

ACER Coordination Group for Electricity Regional Initiatives

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Progress report from the 8th Region prepared by ERCB



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1 Main Insights

The 8th ERI Region is characterised by significant heterogeneity in both its market and regulatory set-up. The largest obstacle for the integration of electricity markets in this region is that its legal basis lacks harmonisation and implementation. Effective market opening is hindered by a number of legislative provisions in some countries, in particular related to public supply, single buyer models, regulated energy prices, market based procurement and trade of electricity and monopoly positions in electricity generation and supply. At the same time, additional commitment from various actors in the region is deemed to be a necessary precondition for further improvements. The differing timelines for implementation of the respective requirements¹ add to the challenges necessary to be overcome in order to promote market opening, integration and functioning in large parts of the region. A central element for promoting the creation of a regional market, together with the final prospect of forming part of the IEM in a consecutive step, is the *Regional Action Plan for Wholesale Market Opening in South East Europe* ((SEE RAP)². The SEE RAP has been developed in line with the elements of the European Electricity Target Model. Table 1 provides an overview of the progress made in the elements of the RAP, in line with the descriptions of the respective chapters below. As compared to the 2014 target of finalising the EU's IEM, the target for the 8th Region is 2015.

RAP element	Meeting the intermediary RAP deadlines	Prospects of meeting the 2015 deadline	Progress achieved / pending issues ³
Capacity Calculation	Partly	unclear	Grid Model updated & LT Coordinated Capacity Calculation in place
Forward Markets	No	likely	With the establishment of the SEE CAO progressing, it becomes likely that coordinated LT allocations can take place in the near future; still, the relations between SEE CAO participating and non participating TSOs in the region need further clarification. The development of the SEE CAO Auction Rules are a significant step forward.
Day-ahead Market	No	¹ announced	The establishment of Power Exchanges was announced for Serbia and Croatia, but real progress was not achieved. The Serbian power exchange was announced to become operational end of 2014. In Macedonia, discussions on the possibilities for establishing a power exchange started, too.
Intraday Market	No	unlikely	No measurable progress achieved
Abandoning of Barriers in National Legislation	To be abolished as part of the legislative reviews to implement the Third Energy Package with deadline of 1 January 2015		In the Region's EU member states and some of the Energy Community's Contracting Parties appropriate measures and market rules have been transposed. Regarding the implementation more detailed setting and application of rules in a coordinated manner is required.

Table 1: Overview of the developments regarding the elements of the 8th Region's Regional Action Plan

¹ The countries forming the region are Contracting Parties of the Energy Community and Member States of the European Union. This results in a two-speed market development, due to the additional time for transposition, and hence implementation, granted to the formerly mentioned.

² <http://www.energy-community.org/pls/portal/docs/1810178.PDF>. The SEE RAP has been jointly developed by the Energy Community Regulatory Board and ENTSO-E RG SEE and received support of the Ministerial Council of the Energy Community. Ukraine has postponed the decision on approval of the RAP till the Study on Ukraine and Moldova energy systems synchronizing conditions with ENTSO-E is finished. It is expected that the Study could be finished not earlier than 2015.

³ For reasons of readability, the pending issues are not displayed here. Please consult the RAP for a detailed overview of the activities and deadlines foreseen, here: <http://www.energy-community.org/pls/portal/docs/1114181.PDF>

2 The 8th Region

The 8th Region⁴ covers the Energy Community⁵ Contracting Parties⁶ and the seven neighbouring EU Member States⁷.

3 Context

On EU level, the entry into force of the Third Energy Package together with the target of completing the internal energy market by 2014 form the framework for electricity market development. The Third Energy Package was incorporated in the Energy Community in October 2011⁸ with a transposition deadline by 1 January 2015 the latest. This also includes adopting the European Network Codes, once legally binding on European level⁹, in the Energy Community.

The goal of integrating the seven European electricity regions into a single market area is addressed through the *Regional Initiatives* process which falls under ACER's responsibility and focuses on four cross-regional roadmaps¹⁰:

- Capacity calculation
- Long term capacity allocation
- DA capacity allocation (Market coupling)
- Continuous mechanisms for implicit cross border intraday trading

The 8th Region participates in ACER's coordination activity. The SEE RAP defines the steps for regional market integration in the 8th Region streamlined with the milestones and actions of the European *Electricity Target Model* and the four cross-regional roadmaps. The objective of this Quarterly Report is to monitor progress in the implementation of the different roadmaps and to ensure that any obstacle is well identified and tackled in the most effective and efficient way.

⁴ The 8th Region was established following a decision by the Ministerial Council of the Energy Community on 27 June 2008 with a view to implement a common procedure for electricity congestion management and transmission capacity allocation on regional level.

⁵ www.energy-community.org

⁶ Albania, Bosnia and Herzegovina, Croatia, Former Yugoslav Republic of Macedonia, Kosovo* , Moldova, Montenegro, Serbia and Ukraine. [* *This designation is without prejudice to positions on status, and is in line with UNSCR 1244 and the ICJ Opinion on the Kosovo declaration of independence*]

⁷ Bulgaria, Croatia, Greece, Italy (limited to its interconnections with Contracting Parties), Hungary, Romania and Slovenia.

⁸ **Decision 2011/02/MC-EnC of the Ministerial Council of 6 October 2011.** Ukraine has abstained from approval of the decision until the internal state procedures of ratification are performed.

⁹ Network Codes will, finally, have the form of a directly binding Regulation. Different from the European Union, European Regulations do not develop direct applicability in the Energy Community but need to be transposed into national legislation. The Energy Community Council by Decision 2011/02/MC-EnC empowered the Energy Community Permanent High Level Group (PHLG) to decide on the applicability of the European Network Codes and Guidelines in the Energy Community. The PHLG has defined its procedures by Procedural Act 2012/01-EnC (<http://www.energy-community.org/pls/portal/docs/1636177.PDF>).

¹⁰ According to the **EU Energy Work Plan for 2011-2014 in Electricity**.

4 Review of progress with implementation in each of the cross-regional projects

4.1 Implementation of a single price market coupling model

4.1.1 Description of the project

Mirroring the European approach, the target model for the day-ahead timeframe in the Energy Community is a single Price Coupling (PC) model which simultaneously determines volumes and prices in all relevant zones, based on the marginal pricing principle. Among the different elements of PC, one of the most important is the choice of a single algorithm that optimises the value of admissible wholesale market trades both within and across bidding zones. At the same time TSOs' requirements in terms of operational network constraints have to be taken into account in order to ensure efficient and feasible allocation results.

4.1.2 Key milestones and accountabilities

The SEE RAP foresaw enhancing the common grid model for SEE and harmonising of the methodologies and procedures for the calculation of yearly, monthly, and day-ahead capacities by the end of 2011. Responsibility for these tasks rested with the region's TSOs via the ENTSO-E Regional Group SEE.

Implementation of PC in the 8th Region entails a step-wise approach. Initially, the starting point for PC was foreseen to establish bilateral or trilateral market coupling by mid 2013 following a nucleus approach. Alternatively different initiatives merging into a single regional PC model by end of 2014 were envisaged. The RAP's scope was then the integration of the then regional PC with the European PC zone by mid 2015. Delays in terms of implementation in the 8th region, but also within other ERI regions, outdated these prospects. The European Commission's delay in developing the Governance Guidelines and the consequent delay in tabling a consolidated proposal for the CACM Network Code exacerbate the outlook for implementing a European Single Price Coupling solution by the end of 2014.

As crucial element of this process, the SEE RAP foresees the establishment of power exchanges (PX) or contracting services from existing PXs by end of 2012. This initial implementation date was not fulfilled. An update of the SEE RAP is envisaged.

4.1.3 Review of progress during this quarter

Concrete progress has not been made; neither related to the development of a single capacity calculation algorithm, nor in relation the introduction of PC and the establishment of PXs or contracting services from existing PXs.

However, developments have been announced in the course of 2013:

- TSOs reported that progress has been made within the ENTSO-E Regional Group SEE on discussing a harmonised capacity calculation algorithm
- The 18th Energy Community Electricity Forum supported the announcement of a Serbian SEEPEX as possible pilot project for development of market coupling across the Region that can be extended to other Contracting Parties¹¹ on a step by step basis. Other comparable initiatives have been started in Croatia and Macedonia with the aim of establishing a PX or entering into joint venture agreements.

The latest endeavours to establish power exchanges in some countries provide a move into the right direction towards the development of spot markets and the provision of a condition for future implicit allocations.

¹¹ Specific arrangements may need to be found for Moldova and Ukraine.

4.1.4 Action needed to overcome the identified constraint(s)

It has to be underlined that all elements of the SEE RAP can be implemented within the legal framework of the 2nd Energy Package. Necessary adjustments in national legislation, preparing the ground for regional implementation, have already been made. Lack of *concrete* progress is even more disappointing in this context. Certainly, stronger political support, promotion and commitment are necessary to proceed.

Effective market opening is also hindered by a number of legislative provisions in the Contracting Parties that need to be abolished, in particular related to public supply, single buyer models, regulated energy prices, market based procurement and trade of electricity and monopoly positions in electricity generation and supply.

Other requirements for the implementation of a PC in the 8th region are the establishment of PX functionalities in each bidding zone, the determination of Coordinated Capacity Calculator responsibilities and the development of attached methodologies, amongst other things for the distribution of congestion income or capacity calculation.

4.2 Implementation of a cross-border continuous intraday trading system across the 8th Region

Although being already required under the 2nd EU Energy Package, the introduction of a specific cross-border continuous intraday trading system at all borders of the 8th region has not started yet.

4.3 Improvement and harmonisation of the allocation and nomination rules for long and medium-term transmission rights

4.3.1 Description of the project

The SEE RAP provisions on the harmonisation of the allocation and nomination rules for long and medium-term transmission rights is streamlined with the related European cross-regional roadmap. The objective is to give market participants an opportunity to hedge themselves against day-ahead price differences, in a manner compatible with zone delimitation, through one single access point and a harmonised set of rules for long-term transmission rights, where financial markets do not enable them to do so in an efficient manner.

The still existing lack of a regionally coordinated capacity allocation mechanisms remains a key concern, both in terms of market liquidity as well as compliance with the Energy Community *acquis communautaire*. Insufficient transmission interconnection capacity with neighbouring systems remains a key barrier for limited cross-border trading and the establishment of a regional electricity market. Coordinated capacity allocation and congestion management schemes are therefore essential. Although the TSOs of all Energy Community Contracting Parties, except Moldova¹², have already introduced market-based capacity allocation mechanisms (based on NTC auctions) for congestion management at their borders, there is still insufficient harmonization in the 8th Region.

¹² With regard to the Republic of Moldova, the draft regulation transposing Regulation (EC) 1223/2008 has been finalised with further amendments; approval is, however, pending and subject to adjustments in primary legislation.

4.3.2 Key milestones and accountabilities

The SEE RAP foresaw a step-wise approach starting from centralized and multilaterally coordinated (NTC based in a first step but flow based remaining the final concept) auctions on relevant SEE borders performed by a Coordinated Auction Office as single point of contact in SEE by end of 2012. This initial implementation date was not fulfilled. An update of the SEE RAP is envisaged. The SEE RAP schedules the final target of multilateral coordinated auctions on all SEE borders as regional one-stop-solution for end of 2014. The development of the Draft Auction Rules of the SEE CAO and the coordinated approach regarding their future approval give promising signals for the successful harmonisation of the largest parts of the Region's allocation of forward capacities, if not for the entire Region.

4.3.3 Review of progress (during this quarter)

SEE Coordinated Auction Office

The establishment of a SEE Coordinated Auction Office (SEE CAO) targets harmonisation of the allocation and nomination rules for long and medium term transmission rights in the 8th Region. The SEE CAO is envisaged to perform coordinated NTC-based capacity allocation as first step and, finally, switch to flow based capacity auctioning. The Energy Community Ministerial Council in December 2008 supported the location of the Coordinated Auction Office in Montenegro.

The so-called *Project Team Company in Charge of Establishing a SEE CAO* (PTC)¹³ has been officially registered in Montenegro on 4 July 2012 with the scope of preparing the effective operation of the SEE CAO. The network operators of Albania, Bosnia and Herzegovina, Croatia, FYR of Macedonia, Greece, Kosovo*¹⁴, Montenegro, Romania, Slovenia and Turkey are shareholders of the PTC. The Company is co-funded by the individual shareholders and significant contributions from International Financing Institutions¹⁵.

The work of the PTC is considered to be finalised by the 10 December 2013. The Board of Directors of the SEE CAO agreed on the termination of the PTC and set the course for the establishment of the factual SEE CAO with the call for applications for an executive director. The SEE CAO is expected to take up its work in the first quarter of 2014, aiming to perform auctions of monthly and daily capacities for the second half of 2014. This constitutes an initial step towards centrally coordinated forward capacity allocation for the entire 8th Region. The SEE CAO is expected to start operation in early 2014.

A significant step forward has been made by the submission of the SEE CAO Auction Rules of the participating TSOs to their NRAs for approval. The Region's NRAs have coordinated their approach in approving the Auction Rules through the ECRB by adopting a common position on the procedure and conditions for approval.¹⁶

4.3.4 Action needed to overcome the identified constraint(s)

It has to be underlined that all elements of the SEE RAP can be implemented within the legal framework of the 2nd Energy Package. The establishment of a regionally coordinated congestion management is explicitly required by Regulation (EC) 1228/2003. However, stronger political support, promotion and commitment are necessary to proceed.

At the 18th Energy Community Electricity Forum the Serbian TSO, EMS, declared readiness to enter into joint bilateral auctions, as a first step, with the SEE CAO; concrete steps in this direction have not been

¹³ www.seecao.com

¹⁴ This designation is without prejudice to positions on status, and is in line with UNSCR 1244 and the ICJ Opinion on the Kosovo declaration of independence.

¹⁵ EBRD, KfD and USAID.

¹⁶ <http://www.energy-community.org/pls/portal/docs/2716178.PDF>

accomplished yet and also the detailed rules for such agreement are not discussed so far. Commitment by the Bulgarian system operator is still missing.

4.4 Implementation of fully coordinated capacity calculation methodologies and particularly the flow-based allocation method in highly meshed networks¹⁷

4.4.1 Description of the project

Following the implementation of a coordinated NTC allocation mechanism, the implementation of a flow-based (FB) capacity calculation and allocation method within the SEE CAO remains the final target with a view to improve:

- Economic signals: for planning transmission network expansions (TSOs) and location of the new power plants/large consumption units (market participants),
- System security: the better identification of critical transmission network conditions on the regional level.

Prior to switching to the FB method, the following requirements are to be fulfilled:

- Full coordination of principles and data;
- No negative impact of the FB method on system security;
- Increased social welfare brought about by the application of the FB method;
- Sufficient time provided for market participants to adapt to the new method;
- Work on and implementation of FB capacity calculation and market coupling need to be closely coordinated.

4.4.2 Key milestones and accountabilities foreseen in the initial cross-regional roadmap

No concrete milestones for the implementation of the flow-based allocation have been defined so far. Still, the implementation of a flow based mechanism has been identified as final target.

4.4.3 Review of progress during this quarter

No concrete steps have been taken.

4.4.4 Action needed to overcome the identified constraint(s)

Concrete milestones for the implementation of FB allocations need to be defined.

¹⁷ The ACER cross-regional roadmap for the Flow-Based Capacity Calculation Method for short-term capacity allocation is available at: http://www.acer.europa.eu/Electricity/Regional_initiatives/Cross_Regional_Roadmaps/Pages/Capacity-Calculation.aspx.

5 Review of progress with implementation in other important areas

Transmission development plans

Since the 8th Region's national transmission grids are relatively small, regional transmission network planning is of utmost importance. Thus SEE TSOs are actively participating in the relevant ENTSO-E working groups. In addition, the SECI transmission planning project provides a platform for the TSOs exchanging information about ongoing transmission projects. SEE TSOs are actively contributing to the development of the ENTSO-E Ten Years Network Development Plan, thus involving SEE transmission grid in the pan-European context. In line with the EU's new guidelines for trans-European energy networks, a process has been launched to identify, coordinate and facilitate Projects of Energy Community Interest (PECI)¹⁸. In this context, a milestone was reached with the Energy Community Permanent High Level Group's (PHLG) endorsement of those projects eligible for assistance and those of high priority amongst these. A list of regulatory investment incentives relevant for these projects was additionally recommended for adoption by the upcoming Ministerial Council. The PECI process contributes to the efficient development of the 8th region's transmission grid in a coordinated manner.

In October 2012, Energy Community Ministerial Council adopted Renewable Energy Directive 2009/28/EC and agreed to binding RES targets for the Contracting Parties in 2020. By 30 June 2013, the Contracting Parties had the obligation to submit National Renewable Action Plans describing the RES policy objectives on how to reach the 2020 RES targets. Part of the requirements for implementation of the RES Directive is also the development of the transmission and distribution grids to increase the uptake of renewable energy and within the TYNDP the 2020 RES objectives for the Contracting Parties will have to be reflected adequately.

Until 30 June 2013, only Serbia submitted the NREAP adopted by the Government and in the upcoming period more Contracting Parties will have it adopted and submitted for publication providing the scope for TYNDP reviewing.

Development of cross-border balancing

During a Joint ENTSO-E & Energy Community Workshop on 3rd Package Network Codes, held in Vienna on 4 November 2013, representatives of the Energy Community Regulatory Board's (ECRB) Electricity Working Group (EWG), ENTSO-E's Regional Group Southeast Europe (RG SEE), and the Energy Community Secretariat endorsed the launching of an Initiative aiming to develop a Regional Balancing Concept for the establishing of a Balancing Market in the 8th Region. In the beginning of 2014, the Terms of Reference of this project will be discussed, and with it a timeframe and the work packages it will contain.

Transparency

In order to increase market transparency most of the SEE TSOs are participating in the ENTSO-E transparency web platform.

Although, the quality of the SEE TSOs websites has increased, none of the CPs TSOs is in full compliance with the legal transparency obligations.

¹⁸ For details on the PECI process, please consult:
http://www.energy-community.org/portal/page/portal/ENC_HOME/AREAS_OF_WORK/Regional_Energy_Strategy/PECIs

The ECRB has adopted a recommendation on the adoption of Regulation 543/2013 on submission and publication of data in electricity markets in the Energy Community. Such recommendation is not binding, but endorses the endeavours of the 8th Region's TSOs and market participants to promote transparency and market development.

Management and use of interconnections

As regards the management and use of interconnections, harmonization of the applied cross border capacity allocation mechanisms has been reached; the marginal price mechanism prevails in the region.

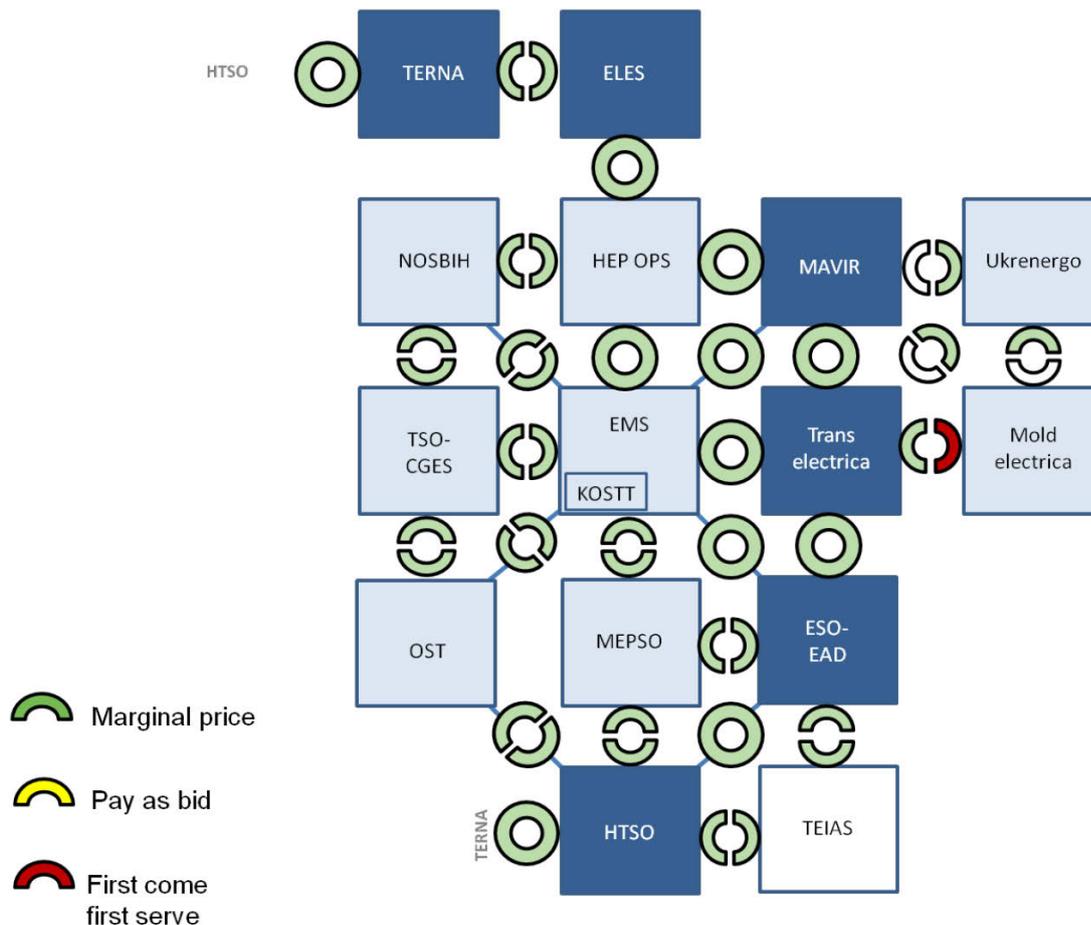


Figure 1: Mechanisms for Capacity Price determination in the 8th Region^{19, 20}

Joint auctions

All Contracting Parties' TSOs, except the TSO of Moldova²¹, have introduced market-based mechanisms for cross-border auctions, namely explicit NTC-based auctions. Auction rules for cross border capacity allocation for the borders of Ukraine have been adopted by the national regulator already in 2009 which Energy Community Secretariat assessed these Auction Rules in 2012 as being not in compliance with the Energy Community acquis. Yearly and monthly allocations are introduced at all electricity borders while

¹⁹ Please note that according to current Ukrainian Electricity Law only unilateral auctions (for export) are allowed.

²⁰ Currently, auctions for interconnection capacity allocation between Ukraine and Republic of Moldova are organized only by Ukrainian TSO.

²¹ With regard to the Republic of Moldova, the draft regulation transposing Regulation (EC) 1223/2008 has been finalised with further amendments; approval is, however, pending and subject to adjustments in primary legislation.

weekly and daily allocations are introduced only at several borders. Intraday allocations are also available at several borders, but on non-market based solution (first come, first served).

Besides the EU member states in the 8th Region also several Contracting Parties TSOs have started to implement joint auctions (see figure 3): the TSOs of Serbia and Croatia started implementing joint auctions with their neighbouring TSOs.²² As of January 2013, Serbia and Romania jointly organize coordinated auctions for long and short term allocation of their cross border capacities.

For 2013 the Croatian borders to Slovenia and Hungary are for the first time involved in CEE Coordinated Auction Office (yearly, monthly and daily auctions).

Romania has declared interest on joining the market coupling mechanism between Czech Republic, Slovakia and Hungary; steps have been made in declaring the common willingness for cooperation and mutual approach in this respect of all involved parties.

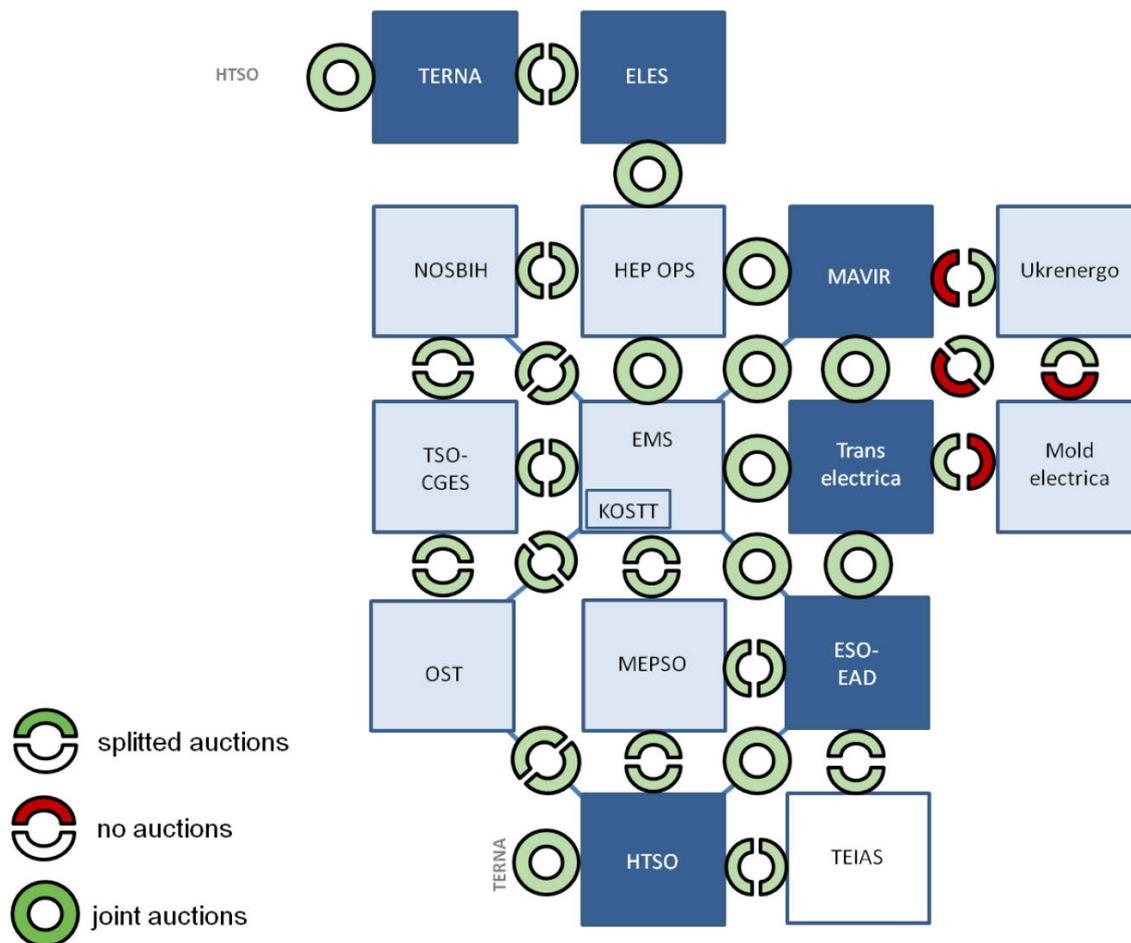


Figure 2: Cross Border Capacity Allocation Mechanisms in the 8th Region ²³

²² Joint auctions with between Croatia and Hungary started already in 2010 (yearly, monthly and daily auctions). The joint auctions between Croatia and Slovenia started in 2011 (yearly, monthly and daily auctions). EMS (Serbia) started joint auctions with Transelectrica (Romania) on 1 January 2013. Joint auctions between Serbia and Hungary started for 2012 in Dec 2011 on yearly, monthly, daily and intra-day level. Joint Auctions between Serbia and Bulgaria and between Croatia and Serbia are held from 2014.

²³ Currently, auctions for interconnection capacity allocation between Ukraine and Republic of Moldova are organized only by the Ukrainian TSO.