

Ukraine Energy Market Observatory

Assessment 1/23

Analysis of Resolution 1689 of NEURC of 17 December 2022 on the settlement of urgent issues of ensuring security of supply and prevention of an emergency situation in the energy system of Ukraine

Introduction

The present assessment follows an informal request of the Ukrainian Energy Regulator National Commission for State Regulation in the Spheres of Energy and Communal Services (“NEURC”) towards the decision taken by NEURC on December 17, 2022 regarding introduction of the emergency situation in the electricity market of Ukraine. The request was received after the decision was taken.

Background

According to the Electricity Market Law¹ the activities of electricity market participants and the relations between them shall be governed by the regulatory legal acts governing implementation of the Law, in particular the Market Rules, the transmission network code and commercial metering code which shall be developed and administered by the transmission system operator NJSC Ukrenergo (“TSO”) and the “Day-ahead” and “intra-day” market rules (“DAM/IDM Rules”) to be developed and administered by the market operator. All these acts are approved by NEURC.

The functioning of the electricity system and market during emergency situations is governed by the Electricity Market Law, the Electricity Market Rules, the DAM/IDM Rules and the Transmission Network Code:

- ✓ The Electricity Market Law envisages that in cases of threat to security of supply,² the TSO may announce an emergency based on technical criteria specified in the Transmission Network Code (Article 16, part 6). Market participants are obliged to follow the TSO’s operational commands in such case.
- ✓ The Electricity Market Rules prescribe the relevant procedure. They provide that in the event of an emergency, imbalance settlements and balancing electricity are priced at historical average of upward- and downward regulation prices (Section IX, Articles 9.1. and 9.2., item 9.2.1). The Rules provide for compensation to market participants in case the emergency lasts more than 24h.
- ✓ The DAM/IDM Rules require the suspension of auctions on the IDM (but not of the DAM) following an emergency announced by the TSO (Article 1.9., part 1.9.3).
- ✓ The Transmission Network Code provides the technical criteria/organizational and communication aspects of announcing emergency in the system (Sections VIII, XI).

¹ Law No.330-IX of 04.12.2019, as amended, Article 2, part 2.

² Emergency in UES of Ukraine is defined by the Electricity Market Law as a situation, at which there is a threat of UES functioning regime (Article 1 item 45). According to Article 16(6) of the Electricity Market Law, “in case of violation of security of supply leading to emergency, the TSO introduces emergency based on technical criteria of the Transmission Code”.

In November 2022 NEURC has published a set of draft amendments to the Electricity Market Rules, DAM/IDM Rules and the Transmission Network Code related to the suspension of operations on the electricity market and the functioning of the market in the event of an emergency situation in the UES of Ukraine. These amendments have not been approved by NEURC and have not been consulted with the Secretariat.

On 25 February 2022, immediately after the introduction of martial law by the Decree of the President of Ukraine No. 64/2022, NEURC adopted Resolution No. 332³ that governs the functioning of the electricity market during martial law and 30 days thereafter. This Resolution does not amend or replace the Electricity Market Rules, the DAM/IDM Rules, the Network Codes or other legislative or regulatory acts which remain in force during the duration of martial law. However, in case of divergence, the provisions of Resolution No. 332 prevail.

The adoption of Resolution No.332 did not follow the established procedure for adoption of regulatory acts such as market rules and network codes stipulated in Articles 14 and 15 of the NEURC Law and NEURC's Resolution No.2133 of 6 December 2016. The document lacks a legal basis and does not contain a reference to any article from the legislation in force. It only stipulates that it is adopted in accordance with the Electricity Market Law, the NEURC Law in connection with the introduction of martial law in Ukraine. Hence, Resolution No.332 and its subsequent amendments have not been put for public consultation and were published only three days prior to approval, or less.

On 17 December 2022, NEURC adopted Resolution No. 1689 on Amendments to NEURC Resolution of 25 February 2022 No.332 ("Resolution No. 1689") which introduces a special regime for the electricity market functioning in cases when an emergency situation was declared by the TSO. In particular, Resolution No. 1689 stipulates that NEURC gives "guidance"⁴ to the transmission system operator (TSO) in its capacity as Settlement Administrator in such cases to immediately suspend the markets for bilateral contracts (forward market) and offers accepted by the TSO in the balancing market. NEURC also gives guidance to the Market Operator ("MO") to suspend day-ahead (DAM) and intra-day (IDM) transactions for the duration of the emergency situation. Before the adoption of Resolution No. 1689, emergency suspension was envisaged only for the IDM. As a consequence, only the balancing market will remain intact. That means that all electricity will be traded on the balancing market (operated by the TSO). Resolution No. 1689 further stipulates that electricity on the balancing market is traded at the average day-ahead market price of the preceding 30 days.

NEURC describes the objective of Resolution 1689 as to minimize the total cost of energy trading at times of system emergencies. There is no assessment provided as to whether this would be the most efficient solution rather than maintaining the DAM or IDM with restrictions and regulated prices. In its substantiation to Resolution 1689, NEURC references a proposal from the TSO (letter No 01/56550 of December 15, 2022) to that effect. The provisions of Resolution No. 1689 have been published on 16 December 2022 in the evening and adopted in the morning on 17 December 2022 without any prior public consultation with the market participants.

On top of the Market Rules, DAM/IDM Rules and the Network Code in force, Resolution 1689 stipulates:

- Delayed payment to electricity market participants trading in the DAM by the Market Operator during martial law, not limited to the emergency situation. According to Article 4.3 of the DAM/IDM Rules, settlements of the Market Operator with sellers of energy is to be done until 15:45 D-1, i.e. on the day of a deal at DAM, which is one day preceding the physical supply. Resolution No. 1689 postpones this time for 2 days, stipulating that such payment shall take

³ NEURC Resolution No.332 on ensuring stable functioning of the electric energy market, including the financial condition of participants in the electric energy market during the period of martial law in Ukraine, dated 25.02.2022.

⁴ The term "guidance" is used by the NEURC in the text of Resolution No.332 and its amendments, but this does not change the fact that these documents as Resolutions adopted by the regulatory authority are legally binding acts.

place “the day following the day of supply”, i.e. D+1 following physical supply. So the Market Operator will be allowed to take money from buyers (both DAM and IDM) at D-1 and keep it for 2 days on its account (not only during emergency situations).

- NEURC’s guidance to the Settlements Administrator (the TSO) to enact the emergency regime described above, including
 - ✓ cancel registered volumes in the bilateral (forward) market as well as accepted offers in the balancing market during the emergency period,
 - ✓ exclude electricity volumes traded during the emergency from the basis for calculating collaterals (financial guarantees) by the TSO in the balancing market, i.e. the only remaining market for the trade of electricity. This is meant to avoid excessive burden on market participants,
 - ✓ give settlements for trade during the emergency period (in the balancing market) priority over other payments, by the TSO as Settlements Administrator executing payments between market participants during the emergency period first. Settlements of contracts between market participants before the emergency period are second-ranked;
- Guidance to the Market Operator (the MO) to:
 - ✓ cancel the results of auctions on DAM and IDM starting on the day on which an emergency was announced. By contrast, the DAM/IDM Rules in Article 1.9.3 stipulate that in the case of system emergency only the IDM should be stopped.
 - ✓ not conduct any further auctions at DAM/IDM starting with the announcement of emergency.
 - ✓ return funds (contracted volume x price on D-1) to market participants for cancelled volumes of trade at DAM due to emergency.
- Additionally, Resolution 1689 regulates that settlements in the balancing market (the only one functioning during emergency) are made at the historical (proceeding 30 days) DAM price. This differs from Article 5.14.5 of the Market Rules, which envisages no price regulation under normal circumstances, as well from Article 9.2.1 which regulates the imbalance price during emergency market suspension at the level of the historical average of the upward/downward regulation prices. NEURC Resolution 413 of April 26, 2022 (amending Resolution No. 332) had already introduced a price cap on balancing energy corresponding to the (actual) DAM price + 20%. Resolution No. 1689 essentially deletes this premium.

Impact on market participants

So far, an emergency in the market was declared only once following emergency declared by the TSO on 17 December for less than 24h. A similar operational emergency has been previously announced by the TSO on 23 November 2022 and resulted in cancellation only of the IDM under the DAM/IDM Rules.⁵

Individual financial effects on market participants resulting from introduction of the new emergency regime introduced by Resolution No. 1689 cannot be evaluated since no public data is available. It may be assumed, however, that the reason for introduction of the proposed regime was to minimize total costs of transactions in the electricity market. Under normal conditions of market operation, the unexpected loss of load due to a technical emergency would result in sharp increase of imbalances, which are priced highest among all other market segments.

The new regime will improve the situation of large generation companies which have to decrease their production in emergency situations but have sold the electricity already commercially. In the case of a decrease of output due to emergency, other companies produce electricity that was already sold commercially by the affected generators in the forward market or DAM. In this case, affected

⁵ <https://ua.energy/zagalni-novyny/do-uvagy-uchasnykiv-rynka/> <https://www.oree.com.ua/index.php/newsctr/n/17306>

companies currently incur additional costs for imbalances at balancing market prices (capped at DAM + 20%), which was decreased under Resolution No. 1689.

On the other hand, balancing services providers are paid for balancing energy under the conditions of market emergency at lower (DAM) instead of higher (DAM +20%) prices. Suppliers and consumers would have to pay again for physically produced energy to TSO in the balancing market during emergency, although they already contracted and paid to other generators and suppliers in the bilateral (forward) market and DAM/IDM, all of which are suspended during the market emergency regime. The compensation of suppliers or consumers for losses due to the suspension of the markets is not addressed by Resolution 1689.

Compliance assessment

In Energy Community law, Articles 35-39 of Commission Regulation (EU) 2017/2196 of 24 November 2017 establishing a network code on electricity emergency and restoration (the “ERNC”) govern the suspension of electricity market activities. The ERNC was only incorporated in the Energy Community acquis on 15 December 2022⁶ and has not been transposed by Ukraine yet. The deadline is 31 December 2023. While, generally speaking, the suspension of market activities in emergency situations, as stipulated by Resolution No. 1689, is in line with Articles 35 et seq. of the ERNC Article 4(2) of the ERNC, requires that such rules are developed by the TSO and submitted to the regulatory authority for approval. The development and adoption of Resolution No. 1689 by NEURC would thus not be in line with Article 4(2) of the ERNC.

Under the currently applicable legal framework of the Energy Community, the adoption of Resolution No. 1689 (as already the basic Resolution No.332 of 25 February 2022) may affect legal certainty. Following the case law by the European Court of Justice, the principle of legal certainty is binding on Contracting Parties’ authorities when acting in the scope of the Energy Community rules.⁷ The principle requires that national rules such as Resolution No. 1689 are known, clear, precise, stable, certain and predictable for those subjected to it,⁸ in particular if they entail negative financial consequences.⁹ The adoption of special and ad hoc rules by the regulatory authority outside the established legal framework (governed by the Market Rules, the DAM/IDM Rules and the Transmission Network Code), and partially overwriting these established rules, affects the unity of the legal order in Ukraine and encroaches upon legal certainty for those subjected to it. This adverse effect is intensified by the fact that Resolution No. 1689 has been adopted in a fast-track procedure and without consultation. Since all rules (Market Rules, DAM / IDM Rules and Transmission Network Code), as well as Resolution No.332 as amended by Resolution No.1689 apply in parallel, the market participants may not have a clear and precise understanding of their respective rights and obligations.

At the same time, any compliance assessment needs to take into account the special circumstances following the frequent attacks by Russian forces on electricity generation and infrastructure facilities. This situation, addressed by the introduction of martial law in Ukraine, has drastically increased the possibility of emergency situations, which requires fast responses for which legal certainty cannot be the only guiding principle. This is reflected in the recommendations and conclusions below.

⁶ Ministerial Council Decision 2022/03/MC-EnC of 15 December 2022 on the incorporation of Regulation (EU) 2019/942, Regulation (EU) 2019/943, Regulation (EU) 2015/1222, Regulation (EU) 2016/1719, Regulation (EU) 2017/2195, Regulation (EU) 2017/2196, Regulation (EU) 2017/1485 in the Energy Community acquis, amending Annex I of the Energy Community Treaty, and on the amendments of the Ministerial Council Decisions No 2021/13/MC-EnC and No 2011/02/MC-EnC

⁷ C-487/01 and C-7/02, *Gemeente Leusden and Holin Groep*, EU:C:2004:263, para. 57; C-376/02, *Goed Wonen*, EU:C:2005:251, para. 32; C-181/04 to C-183/04, *Elmeke NE*, EU:C:2006:563, para. 31.

⁸ Case C-183/14, *Radu Florin Salomie and Nicolae Vasile Oltean v Direcția Generală a Finanțelor Publice Cluj*, ECLI:EU:C:2015:454.

⁹ C-325/85, *Ireland v Commission*, EU:C:1987:546, para.18

Conclusions and recommendations

With the introduction of martial law, the legislative and regulatory framework in Ukraine had to be adapted to the conditions of war. Both primary and secondary legislation has been amended during 2022. Amendments to the rules in place (Market Rules, DAM / IDM Rules and Transmission Network Code) follow an established procedure, including consultation with the market participants. The amendment of this set of rules would have been the appropriate way forward to introduce a new emergency regime such as the one created by Resolution No. 1689. The parallel structures resulting from the adoption of Resolution No. 1689 affect legal certainty.

It is recommended that even under conditions of martial law, NEURC finalizes the draft amendments to the Market Rules, the DAM/IDM Rules and the Transmission Network Code in the proper procedure, and subsequently repeals Resolution No.332 as amended by Resolution No.1689. It is further recommended that these amendments are aligned with the ERNC as much as possible.

Alternative proposals to that of Resolution 1689 to be considered could involve an approach of minimization of the size of commercial imbalances during technical emergency. A special settlements regime during the times of emergencies could be considered, involving, inter alia, the following aspects towards minimization of impacts of the balancing mechanism:

- a) suspension of operation of all balancing groups and introducing one balancing group under TSO in order to offset imbalances for purposes of settlements during hours of emergency;
- b) correction of market participants' positions in all market segments retrospectively by factual volumes of consumption and production during emergency hours;
- c) placing a regulated price on imbalances after minimization of their volume in combination with measure b) above.

The advantage of this approach would be that the market model remains in place but the settlements mechanism is adjusted to minimize the risk of uncontrolled imbalances and resulting financial burden caused by technical emergency.

If the approach to cancel/suspend all market segments is maintained, the Resolution should provide that revenues by sellers in the forward (bilateral) market are returned to their counterparties on the day of introduction of the emergency regime. Thus buyers and consumers of electricity could pay to generators during the emergency regime or recover funds for non-consumed electricity.

Artur Lorkowski

Dirk Buschle

Annex 1. Full Text of NEURC Resolution No. 1689

NATIONAL STATE REGULATORY COMMISSION IN THE SPHERES OF ENERGY AND PUBLIC SERVICES

RESOLUTION

12/17/2022 No. 1689

“On making changes to the resolution of the NEURC of February 25, 2022 No. 332”

In accordance with the laws of Ukraine "On the electric energy market" and "On the National Commission carrying out state regulation in the spheres of energy and communal services", in connection with the martial law in Ukraine, introduced in accordance with the Decree of the President of Ukraine dated February 24, 2022 No. 64/2022 and extended by the Decrees of the President of Ukraine dated March 14, 2022 No. 133/2022, dated April 18, 2022 No. 259/2022, dated May 17, 2022 No. 341/2022, dated August 12, 2022 No. 573/2022 and dated 07 No. 757/2022 of November 2022, taking into account the letter of NEC "Ukrenergo" dated December 15, 2022 No. 01/56550, the National Commission for State Regulation in the Energy and Utilities Sector DECIDES:

1. To include in the resolution of the National Commission, which carries out state regulation in the fields of energy and communal services, dated February 25, 2022 No. 332 "On ensuring the stable functioning of the electric energy market, including the financial condition of participants in the electric energy market during the period of war status in Ukraine" the following changes:

1) paragraph 1 shall be supplemented with a new sub-paragraph of the following content:

"22) The MO (Market Operator) shall provide the authorized bank with payment directions for payment orders for the transfer of the sums of funds determined as the obligation of the MO to pay for the electric energy purchased during trading, from the current account with a special mode of use of the OP until 3:30 p.m. of the day following the day of supply";

2) paragraph 2 shall be amended as follows:

"2. On trading days *d*, on which the United Energy System of Ukraine (hereinafter “UES of Ukraine”) is in an emergency situation, provide the following guidance (укр. - “настанови”) to:

1) the TSO (in the role of Settlement Administrator):

to cancel the volumes of electric energy registered under bilateral contracts and accepted offers for balancing electric energy of BSS (Balancing Services Supplier) starting from the day on which the TSO has announced the occurrence of an emergency situation in the United Energy System of Ukraine, and until the first day (inclusive) after the announcement by the TSO to end the emergency situation in the UES of Ukraine.

Regardless of the duration of the emergency situation in the UES of Ukraine, starting from the day on which the TSO announced the occurrence of an emergency in the UES of Ukraine, and up to the first day (inclusive), after the TSO announced the end of the emergency situation in the UES of Ukraine, when calculating the imbalance payments, apply the value of the arithmetic mean of DAM (day ahead market) price as formed in the corresponding settlement period during the previous 30 days, during which the UES of Ukraine was not in an emergency situation.

Withdrawal/accruals for electricity imbalances for BRP (balance responsible party) on trading days *d*, starting from the day on which the TSO announced the occurrence of an emergency situation in the UES of Ukraine, and until the first day (inclusive), after the TSO announced the termination of the emergency situation in the UES of Ukraine, is carried out at the price calculated in accordance with this sub-item;

ensure the formation and billing of electricity imbalances for trading days d , starting from the day on which the TSO announced the occurrence of an emergency situation in the UES of Ukraine, and up to the first day (inclusive), after the TSO announced the termination of the emergency situation in the UES of Ukraine, not later than the fourth working day, following the announcement by the TSO on the termination of the emergency situation in the UES of Ukraine;

when calculating the value of the maximum amount of electrical energy imbalance for mp market participants, who are part of the balancing group of BRP gr , for one day in the previous 30 days before the trading day d ($Wimbgr, d, z$), not to use the value of the amount of electricity imbalance for market participants mp , which are included in the balancing group of the BRP gr , which was formed on each of the trading days d , starting from the day on which the TSO announced the occurrence of an emergency situation in the UES of Ukraine, and until the first day (inclusive), after the OSP announced the termination of the emergency situation in the UES of Ukraine;

as a priority and until the full fulfilment of the financial obligations of the TSO, which arose from the day on which the TSO announced the occurrence of an emergency situation in the UES of Ukraine, and until the first day (inclusive), after the announcement by the TSO on the termination of the emergency situation in the UES of Ukraine, to direct funds, received on current accounts with a special TSO usage regime;

2) MO

cancel the results of auctions on DAM and IDM on the day of supply, in which the UES of Ukraine is in an emergency situation;

to return to the participants of the DAM/IDM, the purchase volumes of which were accepted based on the results of the auctions on the DAM and IDM and which then were cancelled, the amount of funds, which is determined as the product of the accepted purchase volume on the DAM and IDM by the price of the corresponding accepted volume;

not to conduct auctions on the DAM;

not to conduct auctions on IDM starting from the day on which the TSO announced the beginning of the emergency situation in the UES of Ukraine and until 23:00 on the first day (inclusive), after the TSO announced the termination of the emergency situation in the UES of Ukraine."

3. This resolution enters into force on the day of its adoption.

Head of the NEURC, K. Uschapovskyi