



The Creation of Regional Electricity Markets

An EREG Conclusions Paper

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Executive Summary

EREG in June 2005 published its consultation paper *The Creation of Regional Electricity Markets* and sought views. The paper discussed and sought to identify priority areas for further action in order to facilitate trade between national markets and so allow the development of regional and pan-EU markets. The paper identified four action areas :

- ◆ availability of transmission capacity
- ◆ availability and control of information
- ◆ co-operation between network operators
- ◆ compatibility of wholesale market arrangements

The paper also noted the importance of the role and commitment of government and regulators in putting in place the necessary arrangements to deal with these areas.

EREG received eleven responses to the consultation paper. Respondents included Transmission System Operators, electricity wholesale market participants, and government. Broadly speaking, respondents' comments highlighted many of the issues identified in the consultation paper. Most agreed on the importance of addressing the four priority areas, and the need for government and regulatory commitment. Opinions differed on the extent of the need for harmonization of arrangements between national markets, and the extent of the need for new or duplicate regulation. Some respondents called for a more detailed action plan and timetable in order to progress market integration in a concrete and timely manner.

This EREG conclusions paper summarizes and considers these responses, and sets out next steps for action in order to make concrete progress in integrating electricity markets. Where appropriate, EREG sets out where its first view as expressed in the consultation paper may have been changed or revised in the light of respondents' comments. This conclusions paper therefore complements rather than replaces the consultation paper.

In the light of responses overall, EREG concludes and confirms that it will be appropriate to pursue the priority areas for further action noted in its consultation paper. The 2006 work programmes for EREG and the parallel regulators' group CEER reflect these priority areas. Work will be undertaken for example in order to put forward Guidelines for Good Practice on electricity balancing markets integration and also on Transparency and Information Management. Other work will concern cross border access and investment issues, transmission charging, and the cross border legal and regulatory environment.

Furthermore, in order to make concrete progress in identifying and removing barriers to trade and so integrating markets in the immediate future, EREG proposes that relevant regulators, working with relevant stakeholders, take forward work in each region. This work would include establishing for each region a Regional Co-ordination Committee comprising regulators for the region's national markets.

EREG anticipates a process to include full involvement and consultation of stakeholders, including the European Commission, Member State governments, TSOs, and market participants. Such a process is intended to complement, and not duplicate, existing well established frameworks, initiatives, and national government efforts to integrate markets.

The overall objective would be to make concrete progress within a specified timetable on market integration within each region. Among other things, this timetable would anticipate a further round of mini-fora, starting in spring 2006.

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1 Introduction

Purpose of paper

- 1.1. The aim of ERGEG, the European Commission, and others, is to work towards the creation of a single, efficient and effectively competitive electricity market, while at the same time ensuring security of supply and system reliability. As noted in the European Commission's March 2004 Strategy Paper¹ and elsewhere, it is anticipated that the integrated single market will be reached via the interim step of the establishment and further development of a number of regional markets. Regions or markets would in due course become more closely integrated and so approach the single market paradigm.
- 1.2. ERGEG supports this approach. Accordingly, ERGEG in June 2005 published a consultation paper² on the creation of regional electricity markets and invited comments by 31 August 2005. The consultation paper set out ERGEG's first view of the main obstacles to effective interaction and trade across borders which will need to be addressed in order to establish regional markets.
- 1.3. The paper noted the overall aim of the European Commission, regulators, and others to work towards the creation of a single, efficient and effectively competitive electricity market, and that a pragmatic way of reaching this would be via the interim step of the establishment and further development of a number of regional markets. Each regional market would be a grouping of countries where market arrangements are relatively strongly harmonized, and based on strong underlying physical, institutional, and political links. This regional approach would facilitate addressing the complex problem of knitting together all national markets, since for example each region would be a sub-set of all Member States, and local issues could be more easily assessed and addressed. Regions or markets would in due course become more closely integrated and so approach the single market paradigm.
- 1.4. This paper considers the comments received and sets out ERGEG's conclusions on the issues raised in its consultation paper. Where appropriate, ERGEG sets out where its first view as expressed in the consultation paper may have been changed or revised in the light of comments from respondents. This paper also sets out next steps for action in order to make concrete progress in integrating electricity markets. This includes establishing regional initiatives to tackle market integration issues for each region.
- 1.5. This conclusions paper therefore complements rather than replaces the consultation paper.

¹ *Medium term vision for the internal electricity market* March 2004 European Commission

² *The creation of Regional Electricity Markets An ERGEG Discussion Paper for Public Consultation* 8 June 2005 ERGEG

Recap of ERGEG Consultation Paper

- 1.6. Two broad market design groups were considered in developing ERGEG's first view : network operations and wholesale market arrangements. In addition, the paper also analyzed some broader questions relating to regulation across a regional market and interactions between markets. This analysis was supplemented with 'case studies', that is, experience from a number of existing regional initiatives.
- 1.7. The consultation paper came to the initial view that four broad categories of issues exist where further action may be required for delivery of a regional market :
 - availability of transmission capacity
 - availability and control of information
 - co-operation between network operators
 - compatibility of wholesale market arrangements
- 1.8. The consultation paper also noted the important role of regulators and government required to deliver change to national markets and so facilitate trade between them. For example regulatory competences might be needed 'cross border' in order to oversee cross border investment and monitor market activity.
- 1.9. Recommendations for next steps were also made. It was proposed that regional groups of regulators develop case studies of the priority issues to be addressed, using the issues highlighted in the consultation paper as a checklist. It was intended that these 'case studies' be an active development and integration of markets by the involved regulators. In addition, ERGEG proposed that CEER give consideration to governance arrangements that should apply to the development of these case studies.
- 1.10. In the light of the analysis, initial views and recommendations for next steps in the consultation paper, ERGEG invited comments from interested parties, in particular regarding the following elements :
 - the key market design features that may need to be addressed in creating a regional market
 - the possible need for an overarching regional framework through which interaction across a regional market would be organised and regulated
 - the role of regulators and governments in delivering regional electricity markets
 - the proposed process for taking forward work on the creation of regional markets, in particular:
 - o the use of practical case studies through which the detailed issues for delivery of particular regional markets can be assessed, noting that the issues faced may vary depending on the national markets included within a region
 - o the use of the existing mini-fora regions as a basis for these case studies (with other 'regional groupings' being taken forward where countries agree) and the proposed involvement of member state governments, the Commission, regulators, TSOs, market operators and market participants in taking this work forward

Responses received

- 1.11. EREG received 11 responses to its consultation paper. Five responses were from Transmission System Operators or organisations representing them. Three were from organizations representing national or European electricity market participants. One was from an organization representing national electricity generators. One was from a market participant with interests at all levels of the electricity supply chain. One was from a representative of government. Responses therefore spanned the geographic and industrial structure of the EU electricity market.
- 1.12. The respondents were :
- Association of Austrian Electricity Undertakings (VEÖ)
Organization representing Austrian electricity market participants' interests
 - Association of Electricity Producers (AEP)
Organization representing UK retailers' interests
 - Austrian Power Grid (APG)
 - Eurelectric
Organization representing electricity market participants across EU
 - European Transmission System Operators (ETSO)
 - German Association of Network Operators (VDN)
Organisation representing the 4 German TSOs and in large part German DSOs
 - Nordel
Organisation of TSOs in the Nordic countries (Denmark, Finland, Norway, Sweden)
 - RWE AG
 - Scottish and Southern Energy (SSE)
UK energy retailer
 - Swiss Federal Office of Energy (SFOE)
Swiss government department responsible for energy
 - Union for the Co-ordination of Transmission of Electricity (UCTE)
- 1.13. Copies of these responses are available on the EREG website.

Relevant recent developments

Florence Forum

- 1.14. The 12th Florence Forum of September 2005 devoted a session to the development of regional markets. In particular it noted some good results from the round of the 'mini-fora' held over the 2004/05 winter, although it noted that further progress remains to be made. The Forum also received and welcomed a presentation by EREG of the EREG consultation paper and the idea for regional initiatives.

- 1.15. As a result, the Forum in its conclusions “stressed the need for increased and accelerated harmonisation or compatibility of rules, as well as national legislation, and involvement of and cooperation between governments and between governments and regulators in the development of regional markets” and “confirmed the importance of different regional activities and Mini-fora, and welcomed the results achieved so far. While praising single and pragmatic approaches on a case by case basis, the Forum underlined the need to monitor progress and compatibility of regional solutions, in the perspective of a single EU market.” It called for a further development of regional markets and a new round of mini-fora for spring 2006.
- 1.16. In addition, and in the context of regional market development, participants at the Forum highlighted the need for increased market transparency. ETSO and Eurelectric therefore promised to provide by November 2005 lists of relevant data items needed to ensure an optimal use of the existing infrastructure and for market agents to trade efficiently, particularly with respect to interconnectors spanning borders.

DG TREN and DG Competition reports

- 1.17. DG TREN in November 2005 reported on progress in creating the internal gas and electricity market. DG TREN is required under the terms of the electricity Directive 2003/54/EC and Gas Directive 2003/55/EC to report on progress.
- 1.18. Also in November 2005, DG Competition published its first report – the *Issues Paper* - on its energy (gas and electricity) sector inquiry. DG Competition in June 2005 launched sectoral investigations into the gas and electricity sectors because of concerns over rises in gas and electricity wholesale prices and complaints about barriers to entry and limited customer choice. The inquiry has a legal basis in Article 17 of Regulation 1/2003.
- 1.19. DG TREN and DG Competition found that, among other things, progress in reaching the single market is impeded by a lack of market integration. That is, trade between national markets is impeded because there is for example insufficient interconnection infrastructure between them, or existing infrastructure is inadequately available. Furthermore differences in market designs in adjacent markets are also seen to impede trade.

Legal framework for congestion management

- 1.20. On 25 January 2006, the Electricity Cross-border Committee met for the first time in order to fulfil the ‘Comitology’ procedure necessary to approve the Congestion Management Guidelines based on Art. 8 of Regulation 1228/2003. These guidelines require a regional approach where necessary. The Committee is due to meet again in March 2006 with a view to completing the ‘Comitology’ procedure. It is presently anticipated therefore that, if adopted by the Comitology Committee, these Guidelines will come into force during 2006.

Directive concerning Security of electricity supply and Infrastructure investment

- 1.21. In January 2006, a Directive 89/2006 concerning measures to safeguard security of electricity supply and infrastructure investment was adopted. Among other things, the Directive establishes measures aimed at ensuring an appropriate level of interconnection between Member States for the development of the internal market. Measures also include provisions related to ensuring operational network security and appropriate network investment, taking into account relevant market actors and TSOs

in the relevant connected countries. Member States in addition may require TSOs to provide information on investments related to the building of internal lines that materially affect the provision of cross-border interconnection.

- 1.22. Such measures are clearly linked to, and designed to complement, market integration, the creation of regional electricity markets, and the development of the single market.

Structure of conclusions paper

- 1.23. Chapter 2 of this paper summarizes by issue the ERGEG's consultation paper and respondents' views on this, and sets out a further ERGEG view on each issue in the light of the responses. Chapter 3 provides a broad summary of the key themes to have been raised and ERGEG's conclusions on the priority topics for consideration. Chapter 3 also proposes next steps for regulators and others in order to progress market integration in a concrete manner.

2 Obstacles to trade and interactions between markets

Introduction

- 2.1. This chapter summarizes by issue the ERGEG's consultation paper and respondents' views on this, and sets out a further ERGEG view on each issue in the light of responses.

Overall

Recap from ERGEG consultation paper

- 2.2. The ERGEG consultation paper recalled the background to the concept of regional markets as a stepping stone to a single electricity market. ERGEG also recalled recent developments using a regional approach, such as the Florence Forum's 'mini-fora' and a number of independent instances of market integration between groups of Member States.

Respondents' views

- 2.3. The majority of respondents said that they welcomed the ERGEG initiative and consultation on the creation of regional electricity markets. Most also mentioned between them that the initiative is timely and relevant, and that a step by step regional approach to the single market is useful and pragmatic.

Definition of regional market

Recap from ERGEG consultation paper

- 2.4. ERGEG noted that the discussion about the concept of a "regional market" illustrates important problems when integrating markets. Most notably, regional markets are seen as a key element of the evolution towards a single market for electricity. For this purpose the ERGEG consultation paper was not intended to give a detailed definition for regional energy markets. Rather, it sets out a road-map for taking forward greater co-operation and co-ordination within a region. For this purpose a Regional market is considered to exist when the following conditions are fulfilled :
- sufficient transmission capacity exists between the markets within the region and is made available to market participants (such capacity may be made available through the use of implicit or explicit auctions)
 - no distortions exist within the local markets which significantly affect the functioning of the regional market

- an appropriate legal and regulatory framework is in place which allows for action across a regional market
- national institutions within the regional market co-ordinate and co-operate closely with each other within an appropriate legal framework. In particular :
 - o TSOs working together in order to ensure that interconnector capacity is optimised and allocated efficiently
 - o Regulators working together and exchanging information appropriately so that proper monitoring and regulation both of national and regional markets can happen.

Respondents' views

- 2.5. One market participant suggested that the regional market is a market area consisting of several market participants, operating under an identical framework, with conditions and market rules ensuring compatibility. Such a regional market should span political borders and be non-static concerning its local extent. Also, it should be flexible according to the relevant market powers and develop to the envisaged pan-European market.
- 2.6. One respondent criticised the EREG conclusions paper for insufficiently differentiating between Regional Energy Markets and the status quo. Another contributor stressed that EREG should focus more clearly on definitions and any overlaps between regional markets and noted that a country within several regions can help to ensure consistency between regions.

EREG view

- 2.7. EREG recognizes that regional markets are dynamic. Consequently, their definition may change over time and according to market sector (wholesale, retail etc.). Most importantly, EREG has not left behind the idea of a Single Energy Market. In fact the Regional Energy markets are intended to complement the development of the single market and not to replace it. The concept of a regional market is intended to be a stepping stone to the single market.
- 2.8. Four indicators for the definition of a Regional Market are mentioned in the Discussion Paper, namely, sufficient transmission capacity between the markets within a region; lack of distortions within the local markets which significantly affect the regional market; an appropriate legal and regulatory framework in place; and national institutions within the regional market co-ordinate and co-operate closely.
- 2.9. None of the respondents specifically commented on the topic, but for EREG the issue of the sufficiency of transmission capacity remains a particularly relevant question. The question of the extent to which transmission capacity is 'sufficient' between any two markets will depend on local market conditions and underlying market motivation for trade. It is interesting to note in this context that interconnection capacity between the four countries of the integrated Nord Pool market is about 10% of installed generation capacity.

- 2.10. The other issues mentioned above are also important in terms of defining and identifying a regional energy market. The conditions for reaching regional markets need to be developed and fulfilled in order that markets move from status quo of relatively isolated national markets to more integrated regional markets. For that purpose the stakeholders can and must be involved (e.g. harmonization of market parameters) in further development. Furthermore the target to develop the Single European Energy Market can only be reached if the need to ensure consistency across the whole EU is taken into consideration for any regional energy market initiative.

Obstacles to trade : network operations

Introduction

- 2.11. The EREG consultation paper noted that the TSO's responsibility for the transmission network is of crucial importance for the achievement of an efficient and competitive Single European Market. TSO's core functions include provision of network capacity and investment, network access, secure live network operation, network maintenance, and provision of information. The creation of an effective regional market will also require that interactions take place between the national markets that comprise that region, and this will therefore require TSOs to co-operate and co-ordinate in order to ensure and facilitate compliance with technical and legal obligations.

NETWORK CAPACITY AND INVESTMENT

Recap from EREG consultation paper

- 2.12. The consultation paper noted that national obligations on TSOs to maintain and develop networks do not extend across national borders, and that the 'regulatory contract' which forms the basis for 'regulated' investment decisions does not always apply in a cross border situation. Consequently both the identification of and funding for investment in cross border infrastructure may be impeded or otherwise lead to inefficiencies in the provision of cross border capacity.

Respondents' views

- 2.13. A number of market participants, including both TSOs and market players said that they see investment in cross border transmission capacity as a key issue for regional market development and/ or its design. These respondents generally agreed that it is necessary to evaluate whether or not the investments are economically justified, and noted that such an evaluation requires more market based and harmonized principles. The need for co-ordination between the TSOs and the regulators as early as at the planning stage was also stressed and recommended by some respondents.
- 2.14. Some respondents agreed that a 'regulatory gap' exists that inhibits cross border investment. Four organizations suggested between them that the financing of internal investments needed for external trade is a problem which might be solved for example

- by using common Regional investment plans. These respondents suggested that regulators and government pay attention to this issue.
- 2.15. Others stressed that additional interconnectors between regions should be driven by price signals and be economically and technically justified. One contributor suggested that TSOs should decide on the need for new build in cooperation with regulators and possibly national governments. In doing so, TSOs should include a regional perspective.
- 2.16. Regarding incentives for TSOs to build or maximize interconnector capacities, on the one hand a couple of respondents argued that these are not compliant with Regulation 1228/2003 and that the maximization of ATC at cross border interconnection is limited by the need to maintain a 'Transmission Reliability Margin'. On the other hand other respondents opined that TSOs need incentives to invest in cross border transmission capacity and/or maximize interconnector capacity.
- 2.17. One contributor said that it was not aware of a 'regulatory gap' inhibiting investment, and opined that short term economic conditions may not be enough to justify construction of (cross border) infrastructure. One commentator argued that market splitting is more efficient than explicit auctions. Another suggested that long term contracts must not be questioned because they are important elements for existing and long term investments. According to this statement, the issue of co-ordinated cross border intra day trade, e.g. short term instruments for congestion management, should also be a topic. However, similar gate closures are needed for this instrument to be implemented.
- 2.18. Several respondents emphasised that investment in cross border transmission infrastructure is also dependent on the grant of necessary planning permissions, that these are not always easy to obtain, and that the EREG consultation paper contains too little discussion of the problem. These respondents therefore asked for attention to be paid, by for example governments and other relevant bodies, to this issue as well as to those other issues mentioned in the EREG consultation paper. Two respondents argued for a harmonized European approach to the problem, with one of these suggesting that a solution could include allowing those communities affected by infrastructure developments also to share financially in their benefits.

EREG view

- 2.19. From EREG's point of view the issue of network operation / cross border infrastructure investment and allocation remains a key issue for market integration. Since there are few or no requirements on TSOs to take into account cross border capacity or system reliability and so identify necessary investment, this identification often falls to government or regulators, sometimes on the basis of calls by market parties. It is not always clear in such cases to which regulator or government such market parties should turn to, or even if it necessary to turn to government or regulators. As a further example, in order to improve trade between Finland and Norway, transmission investment needs to take place in Sweden. The questions arise of who pays and who benefits, and which regulators or authorities oversee or approve this. In some cases, EREG members do not have the competencies for oversight of investment plans. Consequently, other competent authorities may have to be involved in the process. Both examples illustrate that it is not clear, for the question of investment necessary for cross border trade, where the regulatory competence lies and

- hence this 'regulatory gap' inhibits investment. In this context EREG remains of the view that a 'regulatory gap' exists which inhibits cross border investment.
- 2.20. There may be a variety of ways of addressing this. EREG's consultation paper for example noted that strong co-operation between regulatory authorities would be necessary in order to ensure that the aims of the national and integrated markets are reconciled. Furthermore it is desirable to ensure that the 'regulatory contract' between regulators and TSOs and market participants is fulfilled both from a national and regional perspective. Government and regulatory action will be required to address these issues. For example, regulators should be able to take account of market conditions in neighbouring markets, and have a proper legal basis for co-operation. EREG agrees moreover that cross border investment will need to be economically and technically justified, and that the solution of the 'regulatory gap' issue will facilitate the proper evaluation of proposed investment.
- 2.21. From EREG's point of view price signals may well be sufficient to justify construction of cross-border infrastructure. For example, merchant interconnectors have been constructed on basis of prevailing (including forward) prices and economic conditions.
- 2.22. EREG also sees the financing of internal investments needed for external trade as an issue. Some form of a regional Cost Benefit Analysis for new investments on a regional and intra-regional basis might be helpful. Such analyses will need to be set and sanctioned within an overarching regional regulatory framework.
- 2.23. Regarding the need to maintain the Transmission Reliability Margin (TRM) when offering capacity, EREG would remark that its maintenance is also an issue when existing capacities are maximised. However, it is also important to realize that interconnector capacity may be maximized through other means (e.g. co-ordinated auctions and capacity calculations, cross border redispatch, appropriate TSO co-ordination) whilst still retaining the appropriate security margins.
- 2.24. Regarding the question of long term contracts for access to capacity, EREG does not support the opinion that long-term contracts must not be questioned. In fact, long-term contracts, if inappropriately framed and depending on contract parties, can strongly impede and distort development of competition. In this context, further evaluation of the recent ruling of the European Court of Justice Case (7th June 2005, C-17/03) is necessary. Some regulators have undertaken action to replace preferential cross-border access for long term contracts with appropriate market based arrangements.
- 2.25. EREG agrees with the proposal for cooperation between regulatory authorities and TSOs to evaluate the need of further building. However, TSOs will retain the primary responsibility for identifying and building infrastructure within the corresponding national regulatory framework (which may involve approval of for example transmission tariffs). Additionally, the option of a joint decision is already implemented for Merchant lines. TSOs do not have exclusive competences in this area. Also it is necessary to note that not all NRAs have the necessary competences to approve or even oversee investment plans of TSOs.
- 2.26. Regarding planning permissions, EREG recognizes and emphasizes that difficulties in obtaining these are a major obstacle to necessary infrastructure investment. It is important to note that regulators do not have any direct competences in this area but might be able to help by for example coordinating with each other and other relevant authorities where permissions are needed both sides of a border.

2.27. The question of setting incentives for maximization of interconnector capacities does not contradict Regulation 1228/2003. EREG in general sees merit in incentive regulation, but would also comment that the desirability of such incentives depends, among other things, on sufficient unbundling of network activities, in order to prevent inappropriate cross subsidy or other distortions. In general EREG agrees with the goal to maximize the available capacity and to provide incentives for TSOs to do so. However, a maximisation has to be done in view of the trade-off with other desirable outcomes, e.g. maintaining system security.

NETWORK ACCESS

Recap from EREG consultation page

2.28. Network access rights may differ among TSOs and national markets. Systems of financially non-firm access may transfer risk to market participants. Moreover these risks are compounded where access rights to interconnector capacity are non-firm, and so this is an issue when considering how to integrate national markets better.

Respondents' views

2.29. One market participant argued that (long term) firm access rights place a financial risk on the TSO as a counterparty which is linked to price differentials and which is not therefore hedgable. If regulatory approval is given, this respondent argued further, this risk is ultimately borne by the consumer and may be suboptimal from an overall public welfare view point. The issue requires that more emphasis should be put on the global economic effect of different types of solutions.

2.30. One respondent made the case that, if there was an allocation for non-firm transmission, the price would end up lower than for firm rights, and that since this a market result, non-firm rights are market oriented.

EREG view

2.31. EREG sees the long term financially firm access rights as an issue that needs further consideration. Financially firm transmission rights have to be studied carefully to see whether the benefit to market can be enhanced or the possibilities of introducing inefficient "excess" infrastructure or capacity provision can be minimized. This shall also include clear distinctions between system responsibility and other duties.

2.32. Regarding non-firm rights, EREG would stress that the issue is one of defining properly and extensively the property rights associated with transmission access, such that market participants can have confidence in the nature of the access and so price it accordingly. Moreover EREG recalls the Regulation 1228/2003 which requires capacity to be offered as firm as possible, subject to force majeure.

TRANSMISSION CHARGING

Recap from ERGEG consultation paper

- 2.33. At present, methodologies for setting transmission tariffs differ between national markets. Differences exist for example concerning the extent of locational charging and the proportion of charges placed on generators. Differences could affect trade at the borders of national markets and so distort trade in a regional market. In principle, efficient transmission charging would be to charge all users a cost reflective amount for the use of the transmission network in their market area in a way which reflected back the costs they impose on the network and for there to be a common standard for the division of charges between generation and load.

Respondents' views

- 2.34. A number of respondents supported the introduction of common transmission charging principles across each region in order to create a level playing field. One of these respondents suggested that a common European transmission charging system, reflecting common principles for network investments, could be introduced at a further stage of market integration. Another of these respondents argued for ERGEG to develop guidelines on the harmonization of locational charges and the Generation / Load split, and suggested that this would reduce otherwise significant trade distortions. A third one of these respondents recommended tariff harmonization through setting average generation charges to zero, and avoiding 'pancaking' of charges at regional level.
- 2.35. One respondent argued that market based congestion management methods between two areas obviates any competitive advantage or disadvantage caused by the existence of locationally different transmission charges in the two areas. This is because, this respondent argued, prices from the relatively low priced area will be bid up on the auction for capacity on the (congested) interconnector.
- 2.36. The use of ITC-methods based on physical measurements of cross border flows was explicitly supported by one respondent. A couple of respondents said that they supported an ITC mechanism that leads to proper allocation of costs.

ERGEG view

- 2.37. ERGEG agrees that further harmonization of transmission charging principles is desirable. Further appropriate harmonization will help to minimize distortions to trade between Member States. When appropriately calibrated, further harmonization can accommodate appropriate and coherent locational price signals across more than one market, and in so doing promote efficient siting, production and consumption decisions across integrated markets.
- 2.38. Regarding distortions between two national markets caused by differences in locational charges in each, ERGEG is of the view that that such distortions may persist even where interconnection between the two national markets are priced using market based methods. Market based pricing on an interconnector for example will tend to reflect the price differences between two national markets, rather than between two

adjacent charging transmission charging zones. Production and consumption decisions could be different where instead two adjacent markets were treated as one for the purposes of the calculation of locational transmission charging. ERGEG recalls in this context the guidelines for transmission tariff harmonization presented at the XI Florence Forum of September 2004 which were intended as a measure to reduce unnecessary distortions of the internal market. The European Commission intends that tariff harmonization guidelines will be adopted as a binding measure under Regulation 1228/2003.

- 2.39. Regarding the ITC mechanism, ERGEG supports a method based on physical measurements and one which leads to an appropriate allocation of costs. ERGEG intends to consult on the issues associated with the ITC mechanism during 2006 and so will provide further clarification of this issue then.

LIVE NETWORK OPERATION

Recap from ERGEG consultation paper

- 2.40. TSOs are responsible for the real time balancing and hence stability of their networks. Approaches to balancing differ among TSOs. Some national markets for example have explicit balancing markets. Since there are gains from trade, in principle regional markets will be enhanced where TSOs can collaborate across borders to achieve efficient balancing. Moreover such collaboration should allow participation from market players to offer balancing services cross border, such that gains from trade are maximized. The ERGEG consultation paper also notes the complementary issue of congestion management here.

Respondents' views

- 2.41. Some organisations representing TSOs noted that TSOs of synchronously connected areas have created common bases for grid operation (e.g. UCTE Operation Handbook, NORDEL rules) and so these bases reduce the variation in the extent to which TSOs operate their networks in individual national markets. Another of these respondents argued for regulators to support the implementation of such standards rather than creating new pan-EU operational requirements. One of these respondents also provided clarification of the way in which TSOs undertake balancing actions in the UCTE area.
- 2.42. A couple of respondents argued between them that sharing balancing services and so on implies firm reserve of some cross border capacity and thus reduces system robustness and capacity for commercial trade, and hence requires regulatory thought.
- 2.43. One respondent called for clarification of the balancing and congestion management costs described in paragraphs 2.39 and 2.44 of the ERGEG consultation paper.
- 2.44. Regarding TSO's congestion management, one respondent argued that it is necessary to have co-ordinated and market-based congestion management mechanisms. Two respondents argued to mention explicit auctions as well in the context, that congestion management is an important area of managing a live network and to differentiate clearly between preventive and curative congestion management.

- 2.45. Regarding the management of cross border congestion, one respondent suggested that further market integration highlights further the need to have harmonized and market based methods. This respondent suggested that market splitting is more efficient than explicit auctions. Another respondent called for cross border transmission capacities to be freely tradable and for the 'use it or lose it' rule to be applied to mid and long term capacity rights. Having market based mechanism for cross border trade is considered to be essential by one respondent.
- 2.46. Concerning the issue of "pushing out" congestions to borders, two commentators suggested addressing the definition of congestion with transparent methods. Others suggested that congestions inside control areas limiting cross border interconnection capacity are only justifiable from a technical and operational security perspective. These respondents went on to say that offering unlimited (or at least the thermal) cross border capacity would need curative measures by a TSO within its control areas that would have to be paid for by national users, and so national users would be discriminated against at the expense of the international users.

ERGEG view

- 2.47. ERGEG welcomes the work of the European TSOs to create further integrated bases for network operation, such as the UCTE Operational Handbook. Such pan European bases should serve to underpin better the secure operation of the European grid and foster trade and hence market integration. ERGEG would caution however that such bases need to be set within a robust legal and regulatory framework such that appropriate implementation and enforcement may be achieved.
- 2.48. ERGEG also believes that a clear distinction between long term, anticipated congestion on one hand and shorter term congestion that TSOs must manage with redispatch, counter trading etc. on the other is necessary.
- 2.49. For ERGEG it is an open question whether sharing balancing services necessarily implies firm reserve of some cross border capacity and reduces capacity for commercial trade. ERGEG is already working on this issue in one of its Task Forces and intends to consult publicly on this issue during 2006.
- 2.50. ERGEG supports the idea of freely tradable cross border transmission capacities and the application of the "us-it-or-lose it" principle. It is also obvious and already required by the current legal framework that a market based mechanism for cross border trading is necessary. Also, a co-ordinated cross border intra-day trade should be envisaged.
- 2.51. Regarding the question of implicit versus explicit auctions, ERGEG would remark that the choice between these will depend on market conditions. ERGEG therefore supports further analysis of this issue
- 2.52. ERGEG questions the notion that pushing congestions to borders does not happen. There is an incentive to do so, so as to minimize penalties and/or costs for TSOs in terms of the national regulatory framework. Such a practice can be discriminatory. ERGEG recalls that transparency concerning the availability of cross border capacity would help to minimize the potential for discrimination and so is necessary.

NETWORK MAINTENANCE

Recap from EREG consultation paper

2.53. TSOs are responsible for network maintenance, and such responsibility is generally governed by technical standards. Such maintenance will necessitate temporary circuit outages. These outages will affect network users by for example creating local constraints or a greater risk of transmission system failure and can affect cross border flows and regional markets. It is likely that TSOs could co-ordinate on such matters so as to reduce its impact.

Respondents' views

2.54. Respondents did not raise this as a significant issue per se. However respondents commented extensively on strongly related topics such as live network operation, TSO co-operation, and constraint management. Hence views are summarized along with those topics.

CO-OPERATION BETWEEN TSOS

Recap from EREG consultation paper

2.55. The operation of synchronously connected control areas requires TSOs to co-operate and adhere to certain standards. Such co-operation and standards will be particularly important where markets integrate and it will be necessary to consider the extent to which regulatory oversight may be mandated. In addition it is possible that existing national standards impede in some manner such co-operation and standards and so it is necessary to consider this when integrating markets.

Respondents' views

2.56. Two respondents noted that TSOs already co-operate well in order to manage technical interactions. One respondent noted for example that UCTE members have now signed the multi-lateral contract underpinning the UCTE Operational Handbook. The other respondent opined that in this case support is required by regulators at a national level to implement these standards, but not at a European level.

2.57. Respondents in general between them agreed that further market interaction required further co-operation between TSOs such as enhanced communication and/or common technical criteria. One of these respondents for example called for TSOs to collaborate more closely over balancing in order to commercially remove physical restrictions. Another argued for implementation existing technical and operational specifications (e.g. as in the UCTE Operational Handbook) across the EU. Some respondents suggested that it was necessary to develop sufficiently harmonized TSO rules (e.g. concerning gate closure, nomination procedures, and balancing rules) in order to allow cross border trading.

2.58. The majority of the contributions received stressed the importance of cooperation between TSOs, especially in case of disturbances and shortage situations. According to these statements, common information tools and procedures are also needed.

EREG view

2.59. Referring to the comments that stressed the role of the UCTE Operation Handbook as a common basis, EREG believes that the UCTE OH is an important step towards common security and reliability standards.

2.60. However, EREG also supports the market participants' view concerning the need for sufficiently harmonized TSO rules in terms of a common definition of system responsibility. For EREG, an efficient co-operation between the TSOs is vitally important. Respondents' views note that TSOs already co-operate and collaborate extensively, and that this is particularly highlighted through the UCTE Operational Handbook. But it is also clear from respondents as a whole that further work and co-operation needs to occur in a number of areas, including security and reliability standards, and cross border alignment of market parameters. EREG recognizes this need and supports statements here.

2.61. In this context, EREG recalls that the Regulation 1228/2003 allows the possibility for a more overarching security and reliability framework. This could be one useful foundation for the necessary further work.

PROVISION OF INFORMATION

Recap from EREG consultation paper

2.62. TSOs generally hold important and unique information regarding the state and likely state of the network and production and trading positions of each wholesale market player. Such information will be crucial for efficient price formation. Any asymmetries in the availability of information or the timing of its release could therefore distort market outcomes. It will be important therefore to ensure that TSOs manage and release information in an appropriate manner.

Respondents' views

2.63. Some respondents agreed that the question of information management by TSOs is a critical or at least key element in the functioning of the single market, and that this should be done in a non-discriminatory manner. One of these respondents noted that complete unbundling of TSO network activity will contribute to more transparent and symmetric information for all market participants and to more efficient market functioning, and so proposed the need for more specific legislation here. Two of these respondents suggested that the minimization of the potential for gaming by market participants could sometimes be facilitated by TSOs publishing less information, or by publishing later.

2.64. A number of respondents agreed that greater harmonization of transparency and data exchange rules across national borders is necessary for markets to interact.

- 2.65. One respondent argued that the question of whether or not a TSO has a market related affiliate is irrelevant to the question of that TSO's information handling provided that such handling is done on a non-discriminatory basis.

ERGEG view

- 2.66. ERGEG remains strongly of the view that TSOs are key gatekeepers of network and market information, which needs to be managed and disseminated appropriately in order to enable the proper functioning of wholesale markets. DG Competition have likewise identified this as a key issue in their Issues Paper. In ERGEG's view therefore it is necessary that TSOs provide data on a non-discriminatory basis. The scope for non-discriminatory information provision will be maximized where TSOs are fully unbundled and thus are not subject to any conflicts of interest.
- 2.67. Regarding the question of the inappropriate use of information for 'gaming', ERGEG would remark that in general market operation is best enabled, and the scope for any anti-competitive abuse best disabled, where all parties have transparent access to market data and oversight of market function. ERGEG recognizes however that some market data will be sensitive – such as the example concerning distressed purchasers – and that discretion will be required.
- 2.68. ERGEG recognizes that differences in national law could affect the precise mechanics of the way in which information is or is not delivered to the market, but would stress the stronger point that such information is crucial to the efficient functioning of the market.
- 2.69. ERGEG intends during 2006 to consult on the issue of information management and guidelines for good practice on transparency and information management. These points should be addressed during that consultation.

OTHER ISSUES AND REMARKS

Respondents' views

- 2.70. A number of respondents representing TSOs raised the question of security of supply in the context of market integration. One respondent for example suggested that the existence of several TSOs across Europe, each able to fulfil independently its system security requirements, effectively creates individual security cells which can provide back up to each other in emergency situations, and argued for this idea to be recognized in the ERGEG paper. Another respondent echoed this point, arguing for existing associations of TSOs (e.g. UCTE, Nordel) to retain responsibility for the technical rules necessary to ensure system security. This respondent also welcomed the possibility of ERGEG's help in giving TSOs powers to enforce technical requirements on other connected market parties such as generation plant.
- 2.71. One respondent representing EU TSOs indicated its willingness to implement a Europe wide security of supply assessment, and welcomed any ERGEG support here.

- 2.72. One market participant emphasised the need for a common definition of system responsibility by legislation, which should include clear distinction between system responsibility and other obligations.
- 2.73. A couple of market participants also proposed to incorporate the TSOs roles as market facilitator and network planner into the list of TSOs functions

ERGEG view

- 2.74. Security of supply issues will clearly continue to be an important issue for both national and integrated markets. The development of increased co-operation and appropriate security and reliability standards as discussed in paragraphs 2.60 and 2.61 above for example will play an important role in delivering this over integrated markets. Such co-operation should allow TSOs to reap gains from trade and minimize any undue duplication of resource such as multiple back up systems or over contracting of reserve capacity. To this extent any need for separate and independent 'security cells' will be reduced. ERGEG notes in passing that previous examples of system operator mergers (e.g. in Great Britain) have dealt with system security issues satisfactorily within the new merged arrangement. ERGEG also notes, as one respondent mentioned, that input from TSOs in monitoring and assessing aspects of security of supply will be helpful.

Obstacles to trade : wholesale market arrangements

MARKET COMPATIBILITY

Recap from ERGEG consultation paper

- 2.75. Wholesale markets may be organized in a number of different ways. Market designs include for example Pool based systems and bilateral markets. Power exchanges may also exist, instead of or alongside other arrangements. A number of market design features may vary, such as the pricing of imbalance positions, gate closure times, and support mechanisms for generation adequacy (e.g. capacity payments) and renewable generation.
- 2.76. Trade between national markets with different wholesale market arrangements and designs may not therefore be that straightforward or efficient. For example, where balancing costs in one market are smeared across all users but in the adjacent market are reflected back onto market participants causing those costs, distortions in trade may arise owing to the impact these pricing rules are likely to have on market participants' trading decisions. Differences in the treatment of security of supply issues in neighbouring markets will affect prices and trades. These issues highlight the need to consider the extent to which markets need to be harmonized or made compatible
- 2.77. Efficient trade in and between markets will also be promoted where price discovery is efficient, reflecting competitive market outcomes rather than any imperfections in market rules or designs. This efficient price discovery should extend to the pricing of

market participants being out of balance, and in particular coherent pricing between two markets so as not to result in distortions.

- 2.78. In sum, EREG put forward the first view that compatibility of national market arrangements, market information, and impact of national market structure are the principal obstacles to effective trade between markets.

Respondents' views

- 2.79. Several respondents noted the possibility for differences in wholesale market design to distort trade. These respondents identified between them, among other things, differences in incentives on market participants to use particular generation technologies (e.g. renewables), differences in balancing incentives, and incompatible approaches to security of supply as potential distortions. One respondent argued that retail price regulation distorts wholesale markets and should be removed where it presently exists. Another respondent mentioned the possibility for taxes and CO2 allowance prices to distort prices.
- 2.80. Regarding harmonization of market rules, one respondent argued for full EU wide harmonization of market rules and regulations, but bearing in mind relevant national market properties. This respondent went on to say that a first relatively easy step would be to introduce explicit auctions between market areas, and that this should be fostered.
- 2.81. Several respondents representing electricity wholesale and retail market players agreed that further harmonization of wholesale market structures is needed in order to promote trade between national markets. Two respondents argued for example for harmonized balancing and wholesale market timetables across Europe. Another respondent argued that a high level of compatibility is required, for example that the basic market design (e.g. pool, bilateral) should be the same across a regional market, and that the choice of this would determine some forms of cross border trade (e.g. congestion management between bilateral markets is likely to be on the basis of explicit auctions). This respondent suggested that harmonization be pursued only to the extent that it is cost benefit justified. Two respondents suggested that the German market, with its four TSOs and liquid OTC trade, serves as a good example of a large market design.
- 2.82. Some respondents argued that although further harmonization is required, it is not necessary for example to have full harmonization or to implement a single model throughout Europe.
- 2.83. Another respondent, representing TSO views, noted that reaching agreement on some elements of harmonization would be difficult given the diverse interests of all market parties, and that therefore regulators needed to consult widely on a regional basis before taking a co-ordinated decision.
- 2.84. In order to maintain the overall goal of a single market, the need to avoid inappropriately large diversions in regional approaches and harmonizations was mentioned by a number of respondents.
- 2.85. Two respondents expressed the view that mandatory pools such as the previous England and Wales Pool are a discredited model. These respondents suggested therefore that pool based systems should not be listed first in the EREG

consultation paper nor described in detail. In this context, two respondents expressed concern about the Nord Pool monopoly on cross-border flows.

- 2.86. Some respondents put forward between them the views that functioning wholesale markets themselves would serve as a market driver for the expansion of national electricity markets into regional and ultimately European markets, with a single price area, and that current trends in the EU electricity markets confirm this. Two respondents suggested between them that it was therefore necessary for electricity markets to have well-designed and functioning transmission and system services managed by TSOs, functioning wholesale trading provided by OTC markets, and trustworthy market determined prices and open intra-day and balancing markets. One of these respondents argued further that any market model should allow the full participation of large consumers such that the demand side is represented and prices are better determined. The other respondents here suggested that the objective of assigning balancing costs against those who cause them must be weighed against any transaction costs.
- 2.87. Two respondents suggested that the comparison of balancing costs given in paragraph 2.39 of EREG's consultation paper needs to be made carefully, and called for a clarification on this point.

EREG view

- 2.88. With reference to respondents' views above, there is a clear consensus that differences in wholesale market design and other factors can distort trade between national markets, and that therefore some degree of harmonization of national arrangements at least at the regional level is required. Opinions differed on the extent of the required harmonization and the issues to tackle first.
- 2.89. EREG supports the views expressed by some respondents that inappropriately large diversions in regional approaches need to be avoided, in order to maintain the goal of a single market.
- 2.90. The German example with four TSOs offers some interesting experiences regarding market integration. It is also worth recalling here that some German TSOs merged during the last few years. The country demonstrates to some extent how markets could co-operate more closely and gives insights into what could be priority issues that need to be addressed. Nevertheless it is necessary to stress that these German developments have occurred against the background of a single nationwide legal framework and that there are no network congestions for trade in the market.
- 2.91. A good example of the integration of national electricity markets is the Nordic experience with electricity markets. In this case, in spite of differences in production mix, energy policy and TSO ownership, a gradual and successful integration has taken place since the mid 1990s. Today the Nordic market is characterized by the close co-operation of four national TSOs and one power exchange serving the whole market.
- 2.92. Experience of the process of moving to a single market during the period since the Florence Fora were established has revealed that there is a diversity of views concerning, for example, the need for further harmonization and how it should be achieved. EREG therefore supports processes which involve both full and open

consultation of interested parties and a timely adoption and implementation of necessary solutions.

- 2.93. Regarding the remark on Pool based systems, ERGEG would note that appropriately designed Pool based systems are a recognized design for, and compatible with, competitive electricity markets, including situations where markets may be integrated. There are plans for example to use such a design in the 'All-Island' market to link the Republic of Ireland and Northern Ireland.
- 2.94. Regarding balancing costs and paragraph 2.39 of ERGEG's consultation paper, ERGEG would comment that the illustrative figures included in the consultation paper show clearly that the way in which the costs of balancing are handled (including the way in which imbalance charges are passed back to users) may vary between areas. This may lead to distortions and needs to be further analyzed. ERGEG will take up this issue in its further work.

TRANSPARENCY

Recap from ERGEG consultation paper

- 2.95. Market efficiency, including the development of liquid pricing and market participation by brokers and traders, strongly depends in addition on the non-discriminatory availability of appropriate information from generation market participants. By providing data to players in adjacent markets, such transparency should also facilitate cross border trade.

Respondents' views

- 2.96. Several respondents agreed that it was essential or appropriate for the development of regional markets that market participants have transparent access to common sets of market information. One of these respondents argued for harmonization of the rules governing market transparency and the provision of data.
- 2.97. A number of respondents expressed concerns about the impact or need for increased transparency, for three main reasons. Two respondents suggested that power exchanges already provide information and transparency to market players. Two respondents raised between them the question of the way in which costs related to market transparency would be borne and the need to assess these costs against their benefits to the market. Three respondents argued for careful assessment of the impact of information on the market, with one suggesting that the provision of some data could facilitate gaming or strategic pricing. One respondent suggested that there are sometimes reasons why data should not be published, citing the example of the possibility for generation outage plans to reveal distressed purchasers.
- 2.98. Three respondents noted that some present regulatory or legal frameworks restrict the publication of some market information, and two of these called on ERGEG, national regulatory authorities and governments to address this issue.

EREG view

- 2.99. Regarding the need for access to market information and transparency, EREG notes that a range of respondents agreed that this is essential for the development of regional markets. EREG would note further that the status quo, even where power exchanges and other organisations provide some data to market, is often insufficient compared to the expressed needs of the market. As other respondents suggest, it will of course be necessary in addressing this issue to consider the cost-benefit and any legal hurdles to be overcome.
- 2.100. Increased transparency will also, in EREG's view, help regulators, other relevant authorities, and industry better to monitor and analyze markets and market behaviour. This possibility for better market scrutiny by both regulators and market participants should by itself discourage 'gaming' and any other inappropriate market behaviour. This point is particularly relevant in the context of access to cross border interconnector infrastructure, where a lack of transparency has hindered the formation of competitive market outcomes.

MARKET STRUCTURE

Recap from EREG consultation paper

- 2.101. EREG noted that the impact of national market structure may also affect market participation and hence interaction between markets. For example, lack of full retail market opening implicitly limits the portion of the market open to trade. Furthermore the presence of a TSO with market affiliations may reduce market participants' confidence that the market will function in a non-discriminatory manner.

Respondents' views

- 2.102. Regarding market structure, one respondent argued that a precondition for the development of regional markets is the existence of a sufficient number of market participants. Another respondent argued that large players can ensure well functioning markets by taking an active part in power exchanges and providing liquidity. Two other respondents argued that unequal retail market opening is the largest market distortion and that the issue should become more prominent.
- 2.103. The full implementation of and compliance with the electricity Directive and Regulation was cited by a number of respondents as a further set of preconditions for the proper functioning of wholesale markets and development of regional markets.

EREG view

- 2.104. Markets in general, and market integration in particular, will require that market is not too concentrated to prevent competitive rivalry and price discovery. Clearly the full and timely implementation in all Member States of the EU legislative basis for the competitive single market is also a prerequisite for market integration. EREG notes that the electricity Directive provides for full retail market opening by 2007.

EREG VIEW OVERALL

- 2.105. In the light of remarks overall, EREG therefore maintains its view that it is essential to address the issues of compatibility of national market arrangements, market information, and national market structures, in order to allow effective and efficient trade between markets.

Obstacles to trade : regulation across a regional market

Recap from EREG consultation paper

- 2.106. Each national market is overseen by at least one (energy) regulatory authority. Their tasks include, in the competitive field, providing a level playing field for market participants, and in the monopoly field, providing a regulatory framework for the setting of network tariffs. Bringing together national markets into a regional market will require a corresponding reorientation of and cooperation between national regulatory authorities in order to ensure the required rules, arrangements and incentives are in place such that the aims of the regional market are realised as well as the aims of the national market. It is also important to recall that at present, given that regulatory authority A in country A will in general have no competences to act in country B, where countries A and B integrate their markets, issues of the need for cross border competences will arise.

Respondents' views

- 2.107. The question of difficulties of co-ordination and co-operation among regulators because of their different roles and responsibilities in each Member State was suggested by some respondents as an important issue to consider. In view of this issue, some respondents between them consequently argued for the need to harmonize fully or partially the regulatory framework across borders and for the need for closer co-operation between regulators. Some respondents suggested that regulators also need to give prominence to their work's European dimensions. One respondent argued that a flexible application of regulation is required in each region, and that new legislation would probably be required in the involved Member States to achieve this.
- 2.108. A number of respondents also argued that since for example TSO to TSO co-operation is already working reasonably well across (some parts of) the EU, or where markets are mature or well designed and market participants make the market work, there was no need for significant further regulatory, legislative or institutional oversight. Furthermore, a few respondents argued that there was no need for global EU market regulation and that any moves to supplement regulatory oversight at an EU level should be designed to avoid duplicate regulation or the introduction of further impediments to trade. One respondent argued that the appropriate extent of regulation should reflect its cost efficiency and the extent to which an issue has cross border effects.
- 2.109. A couple of respondents commented that an appropriate European level regulatory framework would be given to some extent where the electricity Directive and

Regulation are fully in place and properly applied in all Member States. Electricity Regulation 1228/2003 for example, one respondent argued, introduces a decision making process relating to interconnection issues. One respondent argued that relatively immature markets would require greater regulatory involvement than in more developed markets, where market participants would have a correspondingly larger role. Another respondent suggested that regulators should at least provide a stable regulatory framework in order to foster necessary investment in grids.

ERGEG view

- 2.110. It seems clear that regional markets will need to be accompanied by appropriate regulatory oversight. In order to achieve closer co-operation between regulators, it appears likely that at least some form of harmonization or at least clarification of roles and responsibilities will be needed. Regulators or relevant authorities will at least require similar competences regarding the oversight of transmission investment and remuneration in order to co-operate on this issue across borders, and so where cross border issues arise, regulatory competences either side of the border need to be adequate.
- 2.111. Hence ERGEG would stress that one prerequisite for market integration is for national regulators to have appropriate powers, competences and independence. The full implementation of the Directives and Regulation will provide a good foundation for these.
- 2.112. Furthermore, regarding market integration, ERGEG agrees that regulators should have powers appropriate to national and cross border roles. It may be possible to underpin much of the necessary co-operation among regulators by extending only the geographic scope of each regulator. This could be done for example by requiring each regulator to take into account the interests of neighbouring or EU customers in formulating policy, or by enabling regulators to request and exchange market data.
- 2.113. Hence new pan – EU regulatory powers are not necessarily foreseen under this approach, and the possibilities for ‘duplicate’ regulation are correspondingly reduced. ERGEG would stress that such an approach does not imply an inappropriately far reaching extension of the scope of regulators’ powers. Any revision or extension of the scope of regulatory competences will need to be justified in terms of their benefits.

Interactions between markets – key themes for the case studies

Recap from ERGEG consultation paper

- 2.114. The ERGEG paper set out 5 case studies of real practical experience of initiatives to integrate markets. These were :
- Great Britain
 - All-island market for the Republic of Ireland and Northern Ireland
 - Iberian peninsula
 - Nordic countries
 - Australian national market

- 2.115. The case studies seemed to indicate a number of key factors important in terms of market design for market integration. These are :
- Key market arrangements must be compatible, although full harmonization is not always necessary since different arrangements can function provided they are made compatible.
 - Market transparency at the national and regional level are very important to facilitate trade.
 - TSOs within a region need to interact and co-operate appropriately.
 - The stage of liberalization within each national market comprising the region needs to be similar and preferably advanced, such that trade and interaction is enhanced.
- 2.116. Moreover the case studies indicated a need for a clear overarching regional regulatory framework. This will facilitate for example cross border investment.
- 2.117. The case studies delivered strong evidence that commitment from all stakeholders is necessary to deliver market integration. Government action in particular is essential, by underpinning and fostering such integration, and by making the necessary legislative changes and also through providing impetus to market parties.

Respondents' views

- 2.118. Several respondents agreed that the case studies were useful in identifying the issues to be addressed in integrating markets. The use of Germany – Austria and Germany – Netherlands as useful further case studies of regional markets that are market outcomes was suggested by one respondent. One respondent highlighted the Great Britain case study as a good example of pricing arrangements across the interconnector prior to market integration distorting the two connected markets, i.e. England and Wales and Scotland.
- 2.119. Two respondents said that they saw more limited lessons to be learnt from the case studies, since most referred to island or near-island (peninsular) situations, whereas the continental plate has a largely integrated network which is also crossed with political borders.
- 2.120. Of those respondents that saw value in the case studies, several agreed between them that the clear message from the case studies is that agreement between governments, political support and strong commitment from all stakeholders including regulators, TSOs, market players, and the European Commission is necessary to integrate markets successfully.
- 2.121. A couple of respondents also emphasised that TSOs have an important role to play in integrating markets. Two respondents nevertheless argued that TSOs acting alone or first cannot deliver regional markets, and that it is important or necessary to clarify the roles and responsibilities of the other stakeholders.

ERGEG view

- 2.122. Overall, respondents' views chime with those expressed by ERGEG in its consultation paper. ERGEG concludes therefore the case studies point to the key

issues to be addressed in integrating markets, as summarised in paragraph 1.7 to 1.9 above. In particular, it is clear that strong government support is crucial in ensuring the success of market integration initiatives.

- 2.123. As one respondent noted, the Germany-Netherlands and Germany-Austria experiences offer examples of market integration beginning to occur. These experiences will be returned to under the set of regional initiatives that EREG proposes to pursue, as described in chapter 3.
- 2.124. EREG proposes that the case studies given in its consultation paper have now done their work by identifying the relevant issues in integrating markets. The regional initiatives work proposed in chapter 3 is intended to take these issues and allow concrete progress in market integration across the EU.

Recommendations for next steps

Recap from EREG consultation paper

- 2.125. The EREG consultation paper suggested that a number of initiatives – called ‘case studies’ in the paper - be pursued at a regional level in order that market integration at a relevant local level could be achieved. Each regional initiative would correspond to the nations comprising each mini-forum, so creating 7 regional initiatives.
- 2.126. The idea is that each regional initiative’s first task would be to assess the priority issues to be tackled in that region in order to integrate (further) national markets, drawing upon the issues identified by EREG as a checklist. This assessment could then be developed by regulators in co-operation with TSOs, governments and other stakeholders in order to propose and implement solutions.
- 2.127. The paper noted that in parallel to this suggested process, EREG would consider the governance issues to apply to the regional initiatives, and that governance would depend among other things on the regional initiative’s membership.

Respondents’ views

- 2.128. A number of respondents commented between them overall that a regional approach as a step towards a single EU electricity market is a pragmatic one and that there are few if any alternatives available. Some respondents also emphasised the need to maintain an overall coherent approach and for regional markets to be flexible enough to accommodate variable states of development and changing circumstances. Two respondents argued between them for more concrete recommendations and timetable, and a bolder action plan. One respondent called for a better explanation of the advantages of the regional market concept as an intermediate step.
- 2.129. Some respondents agreed with the approach of the regional initiatives and mini-fora. One of these respondents argued that only bodies responsible for market design – governments, regulators, European Commission, and TSOs – should participate in the mini-fora, and that consultation processes with market participants should take place prior to the fora. One respondent argued for a participation in the regional initiatives and mini-fora to include market participants, since these parties are also affected by developments and indeed presently trade on an international basis.

- 2.130. One respondent suggested, and another respondent implicitly agreed - that wholesale markets (trading, liquidity, and transparency) themselves can constitute a driver for market integration. This respondent therefore suggested that market integration should be driven by market forces, where wholesale and transmission markets are functioning and undue intervention is minimized, and supported by a strong political will. This respondent suggested that progress on market integration could be achieved driven primarily through wholesale market integration and in four, perhaps overlapping and parallel, steps :
- continued liberalization of national markets (2005 - 07);
 - development within regions (2005 - 09);
 - co-ordination between regions (2005 - 10); and
 - integration at EU level (2007 - 12).
- 2.131. In putting forward this process, this respondent suggested, among other things, that it would be necessary to have close co-operation between regulators, TSOs, and power exchanges and interaction of these with other market participants, and that proper inter-regional co-ordination should be established by 2010.
- 2.132. Another respondent suggested that a first easy step towards market integration could come from making the overall market framework or the various operational procedures compatible, for example by fostering explicit auctions between national markets. This respondent suggested further that a second step could be the fostering of intra-day trade through implicit auctions.
- 2.133. One respondent also argued for pan-European solutions and approach to be developed alongside the regional initiatives. This pan-European approach would, this respondent argued, tackle issues such as the promotion of infrastructure between regions that otherwise would not be tackled.
- 2.134. Most respondents that commented on the issue agreed that appropriate Member State and government support will be needed in order to facilitate market integration. One respondent suggested that for example government would have a role in establishing frameworks for regional wholesale markets and facilitating authorisation procedures for new investment in generation and transmission lines. Some of these respondents particularly mentioned the financing of cross border infrastructure in this context.
- 2.135. A note of caution was sounded by one respondent, who recalled that it would be important to ensure that the overall goal of the single market is not compromised by too many or too different regional initiatives. Another respondent noted that some Member States are part of more than one regional initiative or mini-forum and that this would raise the need to maintain overall compatibility across all the regions to which a particular national market belongs.
- 2.136. Some respondents representing network operators emphasised that TSOs operate under legislation and regulation, and so TSOs alone cannot initiate the process for or deliver market integration. These respondents therefore also emphasised the need to involve regulators, governments, and the European Commission in the first stages of the creation of the regional initiatives.
- 2.137. Two respondents also called between them for network users to be consulted and involved in any process for developing regional markets, including for example market

design questions. One of these respondents suggested that such consultation be kept separate from the mini-fora process since it would be impossible for these fora to satisfy all network users' interests.

- 2.138. One respondent argued that wholesale and retail price regulation and caps distort competitive markets and so should be quickly removed where they exist.
- 2.139. One respondent argued that long term Power Purchasing Agreements (PPAs) could impede the market, particularly where agreements were entered into before the liberalization process and where agreements were not set in a competitive market context. This respondent argued for such long term PPAs to be terminated, with appropriate compensations.

EREG view

- 2.140. EREG supports calls for action on market integration to be made more concrete and to a firmer timetable. Such action will also need the support of market participants and those market parties responsible for implementing change. Hence consultation of stakeholders will be required. It will be necessary to establish an organizational structure, process and timetable in order to progress market integration as called for. EREG in chapter 3 makes a number of proposals designed to address and progress these points. In particular EREG proposes 'regional initiatives' which will replace the idea of 'case studies' as described in the consultation paper. These regional initiatives will be aimed at obtaining concrete further progress in market integration in the relevant regions. Such progress must be made in the context of the overall goal of reaching a single electricity market.
- 2.141. EREG is aware of some regional initiatives by governments like the Pentalateral initiative in Central Western Europe and the regional framework already established in the Nordic countries. Caution is needed therefore to ensure that such initiatives are consistent with those undertaken by regulators. In the case of already well established frameworks therefore, new frameworks are not necessarily needed and so the need for them should be carefully considered. Coordination of the activities based on the proposals brought forward in this paper is therefore necessary.
- 2.142. Moreover, EREG recalls that the overall aim is to reach a single competitive electricity market across the EU. In building each region therefore, it will be necessary for a dialogue to be maintained between regions in order to ensure that initiatives are compatible with each other and so converge rather than diverge onto this aim. Some Member States will, due to the nature of geography and market dynamics, be part of more than one region. Such a dialogue will also be important therefore to recognize and reconcile the participation of such Member States in multiple regional markets.
- 2.143. Regarding the role of government, EREG would stress that it sees government and legislators having an important role in developing market integration. It is likely for example that legislative changes will be required in order to remedy the 'regulatory gap' by allowing a regulator in one market to take account of circumstances in the neighbouring market. Present developments in the All-Island market of the Republic of Ireland and Northern Ireland point to the need for this when integrating markets.

- 2.144. From ERGEG's point of view, proper oversight and regulation of monopoly activities (e.g. transmission tariffs) is a prerequisite for a functioning, non-discriminatory wholesale market. ERGEG would further comment that it is necessary to recognize that price regulation, in the retail sector, can be a valuable regulatory tool to protect (small) customers' interests during the transition to effectively competitive markets. ERGEG would also stress however that any such price controls must be set in a way to support rather than conflict with the development of competition.
- 2.145. Regarding PPAs, ERGEG notes that the extent to which they may be an impediment to competition in a national or integrated market will depend on the details and circumstances of the particular agreements. Consequently this is an issue that must be dealt with by regulators on a case by case basis.

3 Conclusions and next steps

Introduction

- 3.1. This chapter sets out ERGEG's broad conclusions in terms of a number of key themes, and goes on to map out a process for taking forward the work of market integration.

Key themes

- 3.2. Respondents in the main commented that the regional approach to the single market is a pragmatic and manageable one, and one which recognizes the present realities of disparate market arrangements across the EU. There is broad recognition of and support for the idea that market integration and the creation of regions will require strong commitment from the involved parties, and above all needs to be underpinned by government support to deliver the necessary impetus and legal framework
- 3.3. Responses also highlighted in broad terms a number of key themes regarding market integration. Network issues and availability of transmission capacity in particular featured strongly among responses and comments, and in the main attention focused on cross border investment, network access and charging, congestion management, and interactions between TSOs. Regarding wholesale markets, views highlighted market design compatibility questions. Market parties recognized the need for the market to receive appropriate market information, and for this to be properly managed by TSOs. Further co-operation among TSOs is also flagged as a key issue.
- 3.4. Network capacity and investment, particularly across borders, is seen by many respondents as a key issue for regional market development. Views varied on the elements of detail to focus on in addressing this issue. It is clear however, and ERGEG would support this, that investment will be facilitated and most efficient where they are economically and technically justified and so supported by underlying price signals. The identification and mandate for such cross border and regional investment can only occur where a clear regulatory framework with some form of cross border competence exists. ERGEG notes that a further clear issue that requires attention is the question of the grant of necessary local planning permissions.
- 3.5. Access to transmission infrastructure is clearly an issue for trade across markets and regions, and this again featured in the discussion raised by respondents. Most parties who commented said that they strongly favoured market based congestion management methods, and for these to be brought forward. The question of financially firm transmission access received some comment and discussion, with parties noting the issues here, such as the question of obligations and risks on TSOs compared with benefits to the market
- 3.6. Co-operation between TSOs was recognized as a further issue to be addressed in the context of integrating markets. Opinions differ on the extent to which this is already addressed within the framework of existing institutions (for example the UCTE

- Operational Handbook) or needs to be underpinned by further initiatives. It seems clear however that further attention must at least be paid to the question.
- 3.7. Regarding wholesale markets and the need or otherwise for harmonisation of arrangements, there is a general view that some form of further harmonisation or at least compatibility is required. There is as yet no firm view as to the extent of the required harmonization, or indeed whether this might differ from region to region. Nonetheless, questions of the need for market parameter harmonization (e.g. balancing market timetables and so on) featured prominently.
- 3.8. The importance of availability and control of information and transparency issues in general emerged from discussion points and comments regarding both network and wholesale market issues. Organizations representing market players in particular, and to some extent also TSOs, emphasized the importance of timely and non-discriminatory information on both networks and wholesale market operation as key contributors to efficient price formation and markets. Views on some elements of detail, for example regarding the legal basis, opportunities for gaming and so on, varied.
- 3.9. A key factor emerging from discussion across many of the issues is that government and regulators will have an important role to play. The question of the 'regulatory gap' for example will require attention at a regulatory and legislative level. The perceived need to harmonize some arrangements across regions, including further TSO co-operation, will require legislative oversight. Some of these items might be delivered through further voluntary co-operation between relevant bodies using existing competences, but it is likely that these will prove to be insufficient compared to the new challenges of integrating separate national markets. Some items, as demonstrated by the ERGEG consultation paper's case studies, might be addressed using formal treaties. In the general case however it is likely that governments will need to underpin further progress with legislative measures. Such legislative measures can provide the necessary clear regulatory framework at the regional level.
- 3.10. Considering comments overall, ERGEG concludes that at a broad level the four categories of issues identified in the ERGEG consultation paper are those that should be addressed as priority areas in order to deliver integrated markets. These are :
- availability of transmission capacity
 - availability and control of information
 - co-operation between network operators
 - compatibility of wholesale market arrangements
- 3.11. Furthermore ERGEG considers that it is clear that strong political and regulatory commitment is required to address these areas.

Next steps

ERGEG AND CEER WORK PROGRAMMES

- 3.12. A number of the key themes identified above reflect issues already identified by the ERGEG as important issues to be addressed from a regulatory perspective across the EU. The consultation and responses to it also highlighted other issues which are necessary to address. ERGEG and its parallel organization the CEER have therefore

taken these points into account in developing their work programmes for 2006 and beyond³.

- 3.13. EREG will continue to develop guidelines on an Inter-TSO compensation mechanism designed to compensate TSOs for hosting cross border flows and to eliminate the 'pancaking' of transmission tariffs. This should help to provide a level playing field for electricity wholesale market participants. EREG will also undertake further work on the question of transmission tariff harmonization, such an analysis of the effects and possibilities for harmonized fee structures. The question of the need for and effects of financially firm transmission rights will also be assessed.
- 3.14. Regarding access to interconnectors and recalling EREG's July 2005 publication of advice on Congestion Management guidelines, EREG will follow up on this by for example assessing issues for the implementation and monitoring of them. Congestion management will also be examined in the context of designs of connected national markets. The related topic of the cross border framework for transmission investment will also be examined.
- 3.15. On market harmonization issues, EREG has undertaken a considerable amount of work in considering how balancing markets might be better integrated. This will continue into 2006 and will include a public consultation on Guidelines on Good Practice for electricity balancing markets integration. CEER will also look at the co-existence of bilateral exchange arrangements and organized wholesale markets.
- 3.16. EREG and CEER will continue to develop its position on the need for further market transparency and information management. EREG intends as a part of this work to develop and consult on Guidelines of Good Practice for Transparency and Information Management.
- 3.17. Regarding TSO co-ordination, EREG will consider the extent to which further co-ordination is needed and the appropriate methods for achieving it, in order to ensure a secure and economically efficient network that also facilitates competition across the single market.
- 3.18. Work on cross border issues will be complemented by EREG assessing the compatibility of national legal and commercial conditions for cross border trade, and the compatibility of national regulatory frameworks.

EREG REGIONAL INITIATIVES

Introduction

- 3.19. Policy makers and stakeholders alike agree that their overall aim is the creation of a single electricity market across the EU. Indeed EREG has a statutory role which includes the facilitation of the completion of the internal energy market. A pragmatic way to achieve this aim will be via the interim step of integrating national markets into regions, in a manner which will allow the subsequent step of full market integration. It is clear from responses to the EREG consultation paper that there is a broad consensus that it is therefore necessary to make concrete progress on integrating

³ EREG and CEER Work programmes available at www.ereg.org and www.ceer-eu.org respectively

national markets so that regional markets can be created as the necessary interim step.

- 3.20. It is worth recalling in this context that the mini fora are an important platform for further progress towards a real Integrated European Electricity Market. With the first round of mini fora in 2005 an initial step was achieved, although the progress and results varied across them. In some cases significant progress towards market based Congestion Management has been achieved. In other regions improvements are not yet clearly observable. In order to foster the market-based Congestion Management further and to further establish regional markets, it makes sense to build on the foundation laid by the mini fora within the process for the discussions of the next developments. The XII Florence Forum of September 2005 already anticipates this, since it foresaw a further round of mini-fora in the spring of 2006.
- 3.21. EREG suggests therefore that any regional market initiatives will need to encompass and complement the mini-fora. The mini-fora will, for example, provide an important platform for market participants to discuss and express views. Participants will also expect feedback on reports or projects aimed at further market integration.
- 3.22. Action will clearly be required by many stakeholders and institutions in order for change and progress to occur. EREG suggests that regulators, the EU Commission, Member State governments, TSOs and other market operators, and market participants and other market interested parties will comprise the overall set of parties necessary to identify and effect change. The Florence Forum will play an important role in bringing all these elements together in order for progress to be described and discussed. Market participants responsible for market processes and rules will for example need to consider and implement adjustments to processes and rules in order to foster cross border trade. Such matters are particularly likely to apply to TSOs and other market operators. Hence each regional initiative will require a process designed to marshal and monitor the necessary actions, that is, to implement proposals.
- 3.23. It is also worth recalling that a number of regional initiatives already exist, sometimes in parallel with the previous mini-fora process. A number of these initiatives were described in the EREG consultation paper, such as the All-Island market for the Republic of Ireland and Northern Ireland, the creation of an Iberian market, and the mature Nordic market. Some of these continue to be developed. Some new initiatives have been further developed since June 2005, such as plans for linking wholesale markets in Belgium, France, Luxembourg, the Netherlands, and Germany. A number of these initiatives have already adopted working arrangements and processes, involving stakeholders in an appropriate manner.
- 3.24. EREG would stress therefore that its proposal to initiate a process for further market integration will need to be framed in such a way that any such existing initiatives are complemented rather than duplicated. This points to the need for flexibility in the arrangements adopted in each region. Flexibility should enable each regional initiative to adopt processes suited to its region and so minimize inappropriate, unwieldy or bureaucratic measures. A number of regulators and Member State governments for example have already set in place some initiatives and arrangements, and so it will be helpful to build on these. Furthermore a number of countries potentially belong to more than one region and so regulators and other

stakeholders in these countries are likely to want to combine and / or target resources as necessary.

- 3.25. In pursuing a process for the further creation of regional markets, EREG will need to bear in mind the overall aim of the creation of the single market, and so take steps to ensure that initiatives pursued by EREG at a regional level are coherent with each other. EREG would expect therefore to maintain an overall role in monitoring, comparing and co-ordinating the set of regional initiatives.
- 3.26. EREG notes that such monitoring and co-ordination will in any case be necessary in order to facilitate transparency of the regional initiatives, and dialogue and consultation with the stakeholders. A transparent monitoring process will also enable all stakeholders to understand how and when necessary solutions are being delivered.

Progressing market integration – EREG Proposal for Regional Initiatives

- 3.27. Bearing in mind the above, EREG proposes that it establishes and co-ordinates a number of regional initiatives. The idea will be for each regional initiative to be a grouping of countries with an interest in fostering trade.
- 3.28. EREG intends with this proposal to initiate a process intended to make concrete progress in integrating national markets and so facilitate further the creation of regional markets. The overall aim will be, for each regional market, to identify specific problems of impediments to trade or distortions to trade, and introduce practical improvements that will contribute to removing such impediments. Such 'regional initiatives' should enable local stakeholders to identify, and plans solutions for, the priority areas for action needed to deliver integrated markets.

Objectives

- 3.29. Hence each regional initiative would have the objectives to :
 - Identify and publish, based on the priority areas discussed in this conclusions paper and through open consultation with market participants, the priority areas to be addressed in the region.
 - Establish and publish a timetable for the technical work required to address these areas, including allocating responsibility for the tasks to the stakeholders most able to accomplish the relevant work.
 - Take forward and oversee that this work is done to timetable. Monitor and report progress. Note any reasons for any delay.
- 3.30. Any such regional initiatives will clearly need to involve all stakeholders. It will be necessary to consult on proposals for market integration. Market participants have for example extensive detailed knowledge of market conditions and issues. Established market participants are often already working with local regulators and other relevant authorities to enhance market functioning. New entrants often have helpful perspectives on where impediments to trade exist.
- 3.31. Each regional initiative would identify its own priority issues needed to best foster market integration, taking into account therefore local details and requirements. Each should aim to establish a process for delivering solutions, and so this will need to involve collaboration with and action by, among others, regulators, government, and

TSOs. For the purpose of creating finally a single electricity market it is of utmost importance that each regional initiative considers the need for compatibility of the established processes with those in connected regions, although progress in one region should not be contingent on progress in another.

- 3.32. It will also be important for the overall process to progress compliance with the relevant EU legislation. Full compliance with the EU legislation, in particular the Electricity Directive 2003/54/EC, Regulation (EC) 1228/2003 and the associated congestion management guidelines and other legal instruments of relevance for the European electricity market, must be ensured in all the activities and deliverables of the regional initiatives, including the mini fora. Furthermore, the results of the related activities at the European level, like for example DG-TREN's recent report and Electricity Sector Inquiry by DG Competition shall be taken into account appropriately. Ensuring this compliance shall be the duty of regulators and shall be reported regularly on an annual basis to EREG.

Composition

- 3.33. A first proposal for the composition of each regional initiative will be given by the 7 groups of mini-fora countries, namely :
- Baltic States : Estonia, Latvia, Lithuania
 - Central Eastern Europe : Austria, Czech Republic, Germany, Hungary, Poland, Slovakia, Slovenia
 - Central Southern Europe : Austria, France, Germany, Greece, Italy, Slovenia, (Switzerland)
 - Central Western Europe : Belgium, France, Germany, Luxembourg, Netherlands
 - Northern Europe : Denmark, Finland, Germany, Norway, Poland, Sweden
 - South Western Europe : France, Portugal, Spain
 - UK and Ireland : France, Republic of Ireland, UK

EREG and Inter region co-operation and consistency

- 3.34. Given the overall goal of a single market for electricity, it is important to ensure that each of the regional initiatives are producing proposals and solutions that are ultimately compatible with each other. EREG will therefore retain a strong role in overseeing and comparing progress in each of the regional initiatives. EREG will for example ensure the cooperation, coherence and compatibility of relevant developments among the different initiatives, relying on EREG regular work and procedures as well as on any necessary dedicated tasks.
- 3.35. EREG will therefore maintain a role to receive, evaluate and compare the reports prepared for each region on progress identified and achieved. Such monitoring reports should also be evaluated at Board level. EREG will also serve as a discussion forum, bringing together all regions in order to compare and contrast issues and to help maintain an overall consistency of approach.

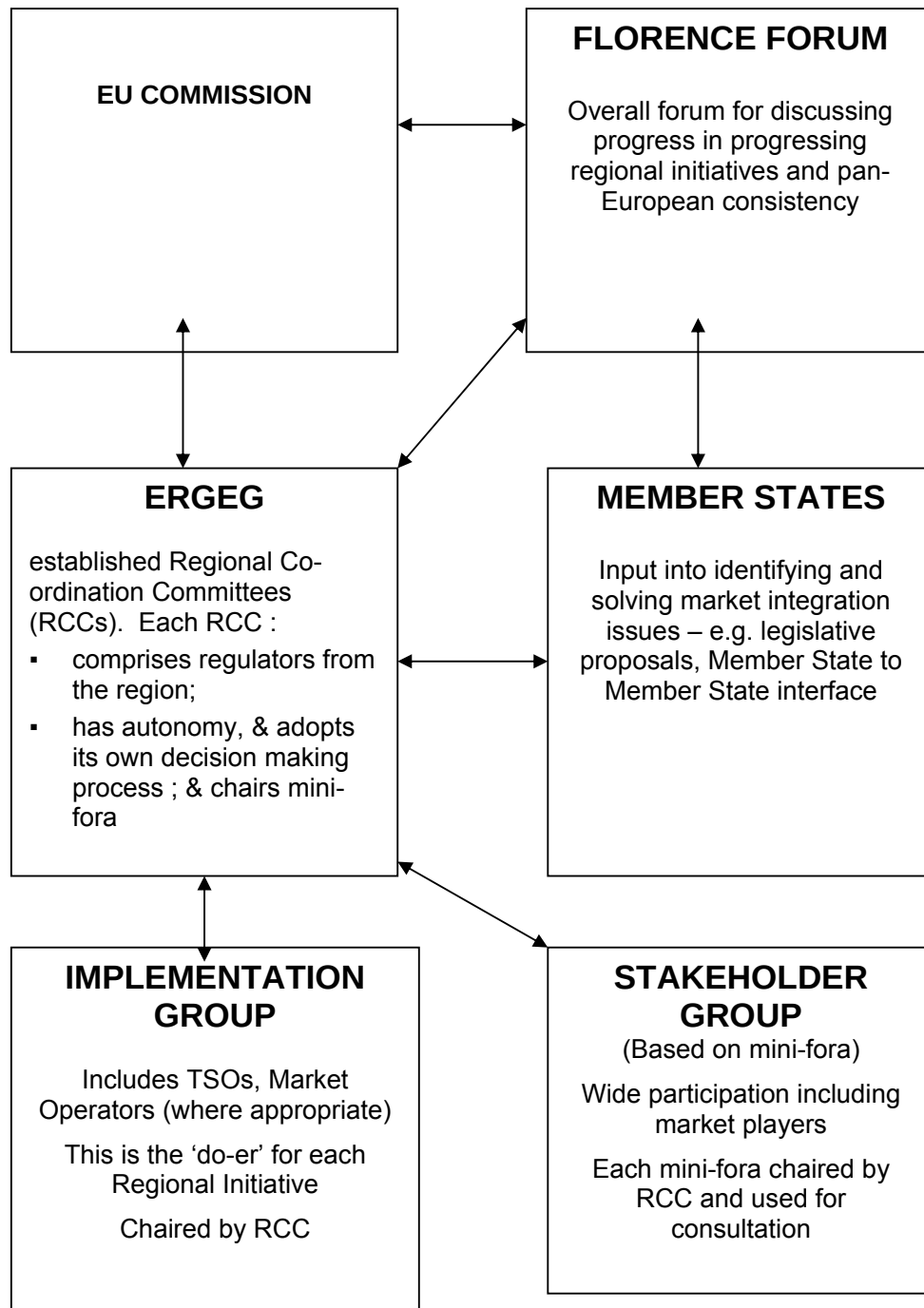
An organizational framework

- 3.36. Besides practical objectives and adequate activities to achieve them, it is particularly important that each regional initiative has a clearly defined organisational and

administrative framework for its future work, including the aspects of governance, decision making and conflict resolution. A suitable organisational framework for each regional initiative might therefore be the one illustrated in the figure.

- 3.37. Given that local circumstances, institutions, and existing initiatives vary, EREG would anticipate that each regional initiative will tailor an organisational framework to its own needs. However the framework must achieve results in accordance with the objectives above, and monitor and report on progress. Some regional initiatives may for example see regulators working closely with member states to identify and publish priority areas for action and action plans for solutions. Regulators and other institutions in countries that are part of more than one region may wish to combine and/or target resources as necessary.
- 3.38. At the core of the framework, EREG will establish Regional Co-ordination Committees (RCCs) which would comprise the regulators for each region. Each of the EREG's RCCs would have responsibility and authority for driving forward the work in their region. An RCC's role would include acting as overall co-ordinator of the tasks facing the Region and providing leadership, strategy and decisions. Each RCC will also consult stakeholders. The RCC's duties could therefore include the establishment and lead of the regional projects and activities such as mini fora, defining the way of work, involving stakeholders and setting up priorities, milestones and deliverables in line with the general EU/EREG objectives, in suitable collaboration with Member States and the Commission. Each RCC should also ensure compliance with the relevant EU legislation. Each RCC would also be responsible for reporting on the progress of their regional initiative through EREG to the Florence Forum.

Regional initiatives – Elements of an Organizational Framework



- 3.39. Given that the characteristics of each Region and its institutions, issues and existing initiatives differ, it will be appropriate for each RCC to have autonomy and flexibility regarding the governance procedures and approach it adopts, as well the geographical and other composition elements of the group. However this autonomy will need to occur within the boundaries of the given overall objectives for each Region. In addition, for pragmatic reasons and in order to foster a transparent, accountable and consistent approach, the organisational procedures, decision making and conflict resolution in each RCC may be drafted in accordance with EREG statutes and principles.
- 3.40. Each of the RCCs should report to EREG on progress and EREG will inform the European Commission, and Florence Forum periodically on the progress of work in the regions, including all the issues of importance and relevance for each region and for the European electricity market more widely.
- 3.41. An important task for each RCC will be to specify detailed roadmaps, milestones and deliverables in each Region. These roadmaps shall cover key milestones for 2-3 years, with a detailed project plan for the first year and general plan for successive years.
- 3.42. In undertaking its functions it will be important that each RCC recognises that regulators alone are unlikely to have the powers or resources to deliver by themselves a fully functioning regional market. Each RCC must involve, appropriately, each key stakeholder with such powers. Hence the organizational framework anticipates that an RCC will, among other things, work with Member State governments.
- 3.43. The organizational framework also anticipates that each RCC would establish and chair an Implementation Group (IG) or equivalent body. Each RCC would liaise closely with the IG and could for example request the IG to make proposals for action to deal with the priority issues identified by the RCC. The RCC would therefore need to meet with the IG on a regular and reasonably frequent basis in order to set out the issues that the IG will need to consider, and in order to monitor and assess progress that the IG is making in coming forward with proposals.

European Commission

- 3.44. It will be necessary to involve fully European Commission in each of the regional initiatives, particularly since it will be expected to help deliver some of the objectives in some regions, and it is important that the appropriate support for the establishment of each regional market is forthcoming. Each RCC should decide how best to achieve this. It would seem likely that each RCC will invite the Commission to attend RCC meetings. The RCCs will in addition need to commit to report to the Commission.

Member States

- 3.45. Clear political support for identifying and solving impediments to market integration will be particularly important for the regional initiatives. Indeed many of the existing regional initiatives, for example those described in the case studies in the EREG consultation paper, are underpinned by government to government agreements and / or government commitment to bring forth the necessary legislation. It is likely also to be the case that regulators lack a full legal basis to address issues outside national borders and so they may not be able to mandate fully all efforts concerning cross

border market integration. Member State support therefore will be particularly important in this regard.

- 3.46. Each RCC will need to decide how best to work with member state governments in order to progress its work. This should include a commitment by the RCC to report on progress to Member States.

Implementation Group

- 3.47. In order to deliver concrete progress 'on the ground', commitment and action will be required from the main stakeholders. These could include TSOs, market operators, and power exchanges, as well regulators from the relevant region. An Implementation Group (IG), comprising such stakeholders, should be able to propose, and commit to undertake, concrete actions in response to the priority issues identified at the RCC level. The RCC and IG should therefore maintain a close liaison.
- 3.48. Proposals of the IG should be subject to consultation of stakeholders. For this reason it would be helpful to establish a Stakeholder Group. Consultation should formally be with stakeholders, and this may include written consultation exercises, public hearings, and workshops. Stakeholders should have an opportunity here to express how solutions to market integration problems affect them and market functioning, and how solutions might best be conceived and implemented.

Stakeholder Group and Mini-fora

- 3.49. Given that the overall objective of the regional initiatives is to promote efficient trade between market participants, it will be crucial to involve these stakeholders in the regional initiatives. Market participants should for example be able to express their views on the need to address particular issues, how these issues might be addressed, and how market participants may be affected. Such consultation should be done in a full and transparent manner.
- 3.50. One important further element of this involvement will be the establishment of a further round of 'mini-fora'. Where appropriate and required, the representatives of the TSOs, traders, etc. may participate in the work of mini fora, bearing efficiency in mind. Overall direction and chairing of each mini-forum should be provided by the RCC, in suitable collaboration with the IG. Roles and responsibilities of all parties involved in the work of mini fora should be defined and agreed upon in advance, including here regulators, TSOs, traders, power exchanges, etc. Furthermore, the necessary commitment for a particular mini forum, on specific activities and tasks should be ensured by the parties required to do the job.

Reporting

- 3.51. An important element of the overall structure will be a requirement for regular reporting and updates. The RCCs should endeavour to keep EREG overall informed of initiatives, progress, and any reasons for delays in progress. EREG will take on the task of co-ordinating an overall position to the Florence Forum, presently scheduled for autumn 2006.

Timetable

- 3.52. ERGEG presently anticipates that each RCC will need to establish itself in early spring 2006. This could be done as part of the initial preparations for the first round of mini-fora anticipated in for June/July 2006. Each RCC would need to establish a governance structure for itself and identify priority actions. Following this each RCC would need to liaise with stakeholders in order to set in place the Implementation and Stakeholder Groups. In the roadmap below, the objectives have been summarized into the main phases, proposed as the general framework of the Steering Group priorities.

Indicative Timetable	Task
April / May 2006	Finalise regional groupings
	First meeting of each of ERGEG's Regional Co-ordination Committee : – Establish governance structure – Identify priority actions based on ERGEG Roadmap – Report to ERGEG
May/ June 2006	RCC's to invite TSO and any other relevant market operators to form an Implementation Group
June / July 2006	Each RCC to establish forward timetable for technical work. RCC's arrange and chair mini-fora, in suitable collaboration with IG
Late Summer 2006	Initial reports from RCCs to ERGEG
Autumn 2006	First ERGEG report on progress to Florence Forum
Post 2006	Each RCC progresses its identified issues, in accordance with its established timetable Each RCC monitors and reports progress