

Value flexibility through markets - EPEX SPOT considerations for further improving the new European Network Code on Demand Response

Executive Summary of the EPEX SPOT response of 31 October 2024 to the public consultation of ACER on the Demand Response Network Code proposal of 5 September 2024

Key Recommendations for further improving the Network Code on Demand Response

1. Set strong **incentives to system operators** to engage in market-based flexibility procurement.
2. Keep clear and strong promotion of **market-based flexibility procurement** of congestion management services by system operators over cost-based or regulated price setting approaches.
3. **Ensure multi-market access** for flexibility service providers across wholesale, flexibility and balancing markets while **avoiding combined markets with forwarding of bids**.
4. Reintroduce **requirements for local market operation**, including neutrality and transparency, proven expertise and resources, highest market surveillance standards
5. Foster **DSO-TSO coordination** to solve congestions in the most efficient ways.

Flexibility is a key pillar for a successful energy transition. EPEX SPOT is the leading power spot exchange in Europe, empowering communities to achieve a competitive and climate neutral Europe. We are pioneer in the development of local flexibility markets. Local flexibility markets can tackle grid congestions, reduce grid expansion costs and unlock the full potential of demand-side flexibility.

The European Network Code on Demand Response will create the European regulatory framework for local flexibility markets. The regulation is of high importance to unlock the full potential of demand response to deal with the huge increase of renewables and to ensure a safe, affordable and clean electricity supply. Based on our strong experiences in developing and operating energy markets, we identified five key areas for further improving the Network Code on Demand Response to ensure that the Network Code becomes a successful hour of birth for local flexibility markets in Europe.

1. **Set strong incentives to system operators to engage in market-based flexibility procurement (Art. 17)**

The lack of incentives for TSOs and DSOs to consider non-wire alternatives is an important barrier for demand response and for the use of market-based congestion management. In order to set strong incentives to system operators to engage in market-based flexibility procurement, costs for market-based flexibility procurement shall be recognized/ recovered.

This can be achieved for example by moving from a CAPEX dominated approach rewarding in particular new grid infrastructure to a TOTEX approach that also takes into account non-wire alternatives. The CAPEX-focused approach, which favours infrastructure solutions, should be further developed and supplemented to include short-term operating costs to a greater extent. In this way, an economically efficient balance between long-term grid investments and short-term operating costs (proactive grid management, flexibility utilisation) can be achieved for the benefit of end consumers. In the UK, for example, the TOTEX approach of the RIIO-1 scheme (RIIO: Revenue = Incentives + Innovation + Outputs) has successfully helped grid operators to utilise

market-based solutions for congestion management in addition to grid expansion, thereby saving grid expansion costs.

In addition, System operators should be enabled to participate in projects for the market-based procurement of flexibility for congestion management with "sandbox regulations", i.e. by granting exceptions to the current purely cost-based redispatch in these cases. Sandbox regulations can be used to further test suitable solutions. The approach of the Sinteg project "enera" of a local flexibility market in Northern Germany from 2017-2020, for example, was the right approach. Here the regulatory framework of sandbox regulation has made it possible to demonstrate the use of a local market for flexibility for congestion management. The enera project provided important insights for further development and was a technical success, as the project showed that local flexibility markets for congestion management are technically possible and work.

For these reasons, we welcome that Art. 17 of the ACER proposal of 5 September 2024 stipulates that the costs borne by the relevant system operators stemming from the Network Code on Demand Response shall be recovered through the network tariffs or other appropriate mechanisms.

2. Keep clear and strong promotion of market-based flexibility procurement of congestion management services by system operators over cost-based or regulated price setting approaches (Art. 38, Art. 39)

The market-based flexibility procurement for congestion management can in many cases be more efficient than cost-based or regulated price setting method. It allows to select the least expensive flexibility sources matching the need of the procuring TSO(s) or DSO(s). This contributes to a better usage of public money and fosters the development of new flexibility resources through local price signals. This is particularly true in the case of complex usage profiles like demand response.

A market is the most efficient way to match demand and supply. It reduces market entry barriers through standardization of products and processes while at the same time leaving sufficient room for adaptation to local constraints and specificities. Therefore, we strongly welcome the provisions of the ACER proposal of 5 September 2024 of Art. 38 and Art. 39 that clearly establish market-based flexibility procurement by default and that further clarify derogations from it. In particular, we welcome the introduction of an assessment prior to granting a derogation (Art. 38.3) and the introduction of a maximum validity period of derogations of two years (Art. 39.4). Our recommendation therefore is to keep the provisions of Art. 38 and Art. 39.

3. Ensure multi-market access for flexibility service providers across wholesale, flexibility and balancing markets while avoiding combined markets with forwarding of bids (whereas 26, Art. 6, Art. 41, Art. 42, Art. 43, Art. 44, Art. 48)

What needs to be achieved is a multi-market access for flexibility service providers to wholesale, balancing and local flexibility markets because this enables them to commercialise their flexibility assets and portfolios on all different market segments without any barriers. Multi-market access can be best achieved through i) standardization of processes, product compatibility, and technical standards such as CIM, ii) a clear and efficient TSO-DSO coordination avoiding conflicting bid activation, and iii) BRP rules incentivising that market participants are balanced before gate closure time.

The EPEX SPOT localflex trading platform offers exactly this kind of TSO-DSO coordination mechanism to avoid double or conflicting flexibility activation, e.g. by identifying conflicting flexibility bids on the TSO and DSO side, and by coordination rules in the clearing engine. This coordination between TSOs and DSOs is

important in order to optimize the limited pool of flexibility sources for the different needs at the various voltage levels.

A multi-market access does not require a blurry concept of combined markets with forwarding of bids between local flexibility and day-ahead and intraday markets. Flexibility and electricity spot markets shall not be mixed up. These markets have different products, different prices, different collaterals, different memberships, and different risks hedged. It remains unclear from the ACER proposal of 5 September 2024 for what purpose bids should be forwarded and under which conditions. The bid forwarding idea raises many practical implementation questions, such as on roles, responsibilities, contractual relationships e.g. membership with exchanges, cost structure e.g. collaterals when relevant, and level playing field with other market participants. In addition, it is difficult to see how the suggested usage of bids offered in day-ahead and intraday markets to solve congestions could work in countries with portfolio bidding and also because there are no locational tags in single intraday and single day-ahead markets (SDAC and SIDC) (Art. 43.1). Locational information is required for any bid in a local flexibility market in order to solve a local congestion.

The Network Code should focus on facilitating multi-market access and revenue stacking, not proposing a solution (bid forwarding) that has not been thought through. Giving „consent“ is clearly not enough of a condition to be able to „forward bids“, as ACER suggests in Art. 42.6. In addition, it is the clear role and task of aggregators to push volumes of flexibility assets to the different existing market segments, be it wholesale, balancing or local flexibility markets, in order to commercialise the flexibility assets in the optimal way according to their clients' needs. Forwarding of bids is not a role or task for system operators or local market operators.

4. Reintroduce requirements for local market operation to ensure a neutral, secure and robust functioning of local flexibility markets (Art. 16, Art. 42)

We generally agree with the ACER proposal of 5 September 2024 that the local flexibility market operation becomes a system operator responsibility by default and that this responsibility can be delegated by the system operator or a member state to a third party. However, it is of utmost importance to reintroduce a certain set of European-wide harmonized minimum requirements for the local market operation to ensure a neutral, secure and robust functioning of local flexibility markets.

The requirements for local market operation shall include at least (i) neutrality and transparency in case that several system operators, service providers or stakeholders are involved, (ii) proven technical, personal, operational and organisational expertise and resources with regard to the operation of local markets, (iii) appropriate market surveillance arrangements in place, and (iv) an adequate level of business separation in case of potential conflicts of interest. In addition, the Network Code needs to clarify that in case a system operator decides to delegate the local market operation task to a third party, the delegation needs to be done through a transparent and non-discriminatory process.

5. Foster DSO-TSO coordination to solve congestions in the most efficient ways (Art. 54 – Art. 59)

We welcome that the proposal for a Network Code on Demand Response contains a dedicated chapter (“Title VII”) on the important topic of TSO-DSO coordination, including the provision that system operators shall develop a common proposal for TSO-DSO and DSO-DSO coordination. TSO-DSO and DSO-DSO coordination needs to be fostered for a coordinated collaboration to solve congestions in the most efficient ways. Also, BRP and local flexibility markets need to be linked more closely. We suggest encouraging the use of local flexibility markets for TSO-DSO coordination. Its costs shall also be recovered for that purpose.