Urgent Call for Action on Core TSOs Regarding Local Auctions at a Decoupled NEMO in the Core MNA Areas

URGENT: LOCAL AUCTIONS IN CORE MNA AREAS

Local Auctions in Core MNA areas: In Breach of European Law

Since the entering into force of Article 7 of the newly adopted Electricity Regulation on 16 July 2024, a Nominated Electricity Market Operator (NEMO – power exchange) is **in breach of European law**, if it operates a **proprietary auction (Local Auction) as a decoupled NEMO in the MNA areas of the Core region (Germany, Austria, France, Belgium, the Netherlands)** whilst another NEMO in the same bidding zone is coupled to the single day-ahead coupling (SDAC).

Article 7 states that "*NEMOs shall not organise trading with day-ahead products or products with the same characteristics outside the single day-ahead coupling*". [*emphasis added*]

In other words, for as long as one NEMO in a bidding zone is coupled to the single day-ahead coupling (SDAC), **no NEMO is allowed to operate *in parallel* a Local Auction with day-ahead products.**

Article 7, as the higher ranking European law, **automatically overrides** any conflicting provisions included in **the Core Fallback Procedures and the Core Multi-NEMO Arrangements (MNAs),** which allow a decoupled NEMO to operate a Local Auction in an MNA area, when another NEMO operating in the same bidding zone(s) is coupled to the single day-ahead coupling (SDAC).

For Core Transmission System Operators (TSOs) and NEMOs this means that, since 16 July 2024, they must **not** allow a NEMO to operate a Local Auction in parallel to the SDAC - even if a formal revision to align the Core fall-back procedures and the Core MNAs with European law has not yet taken place. Nord Pool encourages the Core TSOs to align the procedures with European law as soon as possible.

Until the Core Fallback Procedures and the Core MNAs are formally aligned with European law, market participants need to be aware that, if they submit offers to a Local Auction of a decoupled NEMO in the MNA areas of the Core region, they risk participating in an auction which, in all likelihood, is subject to challenge in front of national and European authorities and courts.

Local Auctions: Isolation Leads to Skewed Results

The available time for NEMOs to submit aggregated order books received for the SDAC auction at 12:00h is just 10 minutes. If a NEMO is unable to submit its order books to the SDAC by 12:10h, all NEMOs are notified and the NEMO experiencing the problem has a maximum of **55 minutes** more, in which to resolve it.

If such NEMO is unable to submit its order books **by 13:05h, the Core Fallback Procedures** foresee the decoupling **of the individual NEMO** from the SDAC (termed a '**partial decoupling'**).

Under current procedures, the decoupled NEMO is then allowed to operate a day-ahead auction in isolation, i.e. based solely on its own, proprietary order book and without any access to cross-border capacity (**Local Auction**).

Local Auctions, operated in isolation and based solely on the proprietary order book of the decoupled NEMO have produced **skewed results**. The incident of 25 June 2024 showed that it is **not possible** for a single NEMO in an MNA area - once decoupled - to get reasonable market prices **without access to either other NEMOs' order books or interconnector capacity** to neighbouring areas. Isolated order books can be heavily weighted to either the buy or the sell side, and, in general, lack the "checks-and-balances" from "outside liquidity" through coupling with other NEMOs' order books and across bidding zones.

Local Auctions: Unacceptable and Anti-Competitive

In addition, Local Auctions operated by a decoupled NEMO in the MNA areas of the Core region cause **unacceptable risks for the orderly conduct of the markets** and **have detrimental effects on competition between power exchanges**. The incumbent power exchange benefits massively from market participants moving to, and hedging their contracts against the prices of, the power exchange with the higher liquidity, in an attempt to avoid price uncertainty.

Another partial decoupling in one of the MNA-areas of the Core region would inflict another severe blow to power exchange competition in the MNA areas in the region.

Local Auctions: Time to take Immediate Action

In the interest of orderly and safe market operation and in line with Article 7 of the Electricity Regulation, **any uncertainty for market participants** about the operation of Local Auctions and the applicable SDAC price in case of the decoupling of a NEMO in an MNA area of the Core region **should be removed immediately**.

Against this background, Nord Pool urges DG ENER, ACER and Core TSOs to take three urgent and immediate actions:

URGENT ACTION 1:

- **DG ENER and ACER should immediately notify market participants that, since the entering into force of Article 7 of the Electricity Regulation on 16 July 2024, the concept of Local Auctions operated by a partially decoupled NEMO in the MNA areas of the Core region is no longer applicable.**

URGENT ACTION 2:

- **Core TSOs should immediately amend the existing Core Fallback Procedures for 'partial decoupling' of a NEMO and the Core MNAs and align them with European law.**

URGENT ACTION 3:

- **Core TSOs should further immediately amend the existing Core Fallback Procedures for 'partial decoupling' of a NEMO and the Core MNAs, to guarantee that there is a single SDAC price in the affected areas.**

The co-existence of a Local Auction price published by the decoupled NEMO(s) alongside the SDAC coupled price published by the NEMOs which remain in the coupling, **creates a strong incentive for market participants to use the price of the NEMO with the higher liquidity** for their physical trading, clearing and settlement and as the reference for the settlement of their financial contracts.

Without a "competing" Local Auction price in the MNA areas of the Core region, market participants **could reliably use the SDAC price as a reference for their hedges at all times.** Existing bilateral and financial contracts referring to an individual NEMO's price publication would not need to be renegotiated, as the price published by the decoupled NEMO would also be the SDAC price.

Likewise, **European and national legislation and regulation** could reliably refer to the SDAC price as the **relevant market price** for calculating **any feed-in tariffs for renewable energy** (e.g. in the German Renewables Act (EEG)) and as the **binding reference price** for **any other European and national regulation** (e.g. regulation regarding balancing markets) – without having to worry about price differentials in cases of partial decoupling of a NEMO.

Therefore, in addition to the removal of "Local Auctions" in the MNA-areas of the Core region, Nord Pool calls for the amendment of the existing Core Fallback Procedures for "partial decoupling of a NEMO" in the MNA-areas of the Core region as follows, to **guarantee there is always a single SDAC price:**

(i) **If a NEMO is not able to submit an order book to the SDAC, the affected NEMO in an MNA-area of the Core region cancels its participation in the SDAC auction**. The affected NEMO is decoupled from the SDAC ("**partial decoupling**"). The affected NEMO announces its partial decoupling to market participants as soon as the affected NEMO becomes aware that it will be unable to meet the deadline for submitting an order book (currently 13:05h).

(ii) The SDAC price is then calculated **without the orders from the decoupled NEMO**. The SDAC price is **published by all NEMOs**, including by the decoupled NEMO. The SDAC price is the only price publication at all NEMOs. The decoupled NEMO is NOT allowed to operate a Local Auction.

(iii) **After the SDAC price is published, the decoupled NEMO can offer market participants the opportunity to have some of their volumes settled at the (fixed) SDAC price:** market participants may – by a certain deadline - (i) confirm or withdraw the volumes behind any

orders they have submitted to the decoupled NEMOs order book prior to the 12:00h SDAC auction, or (ii) adjust or add new volume orders. The decoupled NEMO will allocate buy- and sell-volumes on a pro-rata basis at the SDAC price until all volumes that can be balanced/cancelled out are allocated. **Any "overshooting" buy or sell volumes will remain unmatched** and should be traded OTC or in the intraday market. This pro-rata volume allocation at the (fixed) SDAC price should help to clear physical volumes which could not participate in the SDAC auction, from the market at least up to a certain level.

ADDITIONAL PROPOSALS (FOR CACM 2.0)

Additional recommendations to further reduce the risk of decoupling

In addition to the urgent and immediate actions set out above, Nord Pool proposes the following amendments to the Core fall-back procedures, to further reduce the risk that another decoupling occurs in the Core region:

PROPOSAL 1:

Oblige Core TSOs to give NEMOs in the Core region more time to resolve problems

Core TSOs have set a strict deadline at 15:30h, by which they need to receive the cross-border day-ahead volume nominations from NEMOs. Unlike the Nordic and Baltic TSOs, Core TSOs do not allow any flexibility around this deadline, even if its extension could help prevent a decoupling. This policy has huge negative consequences for the market and increases risks to the operational security of the grid.

Nord Pool believes that a successful implementation of the energy transition in Europe urgently requires **maintaining a coupled day-ahead market**. **TSO processes**, while important, **should allow for flexibility in exceptional circumstances** to grant NEMOs more time to resolve problems. This provision will ensure that there is a trustworthy price signal and volume allocation from a pan-European coupled SDAC market and would reduce decoupling risk considerably.

Many of the decoupling incidents that have occurred so far, would have been avoided by granting NEMOs more time to resolve problems. Delayed opening of the intraday market seems a minor price to pay in exchange for producing the strong price signal of a coupled SDAC auction.

PROPOSAL 2:

Oblige NEMOs in the Core region to submit "Shadow Order Books" to avoid decoupling

NEMOs shall offer to market participants the **option to submit bids and offers to order books ("Shadow Order Books") compiled by NEMOs at certain time(s) prior to the respective SDAC auction.** The exact submission deadline(s) are the subject of an ongoing discussion with market

participants. NEMOs will submit any Shadow Order Books to the SDAC immediately after their closure on D-1.

If a NEMO subsequently experiences problems with submitting the order book compiled at 12:00h on the SDAC trading day, it informs the other NEMOs and market participants that the last Shadow Order Book submitted should be included in the SDAC auction.

The Shadow Order Books are submitted at certain time(s) prior to the respective SDAC auction, to allow a NEMO to sort out any problems with their order submission, while also allowing them to provide, at the same time, the most up-to-date Shadow Order Book submitted to the SDAC. Shadow Order Books should therefore be a good back-up for market participants' bids and offers.

The advantage of the Shadow Order Books is that **the NEMO which "activates" a Shadow Order Book remains in the coupling**. The SDAC price is calculated based on orders submitted to the SDAC auction by the coupled NEMOs, including orders in the Shadow Order Book submitted and activated by the NEMO which is having problems. Submission of Shadow Order Books as "hot back-ups" reduces considerably the risk of a partial decoupling of a NEMO and ensures smooth operation of the SDAC auction.

Long term goal: Remove the need to partially or fully decouple a NEMO in an MNA area in the Core region

The proposals in this paper do not replace the need for a thorough redrafting of the Core Day-Ahead Fallback procedures in the long-term. Such redrafting should **ensure that a single SDAC price is calculated at all times based on the order inputs from ALL participating NEMOs and the available capacities from ALL TSOs**.

Realising this long-term goal will require an optimisation of the daily processes which will allow **removing time set aside for full decoupling**. Daily processes should be further optimised with the aim of **freeing up NEMOs and TSOs time by cutting out unnecessary processes and redundancies** – starting, e.g. with the removal of secondary auctions and shadow auctions on the decoupled borders. In addition, a thorough review and streamlining of the TSO processes which take place at the end of the day-ahead timeframe and at the start of the intraday timeframe, is needed.

For a start, Nord Pool suggests the following:

PROPOSAL 3:

Amend the existing Core Fallback Procedures for "full decoupling of all NEMOs" in the Core region to guarantee a single SDAC price in this scenario

Existing Core procedures foresee a **full decoupling** of all NEMOs in the Core region **at 14:20h**, e.g. if the common algorithm is unable to calculate results by then.

All the market participants Nord Pool spoke to after the incident on 25 June 2024 agreed that the **priority of the Core Fallback Procedures** should be **to guarantee that there is ALWAYS only**

one, reliable single day-ahead price (SDAC price) for each bidding zone against which physical contracts are settled and financial contracts can be hedged.

To achieve this, Nord Pool suggests that, if it comes to a **"full decoupling of all NEMOs"** in the Core region, the existing Core Fallback Procedures are amended as follows to ensure that **a single SDAC reference price is guaranteed:**

(i) All NEMOs in the Core region **cancel their participation in the SDAC auction ("full decoupling")** (timings based on the revised procedures).

(ii) A large volume of physical trading will move to SIDC or to the OTC market. If intraday auctions (IDAs) prove liquid enough, the **price of the first (possibly delayed) common intraday auction (IDA), or, alternatively, a suitable index derived from the intraday continuous market defined in the Core Fallback Procedures, is declared to be the SDAC reference price**. As no cross-border capacities were used in the day-ahead time frame, TSOs should be able to assign these as a whole to the first of a (possibly delayed) IDA or to the intraday continuous market, depending on which opens first.

(iii) This process ensures only one SDAC reference price in a situation with full decoupling of the SDAC market.

WHY NORDIC/BALTIC FALLBACK PROCEDURES DO NOT NEED AMENDING

In recognition of the havoc that any decoupling of individual NEMOs causes in the markets, **the Nordic and Baltic market places a priority on keeping the NEMOs in the Nordic/Baltic region coupled**.

As a first step, the entire Nordic/Baltic region is decoupled from the Core region. Then, within the Nordic/Baltic region, the **Nordic and Baltic TSOs** allow all NEMOs **until 20:00h** to resolve any problems.

In the unlikely event that no regional day-ahead auction results can be achieved, and **as a measure of last resort**, **SDAC prices and traded volumes from the previous day will be applied**.

The extended timeline in exceptional cases and the last resort SDAC price, guarantee a single day-ahead price for each bidding zone in the Nordic/Baltic region under all circumstances and thus **do not require amendment**.