POSITION

Subject: Elia study on the evolution towards a daily procurement of mFRR
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Introduction

On the 22nd of May, 2018 Elia published its 'Study on the evolution towards a daily procurement of mFRR'. Elia has invited all stakeholders to submit comments and suggestions by the 15th of June, 2018 at the latest.

FEBEG would like to thank Elia for publishing this study and for creating this opportunity for all stakeholders to express their comments and suggestions. The comments and suggestions of FEBEG are not confidential.

General evaluation

FEBEG supports the evolution towards a market facilitating flexibility offered by demand and renewables as these are necessary steps to shape the future energy landscape. However, FEBEG is concerned that the current proposal favors mFRR capacity offered by demand or renewable sources. This is a general trend FEBEG equally observes in other consultations (e.g. split procurement of FCR/aFRR) striving for a drastic reduction of the dependency of gas-fired power plants. This view is difficult to match with the 2050 study of Elia which considers gas-fired power plants as part of the answer for the increasing flexibility needs.

FEBEG welcomes the proposed evolution to phase out R3 flex and supports a standardized product (without a limitation to the number of activations) and with the inclusion of a day ahead 4 hour product.

Comments and suggestions

On the possible evolution towards daily procurement

An increase of the level of uncertainty and volatility on the future mFFR capacity market has a significant negative effect on any business case focusing on capacity from gas-fired power plants generating their main income from the mFRR market. The revenue basis for such power plants will become less stable and more unpredictable which might in time lead to closures or mothballing if other revenue streams would turn out to be insufficient.

FEBEG would like to understand why there is this clear push towards balancing services provided by capacities which are highly volatile. The ability of renewable sources to provide balancing services is weather driven while the provision of balancing services by demand facilities is process-driven and not at all the core-business of these demand facilities (as also indicated in the iCAROS). So, FEBEG fears that it will become increasingly difficult for Elia to contract sufficient volumes. Therefore FEBEG would like to understand how Elia will in the end ensure a market design that allows all sources of flexibility to participate while guaranteeing a healthy level of liquidity and competition.

It is correct to state that short term tendering might lead to lower risk premiums. But, for a unit which mainly supplies mFRR flexibility, the fixed costs still need to be covered within this market model. The shift to daily procurement could lead to much more volatile and uncertain capacity price levels which in the long term may have a paralyzing effect on capacity investments. Moreover, there could be an increase in capacity prices as market participants will need to distribute their fixed cost over a lower number of days, taking into account the risk of not being retained in future tenders. It is exactly for this reason that, for example, RTE in France continues to prefer yearly tenders above shorter term tenders for RR/RC.

Furthermore, the study proposes to contract the full volume of required mFRR balancing capacity in day ahead to allow Elia to contract or activate additional capacity in case of a lack of available capacity for the identified need. Although FEBEG considers it feasible to propose a short term market to meet the short term identified variable needs, FEBEG is not convinced that a solution where base load mFRR needs are contracted in a 'long term' market and variable needs identified in day ahead in a short term market, would be less economical. Examples in neighboring countries show that combining both is possible as such approach is used by Tennet in The Netherlands both for mFRR (quarterly/monthly tenders) as for aFRR (monthly/weekly tenders) which is not correctly represented in the Elia study. The choice for only one tender timeframe seems to be driven by sentiment rather than by any thorough analysis.

FEBEG also wants to point out that one could find arguments for the following approach: in a first stage the volume to contract is calculated on a monthly basis focusing on a base load need and in a second stage a daily assessment of additional flexibility – which should be contracted for the variable part – is organized. This variable part should allow for short term and time limited flexibility as well as for volatile renewables sources of flexibility to participate.

Stating that any split will lead to different markets with less dynamics and less competition makes sense when the products are inherently different (like R3standard and R3flex) but contracting in different timeframes (month/week and day) may still allow the required healthy competition whilst creating a sufficiently stable framework for mFRR capacity investments.

Committing flexibility for an entire month also ensures Elia to be able to contract sufficient capacity: it also allows to distribute the opportunity value over the entire month. On a short-term basis, the price might spike/peak in a few (4 hour) blocks due to a lack of capacity. Indeed, in case of significant tightness and shortage on the commodity markets, this is translated to the market opportunity component as perceived in day ahead. Therefore it is not unlikely that day ahead OTC deals will be preferred since a producer can capture the full 24 hours of value, whereas for the 6 x 4 hour blocks (with splits in max 10 MW steps) the outcome is uncertain and may lead to intermediate starts/stops to capture the full value of the underlying asset.

Since the units to which this arbitrage is applicable represent significant values to the mFRR Up market, this may lead to a significant reduction of the offered capacity. FEBEG trusts that Elia will take the responsibility to ensure the required mFRR up volumes in day ahead taking into account that certified assets may be committed in the day ahead OTC market or EPEX Belgium Day Ahead clearing. If one contracts for a full month or week, flexibility owners may be willing to accept limited time value on top of opportunity value as this guarantees locking a minimum value for the entire month. The same will apply in day ahead when arbitrating between OTC deals (Peak/Base) and the uncertain mFRR market.

Finally, FEBEG has some doubts with regard to the conclusions on the alignment with other reserve products. Firstly, FEBEG considers it interesting to assess how much of the current certified mFRR capacity can be offered on the FCR/aFRR market. Secondly, it is questionable that – in a model where all products (mFRR/aFRR/FCR) are tendered on a daily basis with a 30 minutes timeframe to re-optimize between two consecutive tenders – there will be possibilities to effectively re-optimize.

On the possible evolutions towards a standard mFRR balancing capacity product

In the study, it is indicated that there is increased level of quality which is correct if you consider the evolution from ICH to R3 flex. But overall, FEBEG is not sure if this statement still stands considering that the former contracted standard R3 could be activated without limitation (24hours) but is now limited to 8 hours per day. The example of the off shore storm effect shows that storms can last relatively long.

FEBEG would like to point out that in order to establish a healthy competition, one needs a healthy market structure whilst respecting the constraint of guaranteeing a certain capacity always being at the disposal to the grid operator in order to assure grid stability.

FEBEG would welcome a fall-back procedure in order to restore the reserve needs in case of congestions impacting large quantities of contracted mFRR or storms reducing capacity contracted on wind parks. If understood correctly, these events can only be predicted with sufficiently high level of certainty in intraday and only the potential risk can be identified in day ahead.

If the storm study would lead to additional internal reserve requirements for BRP's (see the proposal for the Federal Grid Code that refers to 'means'), this capacity will not be offered on the day/week/month ahead mFRR market. It is unclear how the different studies relate to each other: at this stage the studies and proposals as regards storm risk are creating uncertainty, also for investors.

On the impact of non-contracted mFRR (free bids)

Globally, FEBEG agrees with Elia's conclusion that making use of non-contracted bids should be done carefully. Moreover, FEBEG wishes to express its reserves upon the suggestion of Elia to take into account the offering of free bids in the dimensioning of the required mFRR capacity.

Free bids are driven by availability and are therefore not always guaranteed: it is difficult to see how Elia will be able to rely on flexibility of which the market participants themselves consider it is not reliable enough to offer in the capacity auctions.

The other way around: if Elia expects a large volume of free bids with high availability, these assets will also offer in the mFRR capacity auctions driving reservation prices down. In order to make the mFRR market sufficiently attractive and increase liquidity, Elia should guarantee a minimum volume it will procure, also when Elia is applying the dynamic dimensioning.

On the impact of reserve sharing

FEBEG questions if the availability of 99 % of the cross-border contracts – as mentioned in the study – is correctly taking into account the available ATC import capacity. If pre-reserving capacity on the ATC for reserve sharing would be considered – which FEBEG understands is not the case – cross-border capacity allocation should be subject to a co-optimization algorithm allowing to define the social welfare optimum between capacity for the flow based solution versus any balancing capacity contracting gains resulting from contracting reserve in neighboring countries.
