be continuously monitored by the competent authorities to avoid disturbances of cross-border trade. Distorting trade hurts economic efficiency as it in the short run prevents a correct price formation. In the long run it hurts decisions on efficient transmission development as the real scarcity signals are hidden.

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?

We interpret the future legislation such that the capacity between bidding areas is left to market coupling. Given the fact that day ahead capacity between areas is left to market coupling this would imply a push towards higher volumes traded in the day ahead market.

The splitting of a bidding area into several as was done in Sweden implies that the transmission risks between zones is shifted to the market actors. A congestion between the bidding areas is now revealed as a price difference. Requiring TSOs to auction long term financial transmission capacity in the form of e.g, Financial Transmission Rights (FTRs) or Contracts for Differences (CfDs) would alleviate some of the current risks. (The latter would in reality make it possible for actors to create a

synthetic FTR thus in the long run lead to harmonization of risk hedging between the Nordic market and the continental part of the European market).

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?

With the use of financial products based on a calculated Nordic price index, the System Price, it is to a large extent currently possible to hedge electricity prices in the Nordic market. The use of CfDs facilitates hedging in some but not all of the separate bidding zones. For some bidding zones, there are no CfDs at all, whereas in other areas, the liquidity of CfDs may be less than satisfactory. Therefore, it would be beneficial for the market development that the TSOs would participate by auctioning the underlying transmission capacity, thus accommodating the actors' possibilities to hedge their long term exposures.

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?

It is crucial that The Technical report prepared by ENTSO-E makes information on the transmission grid available for market actors, for example information on the current spatial occurrence of congestion, frequency of these congestions and how they have been managed.

Only distorted prices may give rise to inappropriate investment signals. Thus it is important that real congestions are not hidden with practices moving congestion to borders, etc.

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?

Market power is not an issue in the Nordic market. If anything, the wide use of bidding areas as congestion management has moved more quantities into the day-ahead market, thus increasing the transparency in the price formation.

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?

The review should focus on where the real congestions are, and thus if trade across zones are in any way hindered by for example local interpretations on priority dispatch rules. The costs for counter trade and redispatch must be transparently accounted for. This must be analysed in conjunction with the used capacities at the borders. The legislation should be aimed for reasonably stable and robust bidding zones over time.

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?

The creation and changing of bidding must be clarified legally. In an optimal situation the objective criteria for creating the bidding zones, as well as the changing of the zone should be defined in law and supervised by the regulatory authority. When implemented, a working definition on what is structural versus temporary congestion must be defined.

Stockholm 25/9 2013



Anders Richert
Head of Units, Network and Trading