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Capacity allocation at the German-West Danish border

in the context of the ACER Recommendation 02/2016 on the common capacity calculation, and redispatching and countertrading cost sharing methodologies

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EFET Position Paper – 25 November 2016

Foreword

In its 2015 Market Monitoring Report published in September 2016, ACER notes that the cross-border transmission capacity availability at the German-West Danish (DK1) border has significantly deteriorated over the past few years. According to the ACER report, an average of only 13% of the total nominal capacity from West Denmark to German was made available to the market in 2015. This represents a decrease of more than 50% compared to the average values of 2014.

The German-West Danish interconnection is the interconnection in Europe with the second lowest ratio of available capacity allocated to the market compared to the nominal value of the transmission capacity at the bidding zone border.

The situation at the German-West Danish border echoes a general trend in the European Union, whereby interconnection capacity allocation remains widely suboptimal despite investment in transmission networks – including across borders – and improvement in capacity calculation methods. This problem can be observed at virtually all bidding zone borders in Europe, save mainly for merchant high voltage cable interconnections. EFET sincerely deplores this state of play and expects all involved parties – TSOs, regulators and governments as well as their representatives at the EU level and the Commission – to take action to remedy this problem.

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The main target: achieving a cost-efficient use of capacities through greater transparency – the ACER Recommendation

At the heart of the problem of the suboptimal allocation of cross-border transmission capacities in Europe lies a fundamental lack of transparency in the TSOs' capacity calculation process.

While allocation of cross-border transmission capacities at most bidding zone borders within Europe remains low, it is impossible for market participants and probably difficult for regulators and national governments themselves to assess the reality of the situation. The capacity calculation process run by TSOs remains fundamentally opaque, and we suspect TSOs to take excessively conservative assumptions that limit the transmission capacity made available to the market. Such behaviour means that TSOs choose to limit their own financial risk by avoiding remedial actions such as buying back capacity, redispatching or countertrading, when allocating more capacity and running the risk to have to take remedial actions could improve social welfare – on the two sides of the border and beyond. If TSOs were indeed taking such an unreasonably cautious approach to capacity allocation, they would step out of their role of neutral market facilitator.

Our suspicions, however, cannot be backed by evidence given the opaque nature of the capacity calculation process. Therefore, EFET supports the ACER Recommendation 02/2016 that aims to improve transparency in the capacity calculation process and hopefully increase allocated volumes at the European borders[1].

In its Recommendation, ACER proposes to reverse the approach to capacity calculation by requesting TSOs to not consider critical internal network elements or loop flows in their cross-border capacity allocation process anymore. This is intended to avoid that internal congestions or loop flows created by internal congestions are "shifted to the border" and *de facto* discriminating cross-border transactions compared to inter-bidding zone transactions.

TSOs would be allowed to request exemptions to this rule, provided that they prove to the concerned regulators that a reduction of available capacity compared to the interconnection's nominal capacity (taking the N-1 criteria into account) is the most cost efficient remedy to ensure system security or minimise negative effects on the internal electricity market. These principles would come with a polluter-pays rule, whereby the cost of remedial actions linked to internal or loop flows would be assigned to the TSO(s) of the bidding zone at the origin of the phenomenon.

[1] For additional details, see: http://www.acer.europa.eu/Official_documents/Acts_of_the_Agency/Recommendations/ACER%20Recommendation%2002-2016.pdf.

EFET welcomes the ACER Recommendation for a variety of reasons: First, it will force TSOs to reassess their current capacity calculation process and fully inform regulators – and as per ACER's plea, also market participants – of the elements that form part of it. Second, while reductions in allocated cross-border capacities may remain for some time, the approval process for exemptions to the main rule should guarantee that TSOs do not take excessive security margins to ensure the cost-efficient management of the network. Finally, the polluter-payer principle should ensure that appropriate market design reforms, remedial actions and/or network investment decisions are taken in the bidding zones that experience strong internal congestions and/or are at the origin of loop flows in neighbouring zones.

Should the TSOs, regulators and governments of Germany and Denmark be determined to use every megawatt of capacity available at the German-Danish West border in the most cost-efficient manner, they should strive for such a careful and transparent capacity calculation process, and fully implement the ACER Recommendation.

The pragmatic quick win: a regulated minimum allocated capacity – The Energinet DK proposal

The Danish and German government have initiated negotiations to remedy the low level of cross-border capacity at the German-West Danish border.

In this context, the Danish TSO Energinet DK published in September 2016 a proposal to amend the rules for capacity allocation at the concerned border[2]. We understand that the paper published by Energinet DK does not represent a consensus agreement between the different parties, and that discussions are still taking place between TSOs, regulators and Ministries on the two sides of the border.

The Energinet DK paper foresees that, pending any other improvements in the capacity calculation process or infrastructure investment, a minimum volume of capacity should be allocated to the market in any case, accompanied by countertrading from the TSOs when necessary. The Danish TSO links this proposal to a commitment expected from the German authorities to reinforce the internal German transmission network.

EFET welcomes the publication by Energinet DK, and more generally the fact that the German and Danish authorities, together with the concerned TSOs and regulators, have decided to tackle the problem. However, for cross-border questions of such importance, we would expect the discussion to take place openly, both in

[2] Energinet DK proposal for a capacity allocation model at the DK1-DE border, Document 16/06487-7, available in Danish at: http://www.energinet.dk/SiteCollectionDocuments/Danske%20dokumenter/El/Punkt%202_16-06487-7%20DK1-DE%20Modhandelsmodel%20Markedsarbejdsgruppemøde%20oktober%202016.pdf.

Denmark and Germany, and that market participants from the two countries and beyond be given the opportunity to contribute to the debate.

We believe that until full transparency and cost-efficiency justifications are provided in the capacity calculation process following the implementation of the ACER Recommendation, the Energinet DK proposal may be an acceptable, pragmatic first step.

Fixing a minimum capacity volume to be allocated at the German-West Danish border that will increase over time as grid reinforcements in Germany are finalised would allow an immediate improvement in available day-ahead capacity. However, we believe that capacity allocation in the forward timeframe should also be considered in the establishment of this minimum threshold.

Besides, the minimum capacity profile must be ambitious, significantly higher than the current average available capacities at this border and increasing over time. The capacity calculation process should also be sufficiently transparency to ensure that the minimum capacity profile does not become a default value when TSOs can actually allocate more capacity. Finally, appropriate rules need to be established in order to regularly review and possibly adjust the minimum threshold over time.

Conclusion

The suboptimal allocation of cross-border transmission capacities in Europe is holding the market behind. At best, it denotes an overly cautious approach of TSOs in managing European networks; at worst, it is a sign that TSOs, regulators and Member States still lack the willingness to complete the internal energy market that market participants need to ensure cost efficiency in the supply of electricity to consumers throughout Europe.

EFET expects regulators to take action and start implementing the ACER Recommendation as soon as possible. We would like to insist that implementing this reform of cross-border capacity calculation is a no-regret decision that should be taken whichever the bidding zone delineation currently is, or may be in the future: it is in essence is only a long-overdue application of Regulation 714/2009.

Well-designed quick wins that come hand in hand with greater transparency on the capacity calculation process and guarantee that more capacity is allocated at specific borders should also be welcome. They should not exonerate the concerned authorities to take steps to implement the ACER Recommendation.