

TIWAG - Energy with Perspectives

ACER  
Trg Republike 3  
1000 Ljubljana  
Slovenia  
Mailto: [consultation2013E04@acer.europa.eu](mailto:consultation2013E04@acer.europa.eu)

person in charge: Dipl.-Ing. Markus Watscher  
Bereich Stromhandel und Ener-  
giewirtschaft  
Dispatching  
Eduard-Wallnöfer-Platz 2  
6020 Innsbruck  
phone: +43 (0) 50607 21593  
fax: +43 (0) 50607 41593  
mobile phone: +43 (0) 699 1257 2593  
e-mail: [markus.watscher@tiwag.at](mailto:markus.watscher@tiwag.at)  
internet: [www.tiroler-wasserkraft.at](http://www.tiroler-wasserkraft.at)

**Public Consultation on bidding zones**

**Comments by TIWAG-Tiroler Wasserkraft AG (Register ID number: 80966174852-38)**

Dear Madam,  
Dear Sir,

TIWAG-Tiroler Wasserkraft AG welcomes the opportunity to respond on the consultation document: The influence of existing bidding zones on electricity markets, 31 July 2013. The design of bidding zones is indeed central for the market functioning on a national/European level.

**General remarks**

The Third Energy Package aims at a unified, single electricity market.

A well-functioning competitive and unified wholesale electricity market will best:

- Result in social welfare given that bidding zones are as big as possible until a single bidding zone is achieved
- Enable market participants to hedge production and consumption
- Guarantee security of supply
- Minimize regulatory intervention and therewith minimize general expenses to be borne in the end by consumers

We acknowledge the role of TSOs in developing the internal electricity market and emphasize that particularly increasing RES production requires intensified cross-border cooperation between TSOs. But TSOs' work is only one track in completing internal market. The second one is pursued by the market participants as they have to live the market rules and in the end have to take over negative as well as possible positive consequences in their daily work.

Given these two key players in completing the internal market we want to stress that market participants have to be involved in the processes at an earlier stage than it is practiced by now. In our opinion it would be better to take market participants' needs on board at the beginning of a drafting process instead of launching consultations nearly at the end of the discussion process. Full disclosure of

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Recipient: ACER  
Trg Republike 3  
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Slovenia

TIWAG-  
Tiroler Wasserkraft AG  
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the ENTSO-E Technical Report and ACER's Market Monitoring Report should be understood in a non-discriminatory discussion process.

Particularly TSO-TSO models have major impact on market conditions and volumes, therefore an involvement of market participants in the development of models and particularly in the decision process is essential to establish a well-functioning electricity market.

All adequacy assessments and analysis of zonal market design have to respect that competition between market participants in a real level-playing field with harmonized rules in all member states will best guarantee adequate prices, efficient production, optimal collaboration between different production technologies across national borders, investment incentives and social welfare. Political and regulatory framework should focus on respecting all players and supporting cross-border cooperation on the way to the intended single European bidding zone.

The German/Austrian price zone is a highly successful example of the advantages of large bidding zones. Its wholesale market has developed more rapidly and is more mature than others which are lagging behind in tackling market barriers, liquidity and wholesale competition. The German/ Austrian large bidding zone was basis for the development of a regional market which now offers highest liquidity and most intensive competition. Splitting successful regional markets would contradict the objective of a unified, single electricity market. Hence, TSOs thinking should be supranational and a level playing field for market participants by merging bidding zones into even larger ones should be created.

A unified bidding zone offering a single wholesale price supports the necessary characteristics of a well-functioning electricity market whereas smaller bidding zones hinder fair competition and market integration. Moreover, the zonal market design is part of the European Target Model and enables liquid, robust and efficient wholesale markets. In contrast, the nodal market design might have theoretical merits but has failed in reality until now.

Existing technical, physical problems like loop-flows are best tackled by better cooperation of involved TSOs, enhancing grid infrastructure to remove bottlenecks, and redispatching. The charges for aforementioned remedial action described by ACER as being "costly" are only a fraction of costs for other measures. From our point of view, TSOs usually take only technical issues into consideration when urging for smaller bidding zones without taking other economic factors or opportunity costs for market participants into account, particularly a sufficient number of market participants, sufficient liquidity, hedging possibilities and level of competition. It's questionable if small gains in network efficiency can offset significant additional costs at other points.

Regarding loop-flows TIWAG opines that physical flows often diverge from commercial flows because the corresponding markets do not have the same degree of maturity, but there is a chance to develop the markets which are lagging behind. For example, physical flows are unrestricted between zones whereas commercial flows are hampered by different rules or additional charges. By harmonizing rules markets can be improved and trading can develop freely. Moreover, this might cure loop-flow problems more efficiently than just focusing on a limited technical scope with uncertain outcome.



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Liquidity still needs to improve all over the European electricity markets. Adequacy has been achieved so far only in the German/Austrian market. Hence, ACER's attempt to define liquidity solely as a characteristic of spot markets might be misleading and is rejected by TIWAG.

Regarding price hedging TIWAG remarks the fact that hedging is a precondition to offer stable prices to customers. There is no reasonable degree of forward hedging without fundamentally robust markets. This is underpinned by the fact that only larger price zones offer this option.

TIWAG disagrees with ACER's findings regarding market power. Competition is hampered by less market participants and therefore access for new entrants is more difficult in smaller bidding zones. Hence, implementing the European Target Model with regard to congestion management and capacity allocation is necessary to reduce market power.

TIWAG states that bidding zone reconfiguration is such a vital and far-reaching issue that market parties have to be institutionally involved in the discussion process but not only in a formal consultation process.

Again, TIWAG calls for an enlargement of bidding zones based on the success of the German/Austrian bidding zone and warns ACER against the political cost as well as against the loss of social welfare resulting from splitting successful existing bidding zones.

### 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 most effective measure for solving technical and economic issues should be taken into account. General welfare arguments usually taken into account by TSOs in the market coupling process is only considering the congestion rents (without cost for redispatching, which will often be needed since TSOs can't perfectly forecast all parameters) whereas other economic criteria are completely left out. As long as costs for redispatching are relatively low in comparison to the whole grid costs there is no need to change an existing bidding zone. By taking redispatching measures be it in one bidding zone or cross-border in several bidding zones TSOs can change loop-flows when necessary.

Regarding tradeoffs we are of the opinion that redispatching measures need more involvement and cooperation of TSOs, whereas introducing new bidding zones hinders market integration and market development.

TIWAG prefers investments in transmission infrastructure as the only long term measure to tackle loop-flows and congestions on a permanent basis. Since building new transmission lines takes as a rule a long time redispatching can be a measure in the meantime.



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TSOs should cover costs for redispatching via transmission tariffs. In turn, regulators should verify these costs and can therefore set incentives to build new transmission infrastructure. Obviously generators have to be fully compensated for their dispatching service.

**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?**

The existing bidding zone configuration led to several markets in Europe of which some have sufficient liquidity and others are clearly not liquid enough. Liquidity leads to efficient dispatching decisions and can fulfill load requirements adequately and economically. Liquidity is the prerequisite for trustworthy wholesale prices and therefore a guarantee for high numbers of participating bigger and smaller market players which in turn decreases market power.

TIWAG considers the German/Austrian price zone as adequately liquid. It can be proven that the churn rate for the aforementioned bidding zone is the highest in Europe. Consequently, moving on to larger bidding zones would increase liquidity further.

Further reduction of the size of bidding zones would lead to less competition, less liquidity, higher market concentration and in the end higher prices for end-users.

**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?**

Cross-border transmission infrastructure is used efficiently by the market as far as capacity is concerned that is offered by TSOs in auctions. Regarding calculations of capacity we see a lack of transparency, but there might be room for improvement like closer cooperation by TSOs. However, developments regarding the target model (flow-based capacity calculation and common European grid model) are promising. It has to be mentioned that flow-based market coupling has its merits due to a harmonized network model and closer cooperation of TSOs, though, and not due to the structure of the bidding zones.

We think that introducing flow-based market coupling should be done first. Experiences and results can then be analyzed and conclusions can be drawn upon. Market participants would need full transparency and disclosure of all factors in the flow-based calculation.

**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**

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**particular, does the bidding zones configuration limit cross-border capacity to be offered for allocation? Does this have an impact on you?**

Retail activities are impacted and restricted by the current structure insofar that portfolio management outside the German/Austrian bidding zone is highly complicated and can't be done in an overall approach for smaller players. Every bidding zone implies different or at least additional balancing regimes, maybe different RES regimes, different tax systems and so on. Actually, in our opinion cross-border capacity is limited by technical constraints rather than bidding zones. Consequently, TIWAG proposes the enlargement of existing zones to add additional economic benefits for market participants.

**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?**

By increasing the size of bidding zones market participants' own day-ahead and intraday necessary trading volume compared to the whole market would be smaller and therefore less risky to trade and hedge. Bid/ask spreads would be smaller and this would in turn increase liquidity. Regarding forward markets a less risky day-ahead market as the underlying product would add to liquidity.

If the size of bidding zones would be reduced bid/ask spreads due to the smaller number of market participants would increase and would in turn dampen liquidity in the spot markets. Hedging would be aggravated by a multitude of CfDs or transmission rights hence making the hedging process highly complex and costly. If on top of that bidding zones would be reconfigured on a regular basis this would create major issues for market participants for hedging.

Again, TIWAG is very much in favor of enlarging bidding zones to enhance liquidity.

**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?**

There are adequate possibilities to hedge in the German/Austrian bidding zone regarding products and terms up to 3 years. This is due to a robust, constant bidding zone size that has not been changed for many years.

In case of smaller bidding zones additional transaction costs would have to be taken into account, e.g. higher bid/ask spreads, hedging products to cover the basis risk between several bidding zones, and an increasing number of hedging products.

To ensure long-term (considerably longer than 3 years) hedging possibilities a firmer regulatory framework is needed. Consequently, the integrated European electricity market has to be aimed at.





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Pooling liquidity in bigger price zones would definitely help market participants to develop and offer new and longer term products which are now not liquid enough for efficient hedging.

**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?**

The current bidding zone configuration provides adequate price signals for investment in transmission lines. In the framework of the TYNDP the respective projects are included.

Redispatch and counter trading measures on a local level provide signals for either the reinforcement of specific lines or the investment in new transmission lines. The Austrian "Netzentwicklungsplan" lists specific examples.

Power plant investors need – in addition to a firm regulatory framework - particularly stability and reliability of bidding zones as investments are long-term oriented. Moreover, high liquidity and long-term hedging possibilities are needed to secure investments. Risk assessments would qualify smaller bidding zones and regular reshaping of bidding zones negatively.

TIWAG is of the opinion that current price levels are not that much influenced by bidding zones rather than RES generation which feed-in is not market-driven and compensation schemes are not harmonized.

**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?**

In the German/Austrian bidding zone we do not have any issues with market power. There is evidence that market concentration in the aforementioned bidding zone has even declined over the last years. In other zones it might help to merge them with others to create a uniform price level and therefore a level playing field and more competitors.

However, it is evident that any splitting of bidding zones would result in higher market concentration and market power, respectively.

**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?**

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In general, market participants should be included in the process from the beginning. ENTSO-E should take the positive economic effects of larger bidding zone configurations into account, e.g.

- Smaller bid/ask spreads
- Reduced transaction costs
- Higher competition
- Liquidity and availability of long-term hedging products

Redefining and splitting of bidding zones puts major burdens on market participants; they would have to renegotiate all contracts, probably bear significant losses, invest massively in IT systems, and adjust delivery points in all existing contracts. Any incurred cost has to be recovered from end customers via higher electricity prices. Hence, the political cost will be very high and might not be offset by uncertain and small gains in network efficiency. Consequently, TIWAG claims larger bidding zones.

**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 consider – from a European perspective – all market relevant issues and costs. Particularly a sufficient number of market participants to enable a sufficient degree of competition and liquidity (spot and forward) have to be the relevant criteria regarding bidding zones. System needs can most appropriately and efficiently be addressed by redispatching / countertrading (short-term) and net development (mid-/long-term) whereas splitting of bidding zones will definitely not solve loop-flows for instance.

Smaller bidding zones offer no solution quite the contrary; they would increase market concentration, reduce liquidity and hamper necessary investment in transmission network.

Only a stable political and regulatory framework supporting the intended single market by continuing or even enlarging the existing bidding zones will foster confidence of market participants and generate the necessary investments.

Thank you for taking our comments into consideration. If you have any further questions, please do not hesitate to contact us.

Yours sincerely,

