

**DECISION No 10/2021
OF THE EUROPEAN UNION AGENCY
FOR THE COOPERATION OF ENERGY REGULATORS**

of 13 August 2021

**on the market-based allocation process of cross-zonal capacity for
the exchange of balancing capacity for the Baltic CCR**

THE EUROPEAN UNION AGENCY FOR THE COOPERATION OF ENERGY REGULATORS,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) 2019/942 of the European Parliament and of the Council of 5 June 2019 establishing a European Union Agency for the Cooperation of Energy Regulators¹, and, in particular, point (b) of the second subparagraph of Article 6(10) thereof,

Having regard to Commission Regulation (EU) 2017/2195 of 23 November 2017 establishing a guideline on electricity balancing, and, in particular, Articles 5(3)(h) and 6(2) thereof,

Having regard to the outcome of the public consultation and consultation with the concerned regulatory authorities and transmission system operators,

Having regard to the outcome of the consultation with the ACER's Electricity Working Group ('AEWG'),

Having regard to the favourable opinion of the Board of Regulators of 13 July 2021, delivered pursuant to Article 22(5) of Regulation (EU) 2019/942,

Whereas:

1. INTRODUCTION

- (1) Commission Regulation (EU) 2017/2195 of 23 November 2017 establishing a guideline on electricity balancing (the 'EB Regulation') laid down a range of requirements for electricity balancing, for the exchange of balancing capacity, as well as pricing and settlement of balancing capacity. These requirements include the

¹ OJ L158, 14.6.2019, p. 22.

possibility for the transmission system operators of a capacity calculation region ('CCR') to develop a methodology for a market-based allocation process of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves.

- (2) Pursuant to Articles 4(1) and 5(3)(h) of the EB Regulation, transmission system operators of a CCR may agree on a common proposal for the market-based allocation process of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves in accordance with Article 41(1) of the EB Regulation and submit it to the regulatory authorities of that CCR for approval. In accordance with Article 5(6) of the EB Regulation, regulatory authorities shall reach an agreement and take a decision within six months after the receipt of the proposal by the last regulatory authority.
- (3) Regulatory authorities can require an amendment to the proposal in accordance with Article 6(1) of the EB Regulation where transmission system operators have two months to submit an amended proposal to regulatory authorities. Then, regulatory authorities have two months to decide on the amended proposal. When regulatory authorities fail to reach an agreement within the two-month period after the submission of the amended proposal or upon their joint request, ACER, pursuant to Article 6(2) of the EB Regulation, shall adopt a decision concerning the proposal in accordance with point (b) of the second subparagraph of Article 6(10) of Regulation (EU) 2019/942.
- (4) This Decision of ACER follows from the request of regulatory authorities of the Baltic CCR that ACER adopts a decision on the proposal for a market-based allocation process of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves methodology, which the transmission system operators of the Baltic CCR (hereafter referred to as 'the TSOs') submitted to the regulatory authorities of the Baltic CCR (hereafter referred to as 'the regulatory authorities') for approval and on which the regulatory authorities could not agree on. Annex I to this Decision sets out the methodology pursuant to Article 41(1) of the EB Regulation as decided by ACER.

2. PROCEDURE

2.1. Proceedings before regulatory authorities

- (5) Article 41(1) of the EB Regulation allows the TSOs to submit a proposal for a market-based allocation process of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves methodology by two years after the entry into force of the EB Regulation. As the EB Regulation entered into force on 18 December 2017, the deadline to submit a proposal was 18 December 2019.
- (6) On 4 November 2019, the TSOs published for public consultation the draft proposal² for the 'Baltic CCR's Proposal for a Methodology for a market-based allocation

² https://consultations.entsoe.eu/markets/ebgl-art-41-baltic-ccr-market-based-czca/supporting_documents/Baltic%20CCRs%20CZCA%20proposal_20191009.pdf

process of cross zonal capacity for the exchange of balancing capacity or sharing of reserves in accordance with Article 41 of the Commission Regulation (EU) 2017/2195 of 23 November 2017 establishing a guideline on electricity balancing'. The consultation lasted from 4 November 2019 to 4 December 2019.

- (7) On 18 December 2019, the TSOs submitted to the regulatory authorities a 'Baltic CCR's Methodology for a market-based allocation process of cross zonal capacity for the exchange of balancing capacity or sharing of reserves in accordance with Article 41 of the Commission Regulation (EU) 2017/2195 of 23 November 2017 establishing a guideline on electricity balancing'³, which was received by the last regulatory authority on 20 December 2019.
- (8) The regulatory authorities jointly agreed to request an amendment and sent this request to the TSOs. The last regulatory authority issued the request for amendment nationally on 19 June 2020.
- (9) On 13 August 2020, the TSOs resubmitted the amended 'Baltic CCR's Methodology for a market-based allocation process of cross zonal capacity for the exchange of balancing capacity or sharing of reserves in accordance with Article 41 of the Commission Regulation (EU) 2017/2195 of 23 November 2017 establishing a guideline on electricity balancing'⁴ to the regulatory authorities. The last regulatory authority received the Proposal on 31 August 2020. Therefore, the new deadline for approval by the regulatory authorities was 31 October 2020.
- (10) The regulatory authorities jointly agreed to request a second amendment and sent this request to the TSOs. The last regulatory authority issued the request for amendment nationally on 30 October 2020.
- (11) On 30 December 2020, the TSOs resubmitted the amended 'Baltic CCR's Methodology for a market-based allocation process of cross zonal capacity for the exchange of balancing capacity or sharing of reserves in accordance with Article 41 of the Commission Regulation (EU) 2017/2195 of 23 November 2017 establishing a guideline on electricity balancing'⁵ to the regulatory authorities (hereafter referred to as the 'Proposal'). The last regulatory authority received the Proposal on 31 December 2020. Therefore, the new deadline for approval by the regulatory authorities was 28 February 2021.

³ <http://www.acer.europa.eu/en/Electricity/MARKET-CODES/ELECTRICITY-BALANCING/12%20CZCAM/Action%204%20-%20MB%20CZCA%20Baltic%20proposal.pdf>

⁴ <http://www.acer.europa.eu/en/Electricity/MARKET-CODES/ELECTRICITY-BALANCING/12%20CZCAM/Action%2011%20-%20MB%20CZCA%20Baltic%20amended%20proposal.pdf>

⁵ <http://www.acer.europa.eu/en/Electricity/MARKET-CODES/ELECTRICITY-BALANCING/12%20CZCAM/Action%2018%20-%20MB%20CZCA%20Baltic%20second%20amended%20proposal.pdf>

2.2. Proceedings before ACER

- (12) On 26 February 2021 ACER was notified via the ACER notification survey tool and via email that the regulatory authorities were not able to reach an agreement within the two-month deadline and requested ACER to adopt a decision on the Proposal pursuant to Article 6(10) of Regulation 2019/942. This notification included a description of the legal context and an assessment of the Proposal by the regulatory authorities.
- (13) Between 12 April and 2 May 2021, ACER held a public consultation⁶ on the Proposal, seeking views from all interested parties. Annex II provides a summary of comments received along with ACER's responses to these comments.⁷
- (14) Between 26 February 2021 and 1 June 2021, ACER engaged in discussions with the TSOs and regulatory authorities. These discussions involved numerous conference calls and electronic exchange of documents, allowing ACER to gather information and form its preliminary position on the Proposal. These discussions focused on ACER's assessment framework as described in section 6.1 and on reaching a common understanding or exchanging views on aspects of the Proposal as referred to in section 5.2.
- (15) Between 1 and 14 June 2021, ACER consulted the TSOs and regulatory authorities on its preliminary position, by sharing an updated version of the Proposal setting out its suggested amendments and reasoning for these amendments. The consulted parties provided their views by 14 June. These views are summarised in section 5.4.
- (16) ACER considered all the written comments received on its preliminary position, and further discussed them with the individual stakeholders, where necessary. Following this process, ACER introduced further amendments to the Proposal to take some issues raised by the consulted parties into account.
- (17) The AEWG was consulted between 17 and 24 June 2021, and provided its advice on 24 June 2021 (see section 5.5).
- (18) On 13 July 2021, ACER's BoR issued a favourable opinion pursuant to Article 22(5)(a) of Regulation (EU) 2019/942.

3. ACER'S COMPETENCE TO DECIDE ON THE PROPOSAL

- (19) Pursuant to Article 6(2) of the EB Regulation, where the regulatory authorities have not been able to reach an agreement or upon their joint request, ACER shall adopt a

⁶PC/2021/E/02, see ACER's consultation page:

https://www.acer.europa.eu/Official_documents/Public_consultations/Pages/PC_2021_E_02.aspx.

⁷This is a summary and not to be considered a complete representation of the comments received. All non-confidential responses are published on ACER's consultation page (see footnote 6).

decision concerning the submitted terms and conditions or methodologies within six months in accordance with Article 6(10) of Regulation (EU) 2019/942.

- (20) According to the notification received on 26 February 2021, the regulatory authorities did not reach an agreement on the Proposal and therefore ACER became competent to adopt a decision on the Proposal pursuant to Article 6(2) of the EB Regulation.

4. SUMMARY OF THE PROPOSAL

- (21) The Proposal consists of the following elements:
- (a) the ‘Whereas’ section and Articles 1 and 2, which include general provisions on subject matter and scope and definitions and interpretation;
 - (b) Articles 3, 4 and 5, which cover principles for applying the market-based allocation process of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves (hereafter referred to as the ‘market-based allocation process’), the notification process for the use of a market-based allocation process and the timeframe of market-based allocation;
 - (c) Article 6, which describes the maximum volume of allocated cross-zonal capacity for the exchange of balancing capacity;
 - (d) Article 7, on the determination of the market value of cross-zonal capacity for the exchange of energy;
 - (e) Article 8, on the determination of the market value of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves;
 - (f) Article 9, which specifies the determination of the allocated volume of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves;
 - (g) Articles 10, 11 and 12, which describe the pricing of cross-zonal capacity, the firmness regime and the sharing of congestion income; and
 - (h) Articles 13, 14 and 15, which include provisions on publication, implementation timeline and language.

5. OBSERVATIONS RECEIVED BY ACER

5.1. Initial observations of the regulatory authorities

- (22) The notification referred to in Recital (12) stated that the regulatory authorities could not agree to the proposed description of the maximum volume of allocated cross-zonal capacity for the exchange of balancing capacity or sharing of reserves. Furthermore, some regulatory authorities suggested that the proposal could be improved in other aspects than that regarding the process of defining a maximum volume of allocated cross-zonal capacity.

5.2. Consultation of regulatory authorities and TSOs

- (23) ACER closely cooperated and consulted with the regulatory authorities and TSOs, as mentioned in Recital (14), above by discussing and exchanging views and proposals on:
- a) the comments received during the public consultation (see section 5.3) and the views of the regulatory authorities expressed in the aforementioned notification;
 - b) the proposed determination of the maximum volume for the allocation of cross-zonal capacity for the exchange of balancing capacity and sharing of reserves and possible alternative approaches;
 - c) the additions of the necessary details and provisions for the determination of the maximum volume for the allocation of cross-zonal capacity for the exchange of balancing capacity and sharing of reserves;
 - d) the implementation timeline including the submission of an amended proposal for the market-based allocation process;
 - e) the possible timing of performing the market-based allocation process;
 - f) possible approaches for sharing congestion income and possibilities to address the risk of missing money for the remuneration of long-term transmission rights due to an application of the market-based allocation process; and
 - g) other provisions like linking of bids and situations allowing a flexible TSO demand or provisions for situations with local shortage of bids and changes of the Proposal, aiming for a first harmonisation among existing regional market-based methodologies where possible.

5.3. Public consultation

- (24) Responses to ACER's public consultation⁸ are summarised in Annex II to this Decision.

5.4. Consultation on ACER's preliminary position

- (25) The following paragraphs provide a summary⁹ of views on ACER's preliminary position received during the hearing phase between 1 and 14 June 2021. ACER received written comments on 14 June from the following parties:
- (a) the Baltic regulatory authorities and TSOs, namely Elering AS, AS "Augstsprieguma tīkls", LITGRID AB, Estonian Competition Authority, Council

⁸ See footnote 6.

⁹ This is ACER's summary of key concerns and not to be considered a complete representation of the comments received.

of the Public Utilities Commission of the Republic of Latvia and National Energy Regulatory Council of the Republic of Lithuania; and

- (b) the Swedish regulatory authority, Energy Markets Inspectorate (Ei).
- (26) The Baltic regulatory authorities and TSOs submitted a note on the approach proposed by ACER for the determination of the maximum volume of allocated cross-zonal capacity. It included an introduction on the Baltic power system and the vision of the regulatory authorities and TSOs for this, where they stress the connection between the HVDC links, the allocation of the cross-zonal capacity and the procured volume of balancing capacity. In the second part of the note they present the reasoning for their disagreement with ACER's proposed maximum volume, providing also a table indicating the connection between the allocated cross-zonal capacity and the procured balancing capacity. Finally, they list their proposals highlighting that although they do understand ACER's concerns about inefficient allocation between the day-ahead and the balancing capacity markets, they deem it important that the market participants receive the correct signal about the intention of the Baltic TSOs. Their proposals include:
- (a) the differentiation of the maximum volume depending on the direction, with the maximum volume being set to 80% for the borders between Estonia and Latvia, and Lithuania and Latvia, for the direction that the forecasted market value for the cross-zonal capacity for the exchange of energy is zero;
 - (b) setting the maximum volume for the borders between Estonia and Latvia, and Lithuania and Latvia, to not less than 50% and fallback volume to 80%; and
 - (c) setting the deadline for submitting an amended methodology to 12 months (instead of the proposed 18), enabling also to overlook the maximum volume limits with a more detailed forecasting methodology.
- (27) Ei in its submission raised comments on three issues: on the determination of the maximum volume of allocated cross-zonal capacity, on the determination of the market value of cross-zonal capacity for the exchange of balancing capacity and sharing of reserves, and on the sharing of congestion income. More specifically, the comments were related to:
- (a) Regarding the maximum volume: Ei notes that it is important to restrict the maximum level of cross-zonal capacity that TSOs can reserve for balancing resources to "protect" the day-ahead market from over-allocation to the balancing capacity market and links this higher volume with a more precise forecasting methodology, acknowledging the need for the TSOs of the future load frequency control ('LFC') block to have higher limits, agreeing with ACER's proposal. Moreover, Ei suggests a separation between the internal Baltic LFC block and the rest of the Baltic CCR borders in case higher maximum volume is applied. Finally, Ei requests a legal analysis for the requirement this Proposal to respect the 70% rule pursuant to Article 16(8) of Regulation (EU) 2019/943 of the European Parliament and of the Council of 5 June 2019 on the internal market for electricity (recast) ('Electricity Regulation').

- (b) Regarding the market value: Ei requires further clarification on the term “lower quality standard balancing capacity products”.
- (c) Regarding the sharing of congestion income: Ei, although it supports the approach proposed by ACER to include the congestion income generated through the exchange of balancing capacity and sharing of reserves in the day-ahead congestion income distribution methodology developed pursuant to Article 73(1) of Commission Regulation (EU) 2015/1222 of 24 July 2015 establishing a guideline on capacity allocation and congestion management (‘CACM Regulation’), requires more clarifications how this congestion income will be included in the day-ahead one, as the different treatment may have an impact on TSOs’ incentives to reserve capacity for sharing of reserves. Moreover, Ei requires clarifications on the comparison that follows from the assessment introduced in Article 11(3) of Annex I and suggests to replace the annual assessment to be made more frequently (daily, weekly or monthly). Finally, Ei highlights that the risk due to not sufficient congestion income should be borne by the TSOs allocating cross-zonal capacity for the exchange of balancing capacity or sharing of reserves and this should be explicitly stated in the methodology, as the text included now is not clear.

5.5. Consultation of the AEWG

- (28) The AEWG provided its advice on 24 June 2021, broadly endorsing the draft ACER Decision with Annexes. AEWG invited ACER to consider comments made by the regulatory authorities during the AEWG consultation phase. More specifically further clarifications are required regarding the intention of the two limits – one addressing operational security concerns, while the other protecting the day-ahead market from inaccurate forecasts; hence, the improvement of the forecasting method and considering the reserve dimensioning are important steps. Moreover, further improvement of the monitoring provisions is necessary to ensure detecting developments in due time.

6. ASSESSMENT OF THE PROPOSAL

6.1. Legal requirements

- (29) Articles 41(1) and 5(3)(h) of the EB Regulation provide that TSOs of a CCR may propose a methodology for a market-based allocation process of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves in accordance with Article 41(1) of the EB Regulation. This proposal must be submitted to the concerned regulatory authorities for their approval. Additionally, Article 6(1) of the EB Regulation requires the concerned TSOs to submit an amended proposal for the market-based allocation process for approval to the concerned regulatory authorities, following a request for amendment of the initial proposal by the concerned regulatory authorities. The methodology for the market-based allocation process shall apply for the exchange of balancing capacity or sharing of reserves with a contracting period of not more than one day and where the contracting is done not more than one week in

advance of the provision of the balancing capacity. Article 41(1) of the EB Regulation further elaborates on the requirements for such a methodology, which shall include:

- (a) the notification process for the use of the market-based allocation process;
 - (b) a detailed description of how to determine the actual market value of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves, and the forecasted market value of cross-zonal capacity for the exchange of energy, and if applicable the actual market value of cross-zonal capacity for exchanges of energy and the forecasted market value of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves;
 - (c) a detailed description of the pricing method, the firmness regime and the sharing of congestion income for the cross-zonal capacity that has been allocated to bids for the exchange of balancing capacity or sharing of reserves via the market-based allocation process;
 - (d) the process to define the maximum volume of allocated cross-zonal capacity for the exchange of balancing capacity or sharing of reserves pursuant to Article 41(2) of the EB Regulation.
- (30) Article 41(2) of the EB Regulation provides that cross-zonal capacity allocated on a market-based allocation process shall be limited to 10 % of the available capacity for the exchange of energy of the previous relevant calendar year between the respective bidding zones or, in case of new interconnectors, 10 % of the total installed technical capacity of those new interconnectors, and provides the conditions for when this volume limitation may not apply. The second sentence of Article 41(2) of the EB Regulation provides that the volume limitation in the first sentence of Article 41(2) may not apply where the contracting is done not more than two days in advance of the provision of the balancing capacity or for bidding zone borders connected through High Voltage Direct Current ('DC') interconnectors until the co-optimised allocation process is harmonised at Union level pursuant to Article 38(3) of the EB Regulation.
- (31) Article 41(3) of the EB Regulation requires that the methodology is based on a comparison of the actual market value of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves and the forecasted market value of cross-zonal capacity for the exchange of energy, or on a comparison of the forecasted market value of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves, and the actual market value of cross-zonal capacity for the exchange of energy.
- (32) Article 41(4) of the EB Regulation provides that the pricing method, the firmness regime and the sharing of congestion income for cross-zonal capacity that has been allocated for the exchange of balancing capacity or sharing of reserves via the market-based allocation process shall ensure equal treatment with the cross-zonal capacity allocated for the exchange of energy.

- (33) Article 41(5) of the EB Regulation requires that cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves via the market-based allocation process shall be used only for the exchange of balancing capacity or sharing of reserves and associated exchange of balancing energy.
- (34) As a general requirement, Article 5(5) of the EB Regulation requires that the Proposal includes a proposed timescale for its implementation and a description of its impact on the objectives of the same Regulation.
- (35) Article 39 of the EB Regulation sets out the requirements for the calculation of market value of cross-zonal capacity and defines in its paragraph 3 that the actual market value of cross-zonal capacity for the exchange of balancing capacity used in a market-based allocation process shall be calculated based on balancing capacity bids submitted to the capacity procurement optimisation function pursuant to Article 33(3) of the EB Regulation.
- (36) Article 39(4) of the EB Regulation provides that the actual market value of cross-zonal capacity for the sharing of reserves used in a market-based allocation process shall be calculated based on the avoided costs of procuring balancing capacity.
- (37) Article 39(5) of the EB Regulation further elaborates that the forecasted market value of cross-zonal capacity shall be based on one of the following alternative principles:
- (a) the use of transparent market indicators that disclose the market value of cross-zonal capacity; or
 - (b) the use of a forecasting methodology enabling the accurate and reliable assessment of the market value of cross-zonal capacity.
- Moreover, the forecasted market value of cross-zonal capacity for the exchange of energy between bidding zones shall be calculated based on the expected differences in market prices of the day-ahead.
- (38) Article 39(6) of the EB Regulation further allows for the efficiency of the forecasting methodology pursuant to Article 39(5)(b) of the EB Regulation, including a comparison of the forecasted and actual market values of the cross-zonal capacity, to be reviewed by the relevant regulatory authorities. Furthermore it allows that where the contracting is done not more than two days in advance of the provision of the balancing capacity, the relevant regulatory authorities may, following this review, set a limit other than that specified in Article 41(2) of the EB Regulation.
- (39) Article 38(5) of the EB Regulation requires that TSOs may allocate cross-zonal capacity for the exchange of balancing capacity or sharing of reserves only if cross-zonal capacity is calculated in accordance with the capacity calculation methodologies developed pursuant to Regulation (EU) 2015/1222 and (EU) 2016/1719.

- (40) Article 38(6) of the EB Regulation requires that TSOs shall include cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves as already allocated cross-zonal capacity in the calculations of cross-zonal capacity.

6.2. Assessment of the legal requirements

6.2.1. Assessment of the requirements for the development and for the general content of the Proposal

6.2.1.1. Development of the Proposal

- (41) The Proposal fulfils the requirements of Articles 4(1), 4(2) and 5(3)(h) of the EB Regulation, as the TSOs from the Baltic CCR jointly developed a proposal for a market-based allocation process and submitted it for approval to all regulatory authorities of the Baltic CCR.
- (42) The procedure for the development of the Proposal followed the requirements of Article 41(1) of the EB Regulation, as the initial proposal was submitted by the last TSO on 20 December 2019 which is only two days after the submission deadline (i.e. within two years after entry into force of the EB Regulation).
- (43) Additionally, following the request for an amendment by all Baltic regulatory authorities on 19 June 2019 pursuant to Article 6(1) of the EB Regulation, the Baltic TSOs were required to submit the amended proposal for approval to Baltic regulatory authorities within two months, i.e. by 18 August 2019, which is before the date the last Baltic regulatory authority received the amended proposal.
- (44) Finally, following the second request for an amendment by all Baltic regulatory authorities on 30 October 2019 pursuant to Article 6(1) of the EB Regulation, the TSOs were required to submit the amended proposal for approval to Baltic regulatory authorities within two months, i.e. by 30 December 2019, which is the date the last Baltic regulatory authority received the amended proposal.

6.2.1.2. Proposed timescale for implementation

- (45) The Proposal partly fulfils the requirements of Article 5(5) of the EB Regulation with regard to proposing a timescale for implementation.
- (46) Article 14 of the Proposal states that the methodology shall be considered implemented once it is approved. However, questions were raised with respect to the meaning of the implementation of this methodology. Following the consultation with the regulatory authorities and the TSOs, especially with respect to the timeframe for the application of this methodology, as mentioned in Recital (54), ACER together with the regulatory authorities and TSOs, concluded that a single market-based allocation process would run at CCR level. This market-based allocation process should be in line with the requirements set in Annex I. Hence the implementation of this methodology by all Baltic TSOs requires the implementation of all the necessary components described in Annex I, including the algorithm for performing the cross-

zonal capacity allocation for the exchange of balancing capacity or sharing of reserves, and any necessary amendments of other methodologies, in order to fulfil the requirements of Annex I. Therefore, ACER concluded that implementing the cross-zonal capacity allocation process means establishing the cross-zonal capacity allocation function to be ready for application.

- (47) Moreover, pursuant to Article 38(5) of the EB Regulation TSOs may allocate cross-zonal capacity for the exchange of balancing capacity or sharing of reserves only if cross-zonal capacity is calculated in accordance with the capacity calculation methodologies developed pursuant to the CACM Regulation and Commission Regulation (EU) 2016/1719 of 26 September 2016 establishing a guideline on forward capacity allocation ('FCA Regulation'). As explained below, in section 6.2.2.1, the timeframe for the implementation of this methodology is the day-ahead one, hence the capacity calculation pursuant to the CACM Regulation is the prerequisite for the application of this methodology.
- (48) Therefore, ACER amended the second paragraph of Article 14 of the Proposal to include the abovementioned links.

6.2.1.3. Description of the expected impact on the objectives of the EB Regulation

- (49) The Proposal partly fulfils the requirement of Article 5(5) of the EB Regulation on describing the expected impact on the objectives of the EB Regulation. Recital (4) of the Proposal provides a description of the expected impact of the methodology for a market-based allocation process on the objectives of the EB Regulation. However, ACER deemed that the objectives were not sufficiently addressed in some cases or that the description was out of scope of the Proposal while other objectives were not explicitly mentioned. Therefore, ACER amended these recitals to correctly address all objectives of the EB Regulation.

6.2.2. Assessment of the requirements for market-based allocation process

6.2.2.1. Requirements on the timeframe of application of market-based allocation

- (50) Article 41(1) of the EB Regulation describes in general the time periods to which market-based allocation shall be applied, being not more than a week before the provision of the balancing capacity and a maximum contracting period of one day.
- (51) The Proposal addresses the requirements pursuant to Article 41(1) with respect to the timing of the balancing capacity contracting in its Articles 3 and 5. However, following the consultation with the regulatory authorities and the TSOs on further specifying the market-based capacity allocation process and the interaction with the other cross-zonal capacity calculation and allocation processes, it became evident that amendments to the Proposal were required.
- (52) Pursuant to Article 38(5) of the EB Regulation *“TSOs may allocate cross-zonal capacity for the exchange of balancing capacity or sharing of reserves only if cross-zonal capacity is calculated in accordance with the capacity calculation*

methodologies developed pursuant to Regulation (EU) 2015/1222 and (EU) 2016/1719.” Therefore, the timings of the processes of this methodology need to respect the relevant timings of the respective capacity calculation methodology, the outcome of which will be used as input in this methodology. Given that the implementation of the capacity calculation methodology developed pursuant to the CACM Regulation is expected before the FCA one, the relevant timings for the processes of this methodology are chosen to interact with the day-ahead ones.

- (53) Furthermore, Article 6(9) of the Electricity Regulation specifies that “*Contracts for balancing capacity shall not be concluded more than one day before the provision of the balancing capacity and the contracting period shall be no longer than one day, unless and to the extent that the regulatory authority has approved the earlier contracting... Where a derogation is granted, for at least 40 % of the standard balancing products and a minimum of 30 % of all products used for balancing capacity, contracts for the balancing capacity shall be concluded for no more than one day before the provision of the balancing capacity*”. So, earlier – than a day before the provision of balancing capacity – contracting is only allowed if all regulatory authorities (for the TSOs exchanging balancing capacity) provide national derogations, but even in this case, they can only provide the derogation up to a certain percentage of the procured balancing capacity. ACER understands that the target for this methodology should be in line with the target of the Electricity Regulation, which is that the contracting for balancing capacity – hence also the allocation of cross-zonal capacity for the exchange of balancing capacity – is conducted in the day-ahead balancing capacity timeframe.
- (54) Moreover, pursuant to Article 39(3) of the EB Regulation “*The actual market value of cross-zonal capacity for the exchange of balancing capacity used in a co-optimised or a market-based allocation process shall be calculated based on balancing capacity bids submitted to the capacity procurement optimisation function pursuant to Article 33(3).*” Since the balancing capacity bids are one of the inputs to this methodology, it is important to ensure the timely submission of this input. Hence, in Article 3 of the Proposal an explicit requirement has been added, which sets the gate closure time for the submission of the standard balancing capacity product bids at the latest one day before the provision of the standard balancing capacity product. Furthermore, since the cross-zonal capacity that can be allocated by this methodology should be first calculated by the CACM capacity calculation methodology, and afterwards the non-allocated part should be made available for allocation in the SDAC, the time window for the application of this methodology is really limited. This is why ACER, together with regulatory authorities and TSOs, reached the conclusion that a single gate closure time should be set for the standard balancing capacity bids that are input to this methodology. Moreover, differentiated gate closure times and applications of this methodology would raise issues of discrimination and non-equal level playing field among different products, since the allocation of the cross-zonal capacity would take place sequentially (following a first-come-first-served principle), favouring the applications of the methodology that take place earlier, leading to efficiency losses, since the sequential process does not optimise the allocation in economic surplus terms.

- (55) The discrimination and non-equal level playing field concerns were shared also by many participants in the public consultation conducted by ACER on this methodology, as mentioned in Recital (24), where this issue was brought up, with a specific question for the stakeholders. However, there were also arguments in favour of keeping a sequential procurement of the balancing capacity for different products, mainly reasoned by occurring negative consequences which can be addressed by the possibility of linking the bids. It is important to underline that this requirement is only for the submission of balancing capacity bids in the context of the exchange of balancing capacity and not for the national procurement of balancing capacity. Moreover, any arguments for losses in welfare are covered by the possibility of linking bids of different products, as well as the TSO demand – in the context of the balancing capacity exchange – with local balancing capacity bids, used only for the national balancing capacity procurement (see the Recital (82) on linking of bids and flexible TSO demand below).
- (56) Therefore, ACER added the necessary provisions in the newly introduced Article 3 of Annex I. More specifically, Article 3(4) of Annex I describes the limitations for the contracting period, while Article 3(3) of Annex I describes the limits for the gate closure time when applying the market-based allocation process. In order to ensure consistency with the processes of the day-ahead timeframe, the requirement for the gate closure refers to these processes.

6.2.2.2. Requirements on the content of the methodology for a market-based allocation process

- (57) Articles 41(1)(a), (b), (c) and (d) of the EB Regulation set the requirements for the content of the methodology for a market-based allocation process. Following these requirements, the methodology for a market-based allocation process shall address a notification process, a detailed description on how cross-zonal capacity is allocated, a process to define the maximum volume of cross-zonal capacity to be allocated for the exchange of balancing capacity or sharing of reserves and the pricing method, the firmness regime and sharing of congestion income for cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves.
- (58) Article 4 of the Proposal addresses the notification process for the use of the market-based allocation process. Therefore, the Proposal fulfils the general requirement of Article 41(1)(a) of the EB Regulation. However, according to Article 150 of the Commission Regulation (EU) 2017/1485 of 2 August 2017 establishing a guideline on electricity transmission system operation ('SO Regulation'), additional requirements need to be fulfilled for the notification process, in particular with respect to the involved TSOs, the average expected amount of power interchange, the maximum volume of the allocated cross-zonal capacity through the process. Therefore, ACER amended this article in agreement with TSOs to improve its structure and content.
- (59) Article 7 of the Proposal describes how to determine the forecasted market value of cross-zonal capacity for the exchange of energy. Therefore, the Proposal fulfils the general requirement of Article 41(1)(b) of the EB Regulation with respect to the

market value of cross-zonal capacity for the exchange of energy. However, following the consultation with Baltic regulatory authorities and TSOs on the maximum volume of the allocated cross-zonal capacity, ACER deemed it necessary to amend Articles 7 of the Proposal by adding a new paragraph 4, in line with the description in Recital (97).

- (60) Article 8 of the Proposal describes how to determine the actual market value of cross-zonal capacity for the exchange of balancing capacity. Therefore, the Proposal fulfils the general requirement of Article 41(1)(b) of the EB Regulation with respect to the market value of cross-zonal capacity for the exchange of balancing capacity. ACER made small amendments to the text of Article 8 of the Proposal and deemed it necessary to add several provisions to this article. More detailed descriptions to these amendments can be found in section 6.2.2.4.
- (61) Articles 10, 11 and 12 of the Proposal describe the pricing, the firmness regime and the sharing of congestion income for the cross-zonal capacity that has been allocated for the exchange of balancing capacity or sharing of reserves by the market-based allocation process. Therefore, the Proposal fulfils the general requirement of Article 41(1)(c) of the EB Regulation. However, ACER deemed it necessary to amend these articles of the Proposal to increase the general quality of the text, address the possibility of flow-based capacity allocation and to fulfil the requirement on the equal treatment between the exchange of energy and the exchange of balancing capacity or sharing of reserves, pursuant to Article 41(4) of the EB Regulation. ACER's amendments to these Articles are further described in Section 6.2.2.5.
- (62) Article 6 of the Proposal lists the limits pursuant to the SO Regulation that restrict the maximum volume of allocated cross-zonal capacity for the exchange of balancing capacity or sharing of reserves. However, Article 41(1)(d) of the EB Regulation requires the inclusion of the process to define the maximum volume of allocated cross-zonal capacity for the exchange of balancing capacity or sharing of reserves pursuant to Article 41(2) of the EB Regulation. Therefore, the Proposal does not fulfil the requirement of Article 41(1)(d) of the EB Regulation and ACER amended this article as further described in Section 6.2.2.3.

6.2.2.3. Requirements on the determination of the maximum volume of allocated cross-zonal capacity by the market-based allocation process

- (63) Article 41(2) of the EB Regulation limits the maximum volume of allocated cross-zonal capacity for the exchange of balancing capacity or sharing of reserves which can be allocated by the market-based allocation process. While this limit should generally be at 10% of the available capacity for the exchange of energy of the previous relevant calendar year, this specific limit does not apply if the market-based allocation process is performed not more than two days before the provision of the balancing capacity. In case of this exemption, according to Article 39(6) of the EB Regulation, the relevant regulatory authorities can set another limit than the one specified in Article 41(2) of the EB Regulation after a review on the efficiency of the forecasting method by these regulatory authorities.

- (64) As mentioned above Article 6 of the Proposal lists only the relevant limits foreseen in the SO Regulation, although the Baltic regulatory authorities in their second request for amendment requested that any limits concerning the exchange of balancing capacity or sharing of reserves as determined by the cross-zonal capacity allocation optimisation function shall be clearly defined within the methodology. However, after the amendments of the Baltic TSOs, the specific provisions in the Proposal have not addressed the concerns raised by some regulatory authorities, as according to the referral letter: *“The NRAs have diverging views whether the amended methodology can be approved when only including references to SO GL as a process description instead of including a detailed process to define the maximum volume of allocated capacity or concrete value for maximum capacity.”*
- (65) ACER, taking into consideration the Baltic regulatory authorities’ views expressed in the referral letter, discussed this issue during the consultation process with the Baltic TSOs and regulatory authorities, asking for clarifications on the intention of the Baltic TSOs regarding the exchange of balancing capacity in the region. The Baltic TSOs provided ACER with the ‘Baltic reserve capacity market study’ and the ‘Baltic Load-Frequency Control block concept document’, together with examples in slides describing the concept of the market to be established after the synchronisation of the Baltic synchronous area with the Continental Europe synchronous area, and the expected issues with the procurement of balancing capacity. Any reference to the Baltic LFC Block below should be considered as a reference to the situation after the synchronisation with the Continental Europe synchronous area.
- (66) ACER during the consultation with Baltic regulatory authorities and TSOs proposed a process for the definition of the maximum volume of allocated cross-zonal capacity to the exchange of balancing capacity or sharing of reserves similar to the one described in ACER Decision 22/2020 on the market-based allocation process of cross-zonal capacity for the exchange of balancing capacity for the Nordic CCR, with different values for the maximum volume of allocated cross-zonal capacity, with a default threshold of 20% and further provisions on:
- the possibility that if the 20% threshold is not sufficient to meet the local demand for a standard balancing capacity product in a bidding zone, TSOs shall be allowed to increase this threshold up to 50% if such increase can help address the local shortage of bids;
 - an automatic process describing the possibility of changing the default limit of 20% in case of a structural shortage of Balancing Service Providers’ (‘BSPs’) balancing capacity bids in a bidding zone. Following the market-based allocation process described in this methodology, in case of a structural shortage of bids using the existing default limits such an increase would always lead to an overall increase of the economic surplus. Therefore, this process of increasing the default limit of Article 41(2) of the EB Regulation is following the principle of the requirement for changing the default limit in accordance with Article 39(6) of the EB Regulation; and

- references to any other limits concerning the exchange on bidding zone borders due to the provision of the SO Regulation.
- (67) Based on the ‘Baltic Load-Frequency Control block concept document’, ACER understands that although a single LFC block, the three Baltic countries intend, when performing the dimensioning of the reserves, to take into account also the incidents on the LFC area level (i.e. separately for Estonia, Latvia and Lithuania). Based on the ‘Baltic reserve capacity market study’, the reserves currently located in each LFC area are not always sufficient to cover these dimensioning incidents, hence a “sharing of reserves” concept has been developed (although not being sharing of reserves as described in the SO Regulation Article 168, since it is applied within the same LFC block and not across LFC Blocks), to allow a reduction of the total balancing capacity volume procured in the Baltic LFC Block. The TSOs in their presentation ‘Market based cross zonal capacity allocation for exchange and sharing in Baltic LFC block’, dated 6th April, have included tables with the values of the “FRR needs and accessible volume” for each LFC area, indicating the volume they need for covering each LFC area’s incident, and the volume of balancing capacity that should be available to each LFC area independently of the locally procured one. In the same presentation, TSOs have included net transfer capacity (‘NTC’) values for 2021 in the interconnections between the three Baltic countries. In the example provided in the slides the maximum allocated volume is below 40% of the NTC value.
- (68) During the discussions in the context of this decision making process, the Baltic TSOs proposed to use 70% as limit for Baltic LFC block internal borders (EE-LV, LV-LT) and for the rest of the Baltic CCR borders (EE-FI, SE-LT and LT-PL) they suggested that the maximum volume could be harmonized with other regions, i.e. 10% limit. For the case of the unsatisfied TSO demand (local shortage of bids), the Baltic TSOs proposed to use 80% for the Baltic LFC block internal borders, and for Estonia-Finland, Sweden-Lithuania and Lithuania-Poland they suggested that the maximum volume could be harmonized with other regions, i.e. 20% limit. The Baltic TSOs provided examples indicating the impact of increasing the maximum limit to the reduction of the balancing capacity procurement cost.
- (69) ACER understands that the increase of the exchange of balancing capacity reduces the balancing capacity procurement cost, but this is subject to the accuracy of the forecasted market value for the exchange of energy, since, in the context of the market-based capacity allocation process, the actual market value of the cross-zonal capacity for the exchange of balancing capacity is compared with the forecasted market value of the cross-zonal capacity for the exchange of energy. Pursuant to Article 39(5)(b) of the EB Regulation: *“The forecasted market value of cross-zonal capacity shall be based on [...] the use of a forecasting methodology enabling the accurate and reliable assessment of the market value of cross-zonal capacity.”* Additionally, pursuant to Article 39(6) of the EB Regulation: *“The efficiency of the forecasting methodology pursuant to paragraph 5(b), including a comparison of the forecasted and actual market values of the cross-zonal capacity, may be reviewed by the relevant regulatory authorities. Where the contracting is done not more than two days in advance of the provision of the balancing capacity, the relevant regulatory authorities may, following*

this review, set a limit other than that specified in Article 41(2).” The link between the maximum volume of the allocated cross-zonal capacity and the accuracy of the forecasting methodology for the market value of the cross-zonal capacity for the exchange of energy, is related to the protection of the day-ahead market, since the efficiency of the allocation is subject to the accuracy of the forecasting method.

- (70) Baltic TSOs are in the process of further investigating the cross-zonal capacity allocation methodology, including a study on the forecasted market value for the exchange of energy, and based on the roadmap in Table 27 of the “*Baltic Load-Frequency Control block concept document*” they intend to submit a proposal for amending the current MB CZCA methodology next year. Therefore, ACER suggested in the draft methodology shared with Baltic regulatory authorities and TSOs for the hearing, to introduce (as mentioned above) maximum volume limits for inside the Baltic synchronous area equal to 20% for the default case and 50% in case of local shortage of bids, but also to explicitly specify in the methodology, that before the first application (18 months after the approval of this methodology), an amended proposal should be submitted by the Baltic TSOs with an improved forecasting methodology (together with an assessment on various aspects regarding the accuracy of the new methodology) and subsequently new maximum volume for the allocated cross-zonal capacity (subject to the accuracy of the forecasting method). ACER’s intention is to align this process with the one already scheduled by the Baltic TSOs on the submission of the harmonised rules and process for the exchange and procurement of balancing capacity pursuant to Article 33(1) of the EB Regulation (a proposal is expected in Q3 2022) and the application of this market-based allocation process, following the finalisation of the new forecasting methodology (which is expected by the end of this year).
- (71) As mentioned in section 5.4 both the parties that submitted comments on ACER’s preliminary view, dealt with the maximum volume topic. Ei supports ACER’s position for protecting the day-ahead market from over-allocation to the balancing capacity market and it suggests that a higher volume should be linked with a more precise forecasting methodology (see Recital (27)(a) above), while the Baltic regulatory authorities and TSOs propose amendments to the ACER’s approach (see Recital (26) above).
- (72) In their note the Baltic regulatory authorities and TSOs highlight once more the importance of allowing a higher volume of allocated cross-zonal capacity for the exchange of balancing capacity or sharing of reserves, by providing evidence on the strong link between (a) the reserve dimensioning in Baltic LFC block, (b) the allocated cross-zonal capacity, and (c) the procured volume of the balancing capacity. In the first table of their note, they present the different values for 20% maximum volume of allocated cross-zonal capacity for the exchange of balancing capacity or sharing of reserves, showing the limited potential for sharing reserves and the impact of it on the total procured volume of balancing capacity. In the second table of their note, they present the required volume of allocated cross zonal capacity to ensure sharing and exchange within the Baltic LFC block, from reduced NTC values considering 70% of maximum NTC values (2021 data). Based on their conclusion: “*Considering the*

results provided in the table 2 maximum limit for allocation of cross zonal capacity shall be not less than 50% in order to ensure required volumes for sharing between Baltic areas". It is important to note that ACER understands the concerns expressed by the Baltic TSOs regarding the inability of the LFC areas of the Baltic LFC block to cover their incidents with their local reserves, and to the extent that this considered an operational security issue, it has proposed the maximum volume of the allocated cross-zonal capacity of 50% for the case with local shortage of bids. ACER understands that different LFC areas within an LFC block should ensure that the available reserves can cover any incident in the block, through the geographic distribution of the procured reserves, so in case of an outage the reserve provision stays within the operational security limits. The procurement of balancing capacity could subsequently divert from that distribution by the allocation of cross-zonal capacity. Moreover, it is important to note that ACER has also included an additional provision in Article 7(6) of the Annex I for a fall-back procedure in case of local shortage of balancing capacity to provide additional flexibility to the TSOs to address any issues with operational security limits. However, the cost related aspects of the balancing capacity procurement cannot be the basis of further increase of this limit, as these are linked to the efficient allocation of the cross-zonal capacity, and therefore subject to the limited accuracy of the forecasting methodology for the market value of the cross-zonal capacity for the exchange of energy. The limited accuracy of the forecasting methodology affects also the determination of the direction with the zero market value of cross-zonal capacity for the exchange of energy; thus the proposal by the Baltic regulatory authorities and TSOs for differentiation of the maximum volume of the allocated cross-zonal capacity between the two directions is also subject to a more accurate forecasting methodology.

- (73) As mentioned above, during the consultation on ACER's preliminary view, Ei suggested a separation between the internal Baltic LFC block and the rest of the Baltic CCR borders in case higher than 20% maximum volume is applied (see Recital (27)(a) above), and reiterated this position during the AEWG consultation phase. As explained in Recital (72) above, ACER considers that the level of the maximum limit is linked to the accuracy of the forecasting methodology for the market value of the cross-zonal capacity for the exchange of energy. The current forecasting methodology does not differentiate between borders, nor does it provide any evidence for different performance with respected to its accuracy on a border level. Therefore ACER does not consider that any differentiation on the maximum volume could be justified in this methodology.
- (74) As mentioned above, ACER understands the concerns and supports the Baltic TSOs' choice to proceed with extensive sharing in the LFC block with the aim to have a more efficient procurement of balancing capacity, and also welcomes the transparent approach they have taken with respect to communicating this vision to the market participants. Therefore, ACER's decision to keep these levels of maximum volume of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves should not be understood as blocking this approach. More specifically, ACER considers that the limit of 50%, which applies in case of local shortage of balancing capacity, addresses the operational security concerns, and can be used as an indication

of the balancing capacity that can be shared among the Baltic LFC areas, if there is not sufficient local balancing capacity. On the contrary, the limit of 20%, which is the default limit to be used for the maximum cross-zonal capacity to be allocated to the exchange of balancing capacity, is linked to the efficient functioning of the markets; as such it can only be increased if the Baltic CCR TSOs submit an accurate forecasting methodology for the market value of the cross-zonal capacity for the exchange of energy, which is expected next year.

- (75) In this aspect, ACER highlights that setting a higher maximum limit does not necessarily mean that additional cross-zonal capacity will be allocated for the exchange of balancing capacity or sharing of reserves. The allocation is decided based on efficiency criteria, and the maximum limit is only a constraint to the optimisation problem. Whether the change of the maximum limit will change the outcome of the optimisation problem (i.e. the cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves) depends only on the comparison of the economic surpluses of the two markets: the balancing capacity and the day-ahead one (the two markets “compete” for the same cross-zonal capacity). Therefore, the potential future increase should be accompanied by an additional assessment, with respect to how likely reaching a maximum volume of 70% of cross-zonal capacity allocated to the balancing capacity market would be (given that at this level of cross-zonal capacity allocation to the exchange of balancing capacity, the economic surplus of the day-ahead market is still lower than the one of the balancing capacity market).
- (76) As mentioned above, during the consultation on ACER’s preliminary view, Ei requested a legal analysis for the requirement this Proposal to respect the 70% rule pursuant to Article 16(8) of the Electricity Regulation, and reiterated this position during the AEWG consultation phase. The cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves is regulated pursuant to Articles 38 to 42 of the EB Regulation, and has no implications towards the fulfilment of the requirements pursuant to Article 16(8) of the Electricity Regulation. Specifically, the choice whether to allocate the cross-zonal capacity to the exchange of balancing capacity or sharing of reserves does not in any way impose or restrict the application and enforcement of Article 16(8) of the Electricity Regulation. The latter remains under the full responsibility of regulatory authorities. ACER considers any further legal analysis assessing the 70% rule pursuant to Article 16(8) of the Electricity Regulation as out of the scope of this decision.
- (77) Finally, the Baltic regulatory authorities and TSOs proposed during the hearing to set the deadline for Baltic TSOs to submit an amended methodology to 12 months (instead of the 18 months proposed by ACER), as this would enable Baltic TSOs to amend this methodology simultaneously with the discussions for the development of an EU harmonized cross-zonal capacity allocation methodology, ensuring the needed alignment between the two methodologies and providing a smoother implementation of the EU harmonised methodology in the Baltic CCR. ACER understands that the benefit for adopting this timeline, therefore, it amended this in Annex I.

(78) So ACER has adapted accordingly both Articles 5 and 6 of Annex I to include the process described above for the definition of the maximum volume of the allocated cross-zonal capacity for the exchange of balancing capacity and for the submission of an amended proposal next year.

6.2.2.4. Requirement on the comparison of values of cross-zonal capacity for the market-based allocation process

(79) Article 41(3) of the EB Regulation requires the market-based allocation process to be based on the comparison of an actual value of cross-zonal capacity and a forecasted value of cross-zonal capacity for the two relevant markets, energy and balancing capacity. How these values of cross-zonal capacity shall be calculated is specified in Article 39(1), (3), (4) and (5) of the EB Regulation.

(80) Article 9 of the Proposal describes the determination of the allocated volume of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves, by specifying that the objective function of the process is based on a comparison of the two market values: the actual market value of cross-zonal capacity for the exchange of balancing capacity and the forecasted market value of cross-zonal capacity for the exchange of energy. Therefore, the Proposal fulfils the requirement pursuant to Article 41(3) of the EB Regulation. However, ACER amended Article 9 of the Proposal in order to improve the clarity of the text by inserting new provisions (listing analytically the inputs, the constraints, the objective function and the output of the optimisation algorithm for the allocation of the cross-zonal capacity), deleting non necessary parts and improving the wording and structure of the Article.

(81) Article 7 of the Proposal describes the forecasted market value of cross-zonal capacity for the exchange of energy which is calculated based on the market spread of the reference day. Since the market spread is reflecting the expected differences in market prices of the day-ahead market, the Proposal does fulfil the requirement of Article 39(5) of the EB Regulation related to the comparison of values of cross-zonal capacity for the market-based allocation process. Information on ACER's amendment on Article 7 of the Proposal and the requirements related to the forecasted market value of cross-zonal capacity can be found in section 6.2.3.

(82) Article 8 of the Proposal describes that the actual market value of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves is calculated by considering the economic surplus based on balancing capacity bids and the TSO demand. Therefore, the Proposal fulfils the requirement pursuant to Article 39(3) of the EB Regulation. Since the principle of economic surplus from the exchange of balancing capacity or sharing of reserves is also covering the avoided costs of procuring balancing capacity through the sharing of reserves, the Proposal also fulfils the requirement of Article 39(4) of the EB Regulation. ACER made amendments to the related definitions used in Article 8 of the Proposal, including deleting the definition of market value of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves and introducing the definition of economic surplus for the exchange of balancing capacity or sharing of reserves for enhancing clarity and consistency. Following the consultation with Baltic regulatory authorities and TSOs

and their agreement, ACER further added to Article 8 of the Proposal provisions for the possibilities of a flexible TSO demand and specified that, by default, TSOs shall not put a price on their demand in the market-based allocation process. Besides the possible consideration of an indivisible balancing capacity bid for decreasing the overall procurement costs and for sharing of reserves, ACER also introduced a provision which allows TSOs to optimise their procurement among different products. While on a long-term, ACER deems the inclusion of all relevant bids for different standard balancing capacity products in the same process and the optimisation among them performed at a regional level as the most efficient solution,, ACER allows a step wise approach towards this target, where local efficient solutions can be applied in parallel. Therefore, ACER added an exemption which allows TSOs to link a TSO demand within the marked-based allocation process to firm balancing capacity bids from a parallel procurement process not participating in the marked-based allocation process. To incentivise a first step towards a full integration in the marked-based allocation process, ACER limited such external links to standard balancing capacity products. Moreover, such a link is only possible if lower quality products are substituted, meaning that an automatic frequency restoration reserve ('aFRR') standard balancing capacity product may substitute an mFRR standard balancing capacity product, while the opposite is not possible. In line with Ei's request for further clarification (see Recital (27)(b)), the requirement that follows an aFRR standard balancing capacity product bid is the submission of aFRR standard balancing energy product bids for a certain period, and so is the case for an mFRR standard balancing capacity product bid. Although an aFRR standard balancing energy product bid may be activated in the place of an mFRR standard balancing energy product bid, the opposite is not possible as the characteristics of the aFRR standard balancing energy product bid are technically more challenging (e.g. the full activation time). The relevant added provision in Article 7(4)(b) of Annex I therefore allows TSOs to profit from efficiency gains by linking their demand of two parallel procured standard balancing capacity products (also to outside the market-based allocation process) as long as other TSOs are not ready yet to participate in a balancing capacity cooperation for both standard balancing capacity products. For the needed transparency of such process, ACER added a requirement in Article 12(4) of Annex I to publish the relevant information linked to such increase of a TSO demand. Moreover, ACER deems it necessary to add relevant provisions for cases of insufficient local balancing capacity bids to cover a TSO's demand in Article 7(6) and (7) of Annex I. Since the TSOs' demand should be fixed without the general possibility to introduce price caps, these additional paragraphs describe how the actual market value of cross-zonal capacity for the exchange of balancing capacity or the sharing of reserves should be considered in case of a local shortage of bids. The technical price limit included in the definition is referring to a mathematic maximum for the algorithm to function without having the purpose of limiting price formation. As the TSO demand is inelastic, this technical price limit will only affect the allocation in case of a shortage of local bids to cover the TSO demand even after applying the market-based allocation process. Additionally, ACER added a reference for the provision of a fallback procedure, described under the methodology pursuant to Article 33(1) of the EB Regulation, if a local demand cannot be met after applying the market-based allocation process described in this methodology. ACER also included a provision for setting a technical

price limit for balancing capacity for the sole purpose of calculating the change of economic surplus from the exchange of balancing capacity or sharing of reserves in the explicit case of a simultaneously having a scarcity situation in day-head and having local shortage of bids in the balancing capacity market. This provision was added to address Article 41(4) of the EB Regulation, which requires equal treatment of the cross-zonal capacity allocated for the exchange of energy and for the exchange of balancing capacity or sharing of reserves. Any other amendments related to this requirement can be found in the next section.

6.2.2.5. Requirement on the equal treatment between the exchange of energy and the exchange of balancing capacity or sharing of reserves

(83) Article 41(4) of the EB Regulation requires that the pricing method, the firmness regime and the sharing of congestion income for the cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves via the market-based allocation ensures equal treatment with the cross-zonal capacity allocated for the exchange of energy. Articles 10, 11 and 12 of the Proposal aim to fulfil this requirement

6.2.2.5.1. Firmness regime for the cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves

(84) Article 11 of the Proposal describes the firmness regime for cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves and how to deal with its related costs. The described process in this article does address the requirement of Article 41(4) of the EB Regulation, since it is using the same rules for ensuring firmness and sharing related costs as used for the cross-zonal capacities allocated for the exchange of energy.

6.2.2.5.2. Pricing method for the cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves

(85) Article 10 of the Proposal describes the pricing of cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves. To ensure the equal treatment between cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves and allocated for the exchange of energy in accordance with Article 41(4) of the EB Regulation and establish a process which can also apply to a flow-based allocation environment, ACER deemed it necessary to amend the article on pricing of cross-zonal capacity. The wording of Article 10 of the Proposal was changed to provide a description of pricing principles which is also suitable for the flow-based approach.

6.2.2.5.3. Congestion income for the cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves

(86) Article 12 of the Proposal describes the sharing of congestion income for cross-zonal capacity that has been allocated for the exchange of balancing capacity or sharing of reserves. More specifically, Article 12 of the Proposal includes a 50% -50% sharing

rule for congestion income within the balancing capacity timeframe. Given the possibility of a flow-based capacity calculation in the Baltic CCR (not concluded yet in the Baltic CCR) and the possible issue of missing money for the remuneration of long-term transmission rights, ACER proposed, during the consultation with Baltic regulatory authorities and TSOs, the congestion income to be considered day-ahead congestion income and be shared in accordance with the methodology pursuant to Article 73 of the CACM Regulation. Such approach also ensures equal treatment between the exchange of energy and the exchange of balancing capacity or sharing of reserves, pursuant to Article 41(4) of the EB Regulation.

- (87) Ei in its submission during the hearing requested further clarifications on the process for including the congestion income from the exchange of balancing capacity or sharing of reserves, to the day-ahead congestion income, as mentioned in Recital (27)(c), which reiterated during the AEWG phase. ACER deems that the general principles of the methodology pursuant to Article 73 of the CACM Regulation already provides sufficient details on how to share congestion income of the market-based allocation process to meet the requirement of Article 41(1)(c) of the EB Regulation and does not deem it necessary to explicitly repeat the approach of the existing methodology pursuant to Article 73 of the CACM Regulation in Annex I. However, ACER acknowledges that the methodology pursuant to Article 73 of the CACM Regulation should be amended to consider the congestion income from the market-based allocation process together with the congestion income from the single day-ahead coupling. ACER is of the opinion that the relevant detail on how to amend the methodology pursuant to Article 73 of the CACM Regulation should be addressed in the context of the amendment of the methodology pursuant to Article 73 of the CACM Regulation.
- (88) Following this, ACER considers it sufficient to address the congestion income from balancing capacity per application of the market-based allocation process pursuant to Article 38(1) of the EB Regulation which would be equally applicable for a flow-based and NTC approach. While treating the congestion income from balancing capacity as congestion income from day-ahead will largely address the missing money problem, ACER acknowledges the possibility of a remaining risk of missing money for the remuneration of long-term transmission rights.
- (89) Therefore, ACER proposed in the draft version of the methodology, which was shared with the Baltic regulatory authorities and TSOs during the hearing, that TSOs should assess on an annual basis this risk, performing a comparison between the congestion income from the exchange of balancing capacity or sharing of reserves with the congestion income that could have been generated in case the cross-zonal capacity that has been allocated for the exchange of balancing capacity or sharing of reserves, had been allocated to the day-ahead market. Ei in its submission during the hearing, as mentioned in Recital (27)(c) suggested to change the frequency of this assessment and to also clarify the comparison process, which was further specified in the scope of the consultation of the AEWG as mentioned in section 5.5. ACER proposed the annual basis in order to smoothen the effect of the missing money issue. However, taking into account the input provided during the hearing, ACER changed the

frequency of the comparison to a monthly basis, since this is also considered a sufficient time period for assessing the risk of missing money. During the AEWG consultation phase, Ei requested that the comparison described in Article 11(3) of Annex I should be more specific. ACER would like to clarify its understanding that this comparison should use the actual results of the single day-ahead coupling (i.e. the basis for the remuneration of long-term transmission rights) and consider this price for the cross-zonal capacity in the single day-ahead coupling for the amount of cross-zonal capacity which was allocated for the exchange of balancing capacity and sharing of reserves (i.e. amount of cross-zonal capacity, which may be missing to balance the amount of allocated long-term transmission rights which needs to be remunerated). ACER agrees with Ei that the total impact on cross-zonal capacity of the CCR should be addressed by such comparison and confirms that this is addressed by Article 11(3) of Annex I (ACER understands that in case of flow-based cross-zonal capacity the impact is related to critical network elements and not to individual bidding zone borders)

- (90) Moreover, ACER understands that TSOs allocating cross-zonal capacity for the exchange of balancing capacity or sharing of reserves, may opt for safeguarding themselves against this missing money risk, hence they may take this parameter into account, when allocating the cross-zonal capacity. ACER understands that the missing money for the remuneration of long-term transmission rights in the process of sharing congestion income can have an impact on the costs for the exchange of balancing capacity or sharing of reserves. Therefore, ACER added Article 8(2)(d) to Annex I as well as the related publication provision in Article 12(6) of Annex I.
- (91) While ACER expects the congestion income from balancing capacity to be higher than in day-ahead in most cases due to the application of the mark-up in the forecasted market value of the cross-zonal capacity for the exchange of energy, ACER is of the opinion that the remaining risk should be carried by the TSOs profiting from the exchange of balancing capacity and sharing of reserves as described under Article 11(4) of Annex I: *“the TSOs of a cooperation applying the market based process in accordance with Article 38(1) of the EB Regulation should pay a compensation to the single day ahead coupling to cover such deficit”*. However, since the (flow-based) cross-zonal capacities allocated for the exchange of balancing capacity and sharing of reserves are not exclusively provided by the TSOs applying the market-based allocation process but could also be provided from TSOs outside of this application, ACER is of the opinion that the benefits from the use of this cross-zonal capacities shall be shared among all Baltic TSOs. This is not an issue for the NTC approach, but ACER considers important to make the methodology applicable for both capacity calculation approaches.
- (92) For these reasons ACER replaced Article 12 of the Proposal with Article 11 of Annex I and made the abovementioned amendments in Articles 8 and 12 of Annex I.

6.2.2.6. Requirement on the use of cross-zonal capacity allocated for the exchange of balancing capacity or sharing of reserves

- (93) Article 41(5) of the EB Regulation requires that cross-zonal capacity, which is allocated to the exchange of balancing capacity or sharing of reserves by the market-based allocation process, shall only be used for the associated exchange of balancing energy. Articles 38(4) and (9) of the EB Regulation set further requirements on the use of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves.
- (94) The Proposal addresses these requirements pursuant to Article 38(4) and 38(9) of the EB regulation. However, they were placed in different Articles, not relevant with the content. Therefore, ACER included two paragraphs fulfilling these requirements under Article 3 in Annex I listing, the principles for applying market-based capacity allocation process.

6.2.3. Assessment of the requirements for the forecasted market value of cross-zonal capacity

- (95) Article 39(5) of the EB Regulation sets the requirements on how to determine the forecasted market value of cross-zonal capacity. The forecast shall be based on the differences in day-ahead market prices of the relevant bidding zones. When calculating this forecasted value, additional relevant factors influencing demand and generation patterns in the different bidding zones shall be taken into account. The calculation can either be done by using transparent market indicators that disclose the market value of cross-zonal capacity (Article 39(5)(a) of the EB Regulation) or by using a forecasting methodology enabling the accurate and reliable assessment of the market value of cross-zonal capacity (Article 39(5)(b) of the EB Regulation).
- (96) Article 7 of the Proposal describes a method using the day-ahead market price spread between bidding zones from the reference day. Therefore, the Proposal applies the principle in accordance with Article 39(5) of the EB Regulation and fulfils the requirement to base the forecasted market value on day ahead market price differences between relevant bidding zones. To cope with possible inaccuracy of this method due to short term changes in the demand and generation patterns, Article 7(2) of the Proposal includes a fixed mark-up on the value of the reference day. Even though it is likely that the proposed method can be improved in terms of accuracy, such potential improvements are currently linked to significant uncertainties. Therefore, ACER agrees with further analysis as proposed by the Baltic TSOs, it considers important also the closely monitoring after the implementation, when there is more certainty on the impact of the applied process. To ensure this monitoring process, ACER added a paragraph to Article 12 of Annex I for the provision of a yearly report on the efficiency of the forecasting method by TSOs and an additional preliminary report by 3 months after the initial go-live.
- (97) As mentioned above in section 6.2.2.3, in the context of the discussion for the maximum volume, and in particular in Recital (70), Baltic TSOs are in the process of further investigating the cross-zonal capacity allocation methodology, including a

study on the forecasted market value for the exchange of energy, and based on the roadmap in Table 27 of the “*Baltic Load-Frequency Control block concept document*” they intend to submit a proposal for amending the current MB CZCA methodology next year. Therefore, ACER added a new paragraph in Article 6 of Annex I, where it specifies that before the first application (12 months after the approval of this methodology), an amended proposal should be submitted by the Baltic TSOs with a new forecasting methodology (together with an assessment on various aspects regarding the accuracy of the new methodology).

6.2.4. Amendments necessary to ensure legal clarity and consistency with existing legal provisions

- (98) ACER amended Article 1 of the Proposal to improve the wording, clarify the scope of this methodology and clarify how this methodology can be applied. Further, ACER added the Article 1(6) of Annex I to specify that this methodology applies also to integrated scheduling process bids submitted in central dispatch systems, to the extent they are converted to standard balancing capacity product bids. This added paragraph also replaced related paragraphs in the Proposal addressing the central dispatch system.
- (99) Besides some general improvements of wording, ACER amended Article 2 of the Proposal by:
- deleting the definitions for balancing capacity cooperation, allocation of cross-zonal capacity, use of cross-zonal capacity, release of cross-zonal capacity, market value of cross-zonal capacity for the exchange of energy in SDAC, market value of cross-zonal capacity for the exchange of balancing capacity or sharing of reserves, which are terms either redundant or already used in the EB Regulation;
 - introducing a definition for TSO demand;
 - introducing a definition of economic surplus from the exchange of balancing capacity or sharing of reserves to implement the amendments described in Recital (82);
 - introducing the definitions of the mark-up, the reference day, the positive forecast error, in line with the terms used in Article 7 of the Proposal; and
 - clarifying the reference to cross-zonal capacities.
- (100) ACER deleted Article 5 of the Proposal, which described the process and timeframe of the market-based allocation process, to improve the structure of this methodology and leave the further description of the timeframe to the proposal for application of this methodology pursuant to Article 38(1) of the EB Regulation. The relevant content of the provisions of Article 5 have been moved to other Articles of the methodology (e.g. provisions on gate closure time, as addressed in section 6.2.2.1, to Article 3 of Annex I; provisions for central dispatch, as addressed in Recital (98), to Article 1 of Annex I; parts of Article 5(2) of the Proposal on the cross-zonal capacity allocation process were moved to Article 8 of Annex I)

- (101) Besides the amendments already mentioned in Recitals (54), (56) and (94), ACER further amended Article 3 of the Proposal by adding relevant the provisions on linking in Article 3(6) of Annex I, deleting non relevant content and by improving the wording and further clarifying general principles for applying the market-based allocation process. For ensuring the effectiveness of the market-based allocation process, ACER deemed it necessary to further add a provision under Article 3(7) of Annex I ensuring the compatibility between the cross-zonal capacity allocation function and the capacity procurement optimisation function.
- (102) ACER amended Article 13 of the Proposal to include all necessary publication processes of TSOs applying the market-based allocation process. Hence, ACER added one paragraph regarding the publication of the applicable default limits for the maximum volume of allocated cross-zonal capacity for the exchange of balancing capacity or sharing of reserves on the relevant bidding zone borders and one paragraph describing the requirement for publishing an annual report to assess the efficiency of the forecasting method, including a description of the content of such report.
- (103) Besides the explicitly mentioned amendments, ACER provided some additional amendments to improve the wording, clarity and structure of the Proposal and deleting out of scope passages.

6.2.5. Assessment of the requirements for consultation, transparency and stakeholder involvement

6.2.5.1. *Consultation and involvement of stakeholders*

- (104) When drafting the Proposal, the TSOs aimed at addressing the requirements from Article 10 of the EB Regulation regarding the involvement of stakeholders.
- (105) As indicated in Recital (6) above, the TSOs fulfilled the requirements of Article 10(4) of the EB Regulation, since stakeholders were consulted on the draft of the first proposal pursuant to Article 10(1) of the EB Regulation. This involvement took place during a public consultation, which ran from 4 October 2019 to 4 December 2019. In addition, the regulatory authorities were regularly informed and consulted pursuant to Article 10(1) of the EB Regulation. The justifications regarding the consideration given to the views expressed by stakeholders during the public consultation in the drafting of the Proposal were provided in a separate document and submitted to the regulatory authorities.

6.2.5.2. *Publication and transparency*

- (106) The Proposal fulfils the requirements on publication and transparency in accordance with Article 7 of the EB Regulation, as pursuant to Article 14 of the Proposal the Baltic TSOs shall publish this methodology for market-based capacity allocation after its approval.
- (107) Moreover, Article 13 of the Proposal summarises the publication requirements related to the market-based allocation. The provided deadlines and timings in this article are

meeting the requirements of Article 12 of the EB Regulation. However, ACER introduced amendments to this article to improve the wording, provide more clarity on publication processes and added several provisions to ensure sufficient transparency of the market-based allocation process and allow for sufficient possibility of monitoring the effectiveness of this process.

- (108) During the discussion with all regulatory authorities in the framework of the AEWG, as mentioned in section 5.5, the regulatory authorities of Denmark and Sweden proposed to add a publication requirement for monitoring the impact cross-zonal capacity allocation for the exchange of balancing capacity and sharing of reserves has on the price formation on the single day-ahead coupling market. Such provision should allow for better supervision regarding cases of misconduct in bidding behaviour of market participants with market power. ACER agrees and added the relevant requirement in Article 12(8)(c) of Annex I.

7. CONCLUSION

- (109) For all the above reasons, ACER considers the Proposal in line with the requirements of the EB Regulation, provided that the amendments described in this Decision are integrated in the Proposal, as presented in Annex I.
- (110) Therefore, ACER approves the Proposal subject to the necessary amendments and to the necessary editorial amendments. To provide clarity, Annex I to this Decision sets out the Proposal as amended and approved by ACER,

HAS ADOPTED THIS DECISION:

Article 1

The market-based allocation process of cross-zonal capacity for the exchange of balancing capacity for the Baltic CCR in accordance with Article 41(1) of Regulation (EU) 2017/2195 is adopted as set out in Annex I to this Decision.

Article 2

This Decision is addressed to AS Augstsprieguma tīkls, Elering AS, Fingrid Oyj, Litgrid AB, Polskie Sieci Elektroenergetyczne S.A. and Svenska kraftnät.

Done at Ljubljana, on 13 August 2021.

- SIGNED -

*For the Agency
The Director*

C. ZINGLERSEN

Annexes:

- Annex I Methodology for the market-based allocation process of cross-zonal capacity for the exchange of balancing capacity for the Baltic CCR pursuant to Article 41(1) of the Electricity Balancing Regulation
- Annex Ia Methodology for the market-based allocation process of cross-zonal capacity for the exchange of balancing capacity for the Baltic CCR pursuant to Article 41(1) of the Electricity Balancing Regulation (track-change version, for information only)
- Annex II Evaluation of responses to the public consultation on the cross-border capacity allocation methodologies for the exchange of balancing capacity in the Hansa, Core and Baltic regions (for information only)

In accordance with Article 28 of Regulation (EU) 2019/942, the addressees may appeal against this Decision by filing an appeal, together with the statement of grounds, in writing at the Board of Appeal of the Agency within two months of the day of notification of this Decision.