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Business Solutions

Formal public consultation on the CRM design notes (Part II)
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Centrica Business Solutions comments

October 30th, 2019

Summary of remarks

Derating factors

- CBS in principle supports Elia's concept regarding derating factors for energy limited technologies
- However, CBS can't fully support the methodology as long as the detailed derating factors associated with each aggregation category of the "SLA menu" are not defined
- CBS therefore asks Elia to consider the following improvements:
  1. Clarify the "SLA menu"
  2. Provide simulation results and use cases to better comprehend the proposed methodology
  3. Provide the possibility to combine several SLA levels within an aggregation of DPs in a CMU
  4. Clarify whether de-rating factors for availability and SLA levels are fix over the lifetime of a multi-year contract

Prequalification & monitoring

- CBS welcomes the fact that Elia considered stakeholder feedback and confirmed the ability of "self-derating" for energy constrained CMUs
- CBS believes the bank guarantee required for participation in T-4 should be function of the contract duration (i.e. lower than 20k€/MW for 1-year contracts)
- CBS asks Elia to clarify the applicable scheme for unproven Demand Response in T-4 and proposes sound principles to be applied to efficiently pre-monitor such MWs
- CBS believes metering requirements should be relaxed, to achieve a more efficient framework
- CBS asks Elia to clarify the fact the nominal reference power of a CMU is the sum of the individual nominal reference power of each delivery point
- CBS considers the overall role of DSOs in the CRM should be further considered, to avoid adding lengthy and complex procedures during prequalification

Auction process

- No remark

Payback obligation

- CBS advocates for a strike price level which ensures a fair market access to all technologies, fosters competition and lowers the overall cost of the CRM
- CBS asks Elia to enhance the methodology to calculate the single strike price for a given delivery year, by providing a two-step approach which guarantees an appropriate level for the strike price, as previously proposed by Elia

Secondary market

- CBS welcomes that Elia clarified the possibility for participants to realize ex-post secondary market deals.
- CBS asks to further assess the impact of the intermediate price cap in the market-wide option proposed by Elia for availability penalty applied to secondary market deals

Derating factors

While CBS in principle supports Elia's proposal regarding derating factors for energy limited technologies, CBS can't fully support the proposal as long as the detailed derating factors associated with each aggregation category of the "SLA menu" of the design note are not defined. Indeed, Elia does not yet provide concrete values for each SLA category at this stage of the consultation. The methodology presented in the design note to determine these derating factors is rather complex, and its possible outcomes are not presented and might be sensitive to the assumptions taken or the methodology itself. CBS therefore asks Elia to consider the following improvements:

CBS asks Elia to clarify the "SLA menu". The "SLA menu" proposed on page 22 of the design note points to a requirement based on 1 activation per day for the market response categories, but also sets a "NA" value for the SLA#6 category. CBS therefore asks Elia to clarify whether the 5 remaining SLAs #1 to #5 with a 1 activation per day value would be de-rated or not compared to the SLA #6 with no constraint.

CBS asks Elia to provide simulation results and use cases to better comprehend the proposed methodology. To better understand how the methodology works and how sensitive it is to assumptions, CBS believes that market parties would benefit from simulation results of derating factors for energy limited technologies under different scenarios. CBs invites Elia to provide some scenarios and use cases, illustrating what the potential de-rating values for each SLA could be depending on the inputs brought to the model used.

CBS asks Elia to consider the possibility to combine several SLA levels within an aggregation of DPs in a CMU. CBS believes that aggregation should be enabled in the CRM. However, as pointed out during the CRM Task Force, some design choices such as de-rating factors associated to SLA constraints can provide incentives to "dis-aggregate", i.e. push in the direction of offering CMUs with either individual delivery points (DPs), or at a smaller level of aggregation. This will allow to maximize the amount of MWs prequalified and offered to the CRM, reducing the overall costs of the mechanism. However, in the context of a CMU-based settlement, CBS points out that such "dis-aggregation" to cope with SLA constraints can expose CMUs to a risk of penalties, especially for availability tests. Therefore, CBS believes Elia should allow to combine several SLA levels within an aggregation of DPs in a CMU (for example through linked CMUs). This would allow to reflect the different SLA constraints of the DPs constituting an aggregated CMU, while ensuring these "sub-CMUs" are not considered isolated by Elia when performing availability tests. In that case, the CMU owner should be able to activate other "sub-CMUs" of the aggregated CMU to provide the requested volumes (as long of course as the aggregated CMU still complies with the aggregation rules associated to each DP).

CBS asks Elia to clarify whether de-rating factors for availability and SLA levels are fix over the lifetime of a multi-year contract.

Prequalification & monitoring

CBS welcomes that Elia considered stakeholder feedback regarding the "self de-rating" concept. This was a missing part of the initial design proposal and is now described in the design notes "Prequalification and Pre-delivery Monitoring" (Paragraph 3.6 Step 6), and "Auction Process" (Chapter 5).

CBS believes the bank guarantee required for participation in T-4 should be function of the contract duration, i.e. lower than 20k€/MW for 1-year contracts. While CBS supports the principle of a bank guarantee requested to take part in the T-4 auction, a 20k€/MW bank guarantee for existing or additional capacities eligible to 1-year contracts would represent a disproportionate share of the contract value, creating a barrier to participate to the T-4 auction. Indeed, depending on the level of the intermediate price cap, a 20k€/MW bank guarantee is likely to represent over 50% of the contract value, which is unreasonable. CBS therefore asks Elia to consider a bank guarantee in the T-4 auction which is function of the contract duration. This would achieve a fair balance, providing sufficient guarantees to Elia to avoid gaming in T-4 while remaining sufficiently reasonable to allow capacities eligible to 1-year contracts to participate to the auction without disproportionate financial risks.

CBS asks Elia to provide a clear framework for participation and pre-delivery monitoring of unproven Demand Response to the T-4 auction, i.e. DR volumes for which the underlying delivery points are not known at the time the auction takes place. Indeed, CBS considers that the 3 steps currently proposed in Elias design note are hardly applicable to DR (e.g. no permitting or start of works phase), and do not provide Elia with sufficient tools to monitor the progress made

in the development of unproven DR awarded in the T-4 auction before the delivery year. Considering the UK example, where the initial design of this monitoring comprised important loopholes, we believe Elia should further clarify this aspect of the design note, *i.e.* by adding a Scenario 5 describing the treatment of unproven DR in the T-4 auction. It is of utmost importance to define a design that will effectively allow unproven DR volumes to take part to the auctions in T-4, while providing Elia with sufficient guarantees on the progress achieved between the awarding and prequalification of MW. Indeed, taking part to a T-4 auction with DR volumes that are still to be proven, based on anticipated developments and a business plan that can be demonstrated to Elia can be of interest for DR providers: it will offer visibility on revenues ahead of time, increasing chance and time to secure DR volumes in the market in addition to the sole option offered by a participation in the T-1 auction. CBS proposes a concrete pre-monitoring process for unproven DR, which is further detailed in the box below. This process allows CRM candidates to offer volumes of unproven DR in the T-4 auction, to gain access to more volumes than if being limited to T-1, and to gain visibility on future revenues. To do so, the CRM candidate must deposit a bank guarantee to Elia just like other T-4 participants. When the time of T-1 auction comes, he must go through all the prequalification steps that other DR participants go through when entering T-1. The only difference being that Elia checks the progress made at that time, and if this progress is not demonstrated, part of the bank guarantee is seized.

CBS proposal for unproven Demand Response

- Unproven DR should be explicitly foreseen as an eligible category to take part to T-4 auctions
- The CMU owner needs to justify a valid business plan to explain how he intends to develop the proposed volumes of unproven DR
- Unproven DR bids should be subject to the bank guarantee required for the contract duration they apply for (no "free lunch")
- A specific pre-delivery monitoring for unproven DR should be implemented just prior to the T-1 auction based on the following intermediate milestone:

    1. The contract owner needs to present a letter of intention signed by a Delivery Point before the T-1 auction is launched by Elia and justifying the volumes sold are now linked to physical assets
    2. If Elia receives and accepts the letter of intention, part of the bank guarantee is released (25 or 50%, like for generation assets)
    3. If the letter of intention is not provided or refused, the contract owner either:
        a. releases the missing volume that can't be justified, gives up on 50% of the bank guarantee and its CRM remuneration, and allows Elia to procure the missing volumes in the T-1 auction
        b. keeps the volumes unchanged, gives up 25% of the bank guarantee because of the missed milestone, and gets ready to validate the prequalification before the start of delivery period to having Elia release the rest of its bank guarantee

CBS believes that accuracy requirements of meters used for the CRM should be relaxed compared to the ones applied in mFRR, as already pointed out in previous consultations. Especially in the cases where monitoring of available and activated MWs takes place at submeter level, the required accuracy standards often require costly investments that could be avoided. Indeed, most of the time the submeters in place allow for a very high level of accuracy (class 1 typically), limiting the loss of accuracy compared to the required 0.5 class, while enhancing by several orders of magnitude the accuracy of the baseline used to settle the activations. Therefore, CBS believe it is a win-win solution from a collective point of view to slightly relax accuracy requirements of the meters on one hand, in order to allow more MWs to enter in the CRM, and/or avoid increasing the costs of some MWs offered following an investment made in additional metering equipment.

CBS asks Elia to clarify the fact the nominal reference power of a CMU is the sum of the individual nominal reference power of each delivery point. CBS understands from the design note that a way to determine the maximum MWs (before de-rating) a given DP can engage in the CRM would be to look at the nominal reference power at delivery point level. For an aggregated CMU, CBS understands the nominal reference power would be the sum of the individual maximum powers of each DP, reflecting the maximum technical capacity of the CMU before de-rating, and leaving it to the CMU owner to assess how much of this power can be engaged in the CRM (after de-rating and use of the opt-out option to consider availability rate of the CMU).

CBS considers the overall role of DSOs in the CRM should be further considered, to avoid adding lengthy and complex procedures during prequalification. CBS notes that Elia proposes to copy/paste the framework that is used for FCR and

mFRR regarding the participation of DSO connected delivery points in the CRM and contests this approach. While CBS acknowledges that a framework should be foreseen to avoid such capacities creating additional constraints on the distribution grids, we believe the "burden of proof" should be inversed, as the process has proven to be lengthy and overly complex in FCR and mFRR. When adding a DP connected at DSO level, it should be up to the DSO to demonstrate a risk of constraint once the DP is accepted, rather than requesting a prior agreement following an NFS study before being allowed to add a DP to a CMU. CBS believes this would avoid unnecessary delays and avoid risks to hamper participation of DSO connected DP to the CRM. Also, such a process should also be assessed to be extended to ancillary services.

Auction process

CBS has no particular remark on this design note at this stage.

Payback obligation

CBS advocates for a strike price level which ensures a fair market access to all technologies, fosters competition and lowers the overall cost of the CRM. As pointed out in previous consultation responses, CBS understands the choice of a single strike price has to achieve a fair balance, ensuring on hand an efficient payback mechanism, while on the other hand not discriminating certain technologies and distort the CRM in a way that would lead to higher costs to. Since not all technologies with high marginal costs can be captured by a single strike price, CBS advocates for a price level which at least covers the effective marginal costs of the most relevant technologies, including industrial demand response processes. Elias final proposal should therefore:

- limit the share of eligible technologies that will be exposed to undue payback, and potentially totally excluded from the CRM (in particular DSR)
- ensure a fair market access to a broad base of technologies, without having to reimburse revenues not perceived on the energy market
- foster competition and therefore lowers the overall cost of the CRM

CBS asks Elia to enhance the methodology to calculate the single strike price for a given delivery year, by providing a two-step approach which guarantees an appropriate level for the strike price, as previously proposed by Elia. While CBS in principle supports the proposed approach, which has the merit of taking historical market data on elastic volumes from the day-ahead market, it still remains a proxy which does not faithfully reflect the volumes of market response available for a given delivery year. Indeed, as ToE for DA has not yet been implemented, it will take a certain time before all relevant market response volumes can be brought to the market and be reflected in the curves of the DAM exchange. Furthermore, the proposal takes the assumption of perfect economical rational behavior and omits strategic bidding behavior whereby especially during market stress situations suppliers do not necessarily have the incentive to integrate their market response volumes in the DAM offer and demand curves at the price at which the client offered them. Finally, the fact that Elia proposed to exclude certain bids (and in particular block, linked, and simple block bids), could lead to a misleading assessment of the market response volume reached for each strike price value. This is particularly true for Demand Response, which by definition will only represent a limited volume of the overall DAM volumes, and will likely make use of more complex orders than generation assets.

The current proposal of Elia provides no floor nor cap on the possible strike price, exposing the market to a risk of determining for a given delivery year an inappropriate level of the strike price. This could expose certain MWs to undue payback, and possibly even completely exclude certain technologies from the CRM (i.e. technologies which are unable to reflect costs related to undue payback obligation by increasing their bids, for example because of the price cap). This risk is due to the fact that the methodology presented in the design note does not propose a minimal value for the strike price, which is a change compared to the previous discussions, where the different proposals tabled by Elia were foreseeing price range with a floor at 500€/MWh.

Similar to the proposal made by Elia to first go for a pay-as-bid mechanism, and in a second phase only to shift to pay-as-clear, CBS believes the first years of the CRM should come with additional guarantees on the determination of the strike price, to ensure it does not lead to a level which would exclude from the market competitive and useful volumes contributing to the security of supply in Belgium.

CBS therefore asks Elia to amend the proposed methodology in order to render it watertight once it will be used by the authorities to determine the yearly strike price value:

- Step 1: define a range with a clearly defined floor for the strike price (e.g. 500-800€/MWh previously proposed by Elia), taking into account the intrinsic limitations of the proposed methodology described above (time for DAM orders to reflect full elasticity of offer and demand, reflect orders that have been excluded, etc.)
- Step 2: within the range defined in Step 1, determine the value of the strike price based on Elia's current proposal

In addition, Elia should assess the "score" of the DAM curves used to pick the relevant strike price, to monitor when it becomes good enough to drop the floor and got to a full market value. Elia should also assess the risk of cost increase (e.g. MWs being excluded of the CRM because of the price caps) linked to the different levels of strike price that could be chosen, to allow for an overall more efficient decision to be taken while setting the strike price each year.

Secondary market

CBS welcomes the fact that Elia clarified the possibility for participants to realize ex-post secondary market deals. CBS points out that a well-functioning and liquid enough secondary market will be a key feature of the Belgian CRM, as number of key design elements rely on it. CBS also supports the model proposed by Elia based on the transfer of obligation: this model is likely to be simpler to be implement and more efficient, therefore more likely to allow for a secondary market to happen.

CBS asks to further assess the impact of the intermediate price cap in the market-wide option proposed by Elia for availability penalty applied to secondary market deals. CBS points out to Elia that regarding the availability penalties applied following a secondary market transaction, the "market-wide contracted price" option proposed by Elia comes with a risk with regards to the existence of the intermediate price cap in the auction clearing. Because of this price cap, not all CMUs will be eligible to the same level of remuneration in the market: some of them will be limited to the intermediate price cap while others will be eligible to a higher cap. Therefore, looking at the market price coming out of the auctions as a basis for penalties following a secondary market deal creates a risk is the CMU taking over the obligation does not have the same remuneration at all from the auction (because of the price cap) than the CMU selling the obligation. CBS believes that Elia should further analyze the potential impacts and distortions the intermediate price cap can introduce before considering the market-wide approach is the best option to apply for the availability penalty scheme that will be chosen for the secondary market transactions in the end.

Annexes

- Centrica Business Solutions comments to Elia following the first round of design notes, 3rd September 2019
- Centrica Business Solutions comments regarding ELIAs Strike Price proposal, 12th September 2019