European Regulators Group for Electricity & Gas

ERGEG draft advice on the regulatory oversight of energy exchanges

An ERGEG Public Consultation Document

Ref: C10-WMS-13-03
5-APR-2011

Council of European Energy Regulators ASBL
28 rue le Titien, 1000 Bruxelles
Arrondissement judiciaire de Bruxelles
RPM 0861.035.445

INFORMATION PAGE

Abstract

On 18 May 2011, ERGEG launched a public consultation on its draft advice on the regulatory oversight of energy exchanges (Ref. C10-WMS-13-03). It is intended to serve as a background paper, which may be utilised in the discussion of the regulatory framework for an energy wholesale market integrity and transparency regulation.

Target Audience

Energy suppliers, traders, electricity and gas customers, electricity and gas industry, consumer representative groups, network operators, Member States, academics and other interested parties.

How to respond to this consultation

Deadline: **15 July 2011**

This public consultation is carried out through a dedicated online questionnaire on the European energy regulators´ website. To participate in the consultation please go to

http://www.energy-regulators.eu/portal/page/portal/EER_HOME/EER_CONSULT/OPEN%20PUBLIC%20CONSULTATIONS/Oversight%20of%20PXs/BG

and fill in the login request form. You will be provided with a login and technical instructions for the questionnaire.

If you have any queries relating to this consultation document or to the online consultation, please contact:

Ms Natalie McCoy
Tel. +32 (0) 2788 73 30
Email: Natalie.mccoy@ceer.eu

All responses except confidential material will be published on the website www.energy-regulators.eu.

Treatment of Confidential Responses

In the interest of transparency, ERGEG

i) will list the names of all respondents (whether confidential or not) or, alternatively, make public the number (but not the names) of confidential responses received;

ii) requests that any respondent requesting confidentiality submit those confidential aspects of their response by marking them as “confidential” in the dedicated online

questionnaire. ERGEG will publish all part of responses that are not marked confidential.

For further information on ERGEG's rules, see ERGEG Guidelines on Consultation Practices.

Related Documents

CEER/ERGEG documents

- ERGEG and CESR fact-finding results on pre- and post-trade transparency and trading oversight, Ref. CESR/08-527, 18 July 2008, http://www.energy-regulators.eu/portal/page/portal/EER_HOME/EER_PUBLICATIONS/CEER_ERGEG_PAPERS/Cross-Sectoral/2008/CESR%20ERGEG%20fact%20finding%20advice%20compiled%20final_0.pdf

- Market Abuse – ERGEG and CESR advice to the European Commission in the context of the Third Energy Package – Response to Question F.20, Ref. E08-FIS-07-04, 1 October 2008, http://www.energy-regulators.eu/portal/page/portal/EER_HOME/EER_PUBLICATIONS/CEER_ERGEG_PAPERS/Cross-Sectoral/2008/E08-FIS-07-04_%20MAD%20Advice.pdf

- Record-keeping, transparency and exchange of information – ERGEG and CESR advice to the European Commission in the context of the Third Energy Package, Ref. C08-FIS-07-03, 17 December 2008, http://www.energy-regulators.eu/portal/page/portal/EER_HOME/EER_PUBLICATIONS/CEER_ERGEG_PAPERS/Cross-Sectoral/2008/C08-FIS-07-03_Recordkeeping_2008-12-17.pdf

- ERGEG Advice on Comitology Guidelines on Fundamental Electricity Data Transparency, Ref: Ref: E10-ENM-27-03, 7 December 2010, http://www.energy-regulators.eu/portal/page/portal/EER_HOME/EER_CONSULT/CLOSED%20PUBLIC%20CONSULTATIONS/ELECTRICITY/Comitology%20Guideline%20Electricity%20Transparency/CD/E10-ENM-27-03_FEDT_7-Dec-2010.pdf

Other documents

- Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments.
- Directive 2003/6/EC of the European Parliament and of the Council of 28 January 2003 on insider dealing and market manipulation (market abuse).
- Proposal for a Regulation of the European Parliament and of the Council on energy market integrity and transparency of 8 December 2010 (COM(2010)726 final).

Table of Contents

EXECUTIVE SUMMARY

Regulatory oversight of energy exchanges currently differs in the EU Member States due to different national legislation requirements. Competencies and responsibilities are often divided between different authorities, for example the financial market supervisory authority, competition authorities, the energy regulator or others, and may overlap in some cases. That is why European energy regulators decided to elaborate best practices of supervision of energy exchanges and hubs, in order to align these arrangements in the interest of proper and adequate supervision and to support also greater EU market integration.

An internal survey was undertaken with support from NRAs to identify best practices of supervision of energy exchanges. Given the organisation of exchanges, the survey investigates the supervision framework and the monitoring tasks of the regulatory entities as well as misbehaviour treatment and transparency issues. The survey may thus serve as a background paper, which may be utilised in the discussion of the regulatory framework for an energy wholesale market integrity and transparency regulation.

The internal survey recommends that:

- Energy spot exchanges, the regulation of which is currently not harmonised at EU level, should in future be covered by the energy market integrity regime. In view of market coupling, there should be an obligation for energy exchanges to install and maintain a market surveillance department, regardless whether the exchange is a regulated market, a MTF or a currently unregulated market under MiFID. Such a market surveillance department should be sufficiently staffed to continuously monitor and analyse the daily exchange trading, the respect of market rules and the respect of other legal provisions. Any such market surveillance department of an energy exchange should cooperate with national energy regulators. The proper functioning of the market surveillance department should be supervised by a national regulator. In view of market coupling, there should also be an obligation for a close cooperation and exchange of trade data and information between market surveillance departments of different energy exchanges.
- Given the differing energy exchange rules, it should be considered if a harmonisation of legal and operational frameworks could enhance cooperation between European energy exchanges, and facilitate trading. The involvement of market participants is regarded positively by energy regulators.
- Provisions on market makers at energy markets could be elaborated.
- Regarding regulatory requirements for the publication of additional information, principal regulatory requirements should be set to make sure that the energy exchanges establish satisfactory routines.
- The experiences and competences of national energy regulators already monitoring energy wholesale markets could be an archetype for the future monitoring of energy wholesale markets across Europe.
- The results on the treatment of misbehaviours at energy exchanges back up the intention of creating a tailor made sector-specific market abuse framework for the energy wholesale market.
- In view of market coupling, energy regulators should be competent for the regulation of the market design of energy spot markets. This does not necessarily mean that energy regulators should regulate energy (spot) exchanges. This may be the case,

but at least there should be a close cooperation between energy regulators, financial regulators, market surveillance departments of energy exchanges and possibly competition authorities.

Background

This document is an ERGEG draft advice on the regulatory oversight of energy exchanges. It is intended to be utilised in the discussion of the regulatory framework for an energy wholesale market integrity and transparency regulation.

Objectives and contents of the document

The document will be used as an input to the discussion on the regulatory framework for an energy wholesale market integrity and transparency regulation. Beyond that, the specific issues addressed in this document include the history and organisation as well as the areas of the regulatory oversight of energy exchanges.

The document sets out that the regulatory oversight of energy exchanges currently differs in the EU Member States due to different national legislative requirements. Furthermore competencies and responsibilities are often divided between different authorities, for example the financial market supervisory authorities, competition authorities, energy regulators or others, and may overlap in some cases. The document investigates the supervision framework and the monitoring tasks of the regulatory entities as well as misbehaviour treatment and transparency issues and it identifies best practices of supervision of energy exchanges.

Public consultation and next steps

This document is an ERGEG public consultation paper, in line with the ERGEG guidelines on public consultations. The results of this public consultation will be duly evaluated and where applicable integrated into the final version of the ERGEG advice.

1 Introduction

Energy exchanges help creating an efficient and liquid energy wholesale market as called for by the European Commission. Because they are open to any participant, set price signals for standardised products, and offer anonymous transactions, they help creating more transparency and competitive prices, which foster competitiveness within the internal market. They also help creating adequate price signals for detecting potential security of supply or particularly generation adequacy problems.

Power exchanges have emerged in many countries over the last years as a result of the increasing liberalisation of their electricity sectors. Their creation is a quasi-necessary step in markets where different types of market participants have the option to decide their level of production and demand as well as their transaction counterparties. Energy exchanges allow participants to trade physical spot products as well as futures products.

Unlike bilateral trading or brokered trading, energy exchanges have strict exchange rules which contribute to secure transactions for the participants. Energy exchanges offer participants to deal standardised products, in terms of maturity and structure. They also offer clearing services which limit the counterparty failure risks.

Energy exchanges have also an important role in market coupling, since they allow implicit border capacity auctions.

Regulatory oversight of energy exchanges currently differs in the EU Member States due to different national legislation requirements. Competencies and responsibilities are sometimes divided between different authorities, e.g. financial market supervisory authorities, competition authorities, energy regulators or others, and may overlap in some cases. That is why the European energy regulators decided to elaborate best practices of supervision of energy exchanges and gas hubs, in order to align these arrangements in the interest of proper and adequate supervision and to also support greater EU market integration.

To identify best practices of supervision and to investigate the main regulatory oversight aspects of energy exchanges, an internal survey was undertaken gathering input from national regulatory authorities (NRAs). It included the organisation of energy exchanges, especially with regard to the role of internal and external governance bodies in the initial establishment of market rules. Moreover it investigated the diversity of prerequisites to trade at European exchanges and the structure of fees as well as their approval procedure. The appointment of market makers, and the information published was also under scrutiny.

Given the organisation of exchanges, the current document also investigates the supervision framework and the monitoring tasks of the regulatory entities. Misbehaviour treatment is also examined. Regarding transparency, obligations which need to be fulfilled by exchanges, or by participants when trading at exchanges, are to be observed.

Information gathered in this document relies on input provided by 14 European energy regulators, and cover electricity or gas exchanges.

The current document deals with exchanges as entities, as its objective is to describe the regulatory oversight of market places where the price formation processes take place without addressing any other technical services such as those offered by gas hubs.

1.1 Questions for Public Consultation

European Energy Regulators do not want to be prescriptive in terms of the detailed issues that we would like stakeholders to consider and welcome responses on any aspect of the oversight of energy exchanges.

In addition to inviting stakeholders and market participants to respond generally to this consultation and participate in the discussions on this document, ERGEG seeks the opinion of the respondents on a number of specific issues related to the scope and applicability of the document.

Stakeholders are therefore invited to reply and provide comments on the following list of questions which is not exhaustive:

1. In your view, is there a need to create EU level requirements for the organisation, functioning and regulatory oversight of energy exchanges not falling within the scope of MiFID? If yes, what should be the main goals and objectives to be fulfilled?

2. In your view, what are the remits of national energy regulators in supervising energy exchanges and how could a beneficial cooperation between them be organised, in particular for exchanges active under multiple national jurisdictions?

3. Should the regulation of energy spot exchanges in future be covered by the energy market integrity regulation or by a separate future legal proposal by the European Commission?

4. How could in your view a harmonisation of legal and operational frameworks stimulate the cooperation of the European energy exchanges and what is the best way to involve the market/exchange participants?

5. Which criteria should a European framework for market makers include to avoid potential conflicts of interests?

6. How could national energy regulators better work towards publishing of price sensitive information as e.g. foreseen in the ERGEG advice on Guidelines on Fundamental Electricity Data Transparency to increase the level of transparency?

7. Which measures could in your view lead to a sufficient cooperation of market surveillance departments of the energy exchanges and the national energy regulators?

8. What are in your view minimum standards for a harmonised approach to protect energy exchanges from misbehaviours like market abuse?

2 History of energy exchanges

On grounds of energy market liberalisation, energy exchanges were founded incrementally all over Europe. There are respective origins of establishing an energy exchange due to different legal frameworks. In the gathering phase, information about the historic development and its consequential characteristics of the energy exchanges were inquired to outline the different historic backgrounds of existing exchanges.

In 1993, the first European energy exchange Nord Pool was founded in Norway. Only six years later, at the very beginning of energy market liberalisation in continental Europe, APX was established to operate as electricity exchange for the Netherlands. In the following years electricity exchanges started operation step by step mostly all over Europe. The development of gas exchanges started a few years after electricity exchange establishment.

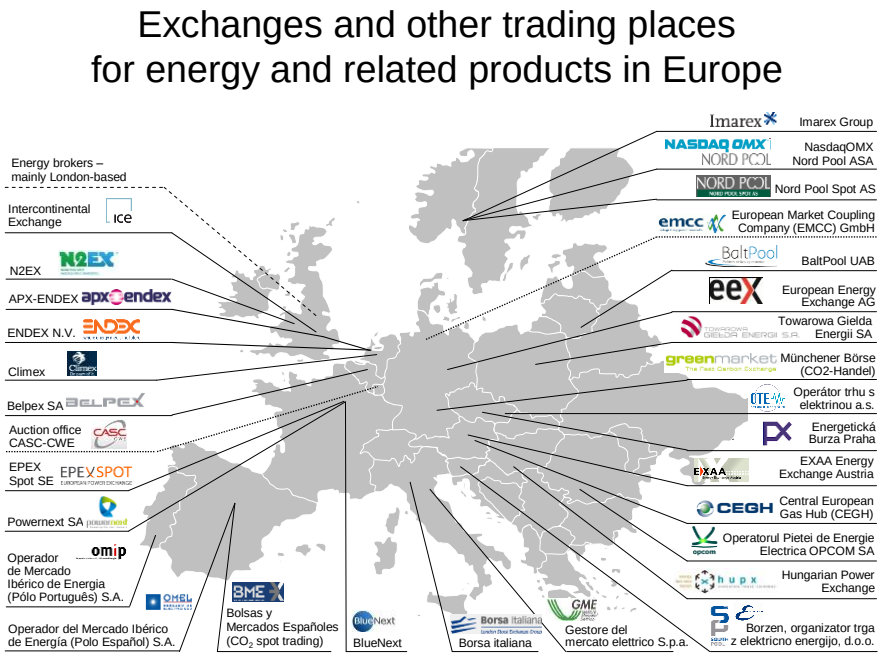


Figure 1: Energy and carbon exchanges in Europe
Source: European Energy Exchange

In the majority of cases, the prevalent initial trigger for the establishment of energy exchanges in Europe was commercial interest. This means that the company running the exchange established it without any legal obligations and considered it profitable to operate the business by charging fees to trading participants for providing the exchange services. There are, however, exceptions from this general rule. The Spanish power exchange OMEL (now involved in the market splitting with Portugal), the Portuguese exchange OMIP and the Romanian exchange OPCOM were established due to legal enforcement by the government. The history of the Nordic power exchange (Nord Pool Spot) can be referred back to 1971, when it was owned by an organisation of Norwegian producers. Today Nord Pool Spot is regulated by licences issued pursuant to the Norwegian Energy Act, and the power

exchange shall contribute to the fulfilment of the purpose of the act which is to ensure socio-economic efficient trade.

There are only some European exchanges which were developed with the involvement of the respective energy regulator. The Norwegian energy regulator granted a license for the power exchange for physical power and was involved when the power exchange was established. The Portuguese regulator was involved through discussions in the MIBEL Council of Regulators, and Romania's energy regulator granted the license for the power exchange, gradually issued and approved the market rules and established the market monitoring system. The Netherlands Competition Authority (NMa) advised the Ministry on the regulation of APX. Most other NRAs were not or not formally involved in the development of energy exchanges.

The development of liquidity differs strongly between exchanges and depends on market maturity, market size and the products traded. Spot electricity products represent between 7 and 72% of annual national consumption, whereas futures electricity products stand for 17% to 189% of annual national consumption. This is due to the fact that future products volumes can be much higher than spot products volumes, since they are traded for a longer time period in advance. As for gas liquidity, a couple of spot exchanges have recently been launched, and their liquidity is still low. APX Netherlands stands out with its gas spot products representing 160% of its national gas consumption.

Below figure shows the year-on-year development in electricity trading volumes in Scandinavia, the Netherlands, France and Germany from 2001 to 2009.

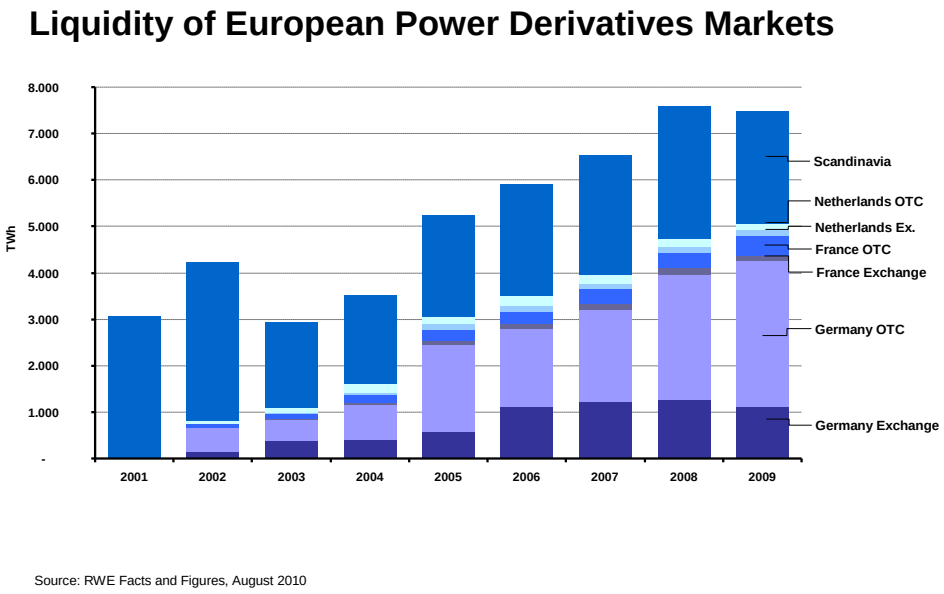


Figure 2: Liquidity of European Power Derivatives Markets
Source: RWE Facts and Figures, August 2010

Efficient capacity allocation through market coupling arrangements should facilitate price convergence throughout Europe. In terms of responsibility, coordinated order matching is for

the exchanges what the coordinated capacity calculation is for the TSOs. Market integration can progress quickly through multi-regional price coupling, building on existing infrastructures and regulatory frameworks, albeit with some degree of harmonisation when technically needed. Developments ahead will however be challenging for energy exchanges, TSOs and energy regulators.

3 Organisation of energy exchanges

Energy exchanges trade an array of products, both physical and derivative. Some of the activities are of a monopolistic nature (either by their nature or because a legal monopoly can be created by Member States), while others are carried out in competitive markets. These two facts affect heavily the way in which each energy exchange is organised and regulated at European and national level.

In most European transmission systems there is only one energy exchange operating for delivery. Information from NRAs indicated a de-facto monopoly (despite market platforms such as broker screens). In Germany, Austria, Romania and Slovenia there are more than one energy exchange in the same transmission zone.

3.1 Legal status of energy exchanges

In the absence of an EU sector-specific regulation, MiFID is currently the only legal framework regulating energy derivatives exchanges at EU level. Under MiFID[1], trading venues are distinguished as regulated markets or multilateral trading facilities (MTFs) defined in Article 4 of MiFID. It applies to financial instruments in the form of commodity derivatives traded at regulated markets and MTFs, hence also to energy exchanges.

Pursuant to Article 4(14) of MiFID, 'Regulated market' (RM) means a multilateral system operated and/or managed by a market operator, which brings together or facilitates the bringing together of multiple third party buying and selling interests in financial instruments – in the system and in accordance with its nondiscretionary rules – in a way that results in a contract, in respect of the financial instruments admitted to trading under its rules and/or systems, and which is authorised and functions regularly and in accordance with the provisions of Title III of MiFID.

The list of regulated markets is published on a yearly basis in the Official Journal of the EU.[2]

Pursuant to Article 4(15) of MiFID, 'Multilateral trading facility (MTF)' means a multilateral system, operated by an investment firm or a market operator, which brings together multiple third-party buying and selling interests in financial instruments – in the system and in accordance with non-discretionary rules – in a way that results in a contract in accordance with the provisions of Title II of MiFID.

The requirements affect amongst other things market transparency, market models and competition between trading venues. A market model of a trading venue can be characterised by three key structural elements:

[1] Markets in Financial Instruments Directive 2004/39/EC.

[2] See, e.g., OJ C 158 of 11.7.2009, p. 3.

- Trading frequency and price determination;
- Pre-trade transparency;
- Post-trade transparency.

MiFID deals with energy derivatives instruments such as:

- futures products traded on RMs and MTFs;
- forward products traded OTC that are cash-settled;
- forward products traded OTC that are physically settled if standardised.

The fundamental difference between a RM and a MTF from a regulatory point of view concerns the organisational requirements for monitoring of compliance with the rules of the market venue and with other legal requirements. At regulated markets, this task is normally carried out by a sufficiently staffed market surveillance department supervised by the competent regulatory authority.

Box 1: Differences between MTFs and Regulated Markets in MiFID

Article 26 MiFID
Monitoring of compliance with the rules of the MTF and with other legal obligations

1. Member States shall require that investment firms and market operators operating an MTF establish and maintain effective arrangements and procedures, relevant to the MTF, for the regular monitoring of the compliance by its users with its rules. Investment firms and market operators operating an MTF shall monitor the transactions undertaken by their users under their systems in order to identify breaches of those rules, disorderly trading conditions or conduct that may involve market abuse.
2. Member States shall require investment firms and market operators operating an MTF to report significant breaches of its rules or disorderly trading conditions or conduct that may involve market abuse to the competent authority. Member States shall also require investment firms and market operators operating an MTF to supply the relevant information without delay to the authority competent for the investigation and prosecution of market abuse and to provide full assistance to the latter in investigating and prosecuting market abuse occurring on or through its systems.

Article 39 MiFID
Organisational requirements
Member States shall require the regulated market:

(a) to have arrangements to identify clearly and manage the potential adverse consequences, for the operation of the regulated market or for its participants, of any conflict of interest between the interest of the regulated market, ist owners or its operator and the sound functioning of the regulated market, and in particular where such conflicts of interest might prove prejudicial to the accomplishment of any functions delegated to the regulated market by the competent authority;
(b) to be adequately equipped to manage the risks to which it is exposed, to implement appropriate arrangements and systems to identify all significant risks to its operation, and to put in place effective measures to mitigate those risks;
(c) to have arrangements for the sound management of the technical operations of the system, including the establishment of effective contingency arrangements to cope with risks of systems disruptions;
(d) to have transparent and non‑discretionary rules and procedures that provide for fair and orderly trading and establish objective criteria for the efficient execution of orders;
(e) to have effective arrangements to facilitate the efficient and timely finalisation of the transactions executed under its systems;

(f) to have available, at the time of authorisation and on an ongoing basis, sufficient financial resources to facilitate its orderly functioning, having regard to the nature and extent of the transactions concluded on the market and the range and degree of the risks to which it is exposed.

Article 43 MiFID
Monitoring of compliance with the rules of the regulated market and with other legal obligations

1. Member States shall require that regulated markets establish and maintain effective arrangements and procedures for the regular monitoring of the compliance by their members or participants with their rules. Regulated markets shall monitor the transactions undertaken by their members or participants under their systems in order to identify breaches of those rules, disorderly trading conditions or conduct that may involve market abuse.
2. Member States shall require the operators of the regulated markets to report significant breaches of their rules or disorderly trading conditions or conduct that may involve market abuse to the competent authority of the regulated market. Member States shall also require the operator of the regulated market to supply the relevant information without delay to the authority competent for the investigation and prosecution of market abuse on the regulated market and to provide full assistance to the latter in investigating and prosecuting market abuse occurring on or through the systems of the regulated market.

Spot energy venues are not covered by MiFID. There are therefore no rules at European level obliging Member States to require *inter alia* a monitoring of compliance with self-regulated rules of the market place or with other legal obligations. As long as spot energy markets are not an annex to a regulated market or MTF, such markets are considered as unregulated markets under MiFID. This is why some Member States, under their national rules, apply the MiFID rules on MTFs and/or RM mutatis mutandis also to spot markets. However, since these spot markets are not covered by MiFID, they cannot benefit from the passport-function of MiFID for operations in other Member States.

3.2 The definition of the exchange rules

Basically, the energy exchanges distinguish between three types of rules: exchange / trading rules, clearing / settlement rules and IT requirements. The conditions contain very different specifications for the trading at the respective energy exchange. For example, trading rules mostly describe financial issues including collaterals, payment procedures and bank accounts. Concerning settlement rules, the trader must appoint an appropriate clearing bank. Some energy exchanges provide a trading platform and demand a special IT software or infrastructure (e.g. data transmission) from the trader.

The energy exchanges included in the survey provide an internal body which elaborates new market rules. Governance bodies are only involved at the end of the development process by an approval act.

In most of the indicated energy exchanges, market participants are involved in the elaboration of new rules. The national energy regulators or other external entities are not involved in such elaboration procedures. Dependent on the respective energy exchange, the participants develop new rules in different ways. At the Central European Gas Hub (CEGH, Austria) EFET and customers discuss new rules through workshops. At the German EEX, it is established by law that the Management Board of the exchange proposes and the Exchange Council (i.e. the elected representation of market participants) approves the market rules. The energy exchanges in Belgium, France, Norway and the Netherlands

established a separate internal body with market participants for that purpose. A so called "Market Agent Committee" enables the market participants in Portugal to take part in the elaboration of the national energy exchanges rules (OMIP). In Romania, new rules have to be agreed in a public consultation. GME S.p.A. (The Italian Ministry of Economy and Finance is the single shareholder of GSE S.p.A., which entirely owns GME S.p.A.) may propose amendments to market rules and notify them to all parties concerned. Then it submits its amendments to the approval of the Minister of Economic Development who decides after having heard the opinion of the Italian energy regulator AEEG. This procedure is not applied to urgent amendments having the purpose of safeguarding the proper functioning of the Italian market. Five energy exchanges do not foresee the possibility for market participants to influence or to initiate the elaboration process.

Except for Slovenia, all answers to the internal survey pointed out that different government bodies (such as the Ministry for Economic Affairs, the Exchange Supervisory Authority or the national financial regulator) are authorised to approve the rules. Romania and Norway were indicated as the countries in which the national energy regulator is competent to approve new market rules. The different government bodies are not designated for further activities within the procedure of setting the rules. Furthermore, the given answers indicate a strict binding character of these rules. However, their relevance exceeds the scope of this ERGEG advice.

3.3 Prerequisites to be fulfilled by market parties for trading at the exchange

Conclusion of a contract
Based on the available information, the conclusion of a contract is a prerequisite for trading at most energy exchanges, both physical and derivative markets.

Entrance fees
In addition to a contract, an entrance fee or an annual fee has to be paid as a prerequisite for trading in most cases. In the Netherlands the annual fee is invoiced monthly to pay.

Credit assessment
Other prerequisites are collaterals or bank guarantees and credit assessment. In most exchanges, a credit assessment as well as an annual fee is prerequisite for trading at the exchange.

Additional requirements
When entering a contract in order to become a participant at the energy exchange, the participant usually also accepts to be bound by the regulations at the exchange, e.g. disclosure requirements, rules regarding insider trading and market manipulation. In some cases, the participants are required to provide a declaration provided by the relevant Ministry (i.e. EPEX Spot France).

3.4 The definition of fees management and fees structure

Usually there are fees to be paid for trading at energy exchanges. In most cases the energy exchanges decide on the level and structure of the fees.

Generally there are different kinds of fees like transaction fees, fees per quantity unit and fees per period of time such as annual fixed fees, one time entry fees or variable trading fees. Most energy exchanges have a fee per quantity. Often, there is also an additional fee per period of time. There are very few energy exchanges which have a fee per period of time but no fee per quantity unit. Furthermore, there are several energy exchanges that charge other kind of fees. For example there is an entrance fee at the Austrian Power Exchange EXAA, at EPEX Spot in France, and at the Dutch APX-Endex.

Most European energy exchanges can decide on the level of their fees without the approval of a public authority. At the Portuguese OMIP the regulatory authority has to approve the fees. At OMEL, the fees are set by law and at the Romania energy exchange the regulator is even in charge of setting the fees. At Nord Pool Spot the level of the fees are not regulated directly, but the revenue from the organisation and operation of the market place shall cover the costs and provide a reasonable profit through efficient operations. At the Austrian Gas exchange of Wiener Börse the question whether fees need to be approved by an authority is currently under discussion.

Furthermore, it was investigated whether these fees were publicly available. This was the case for all exchanges. At most energy exchanges the publication of the fees is required by law.

It is currently under consideration whether financial transmission rights (FTRs) should be the exclusive tools for cross-border capacity allocation (as previously discuss by the Ad Hoc Advisory Group, AHAG and mentioned in the draft framework guidelines on capacity allocation and congestion management for electricity[3]). Against this background, the question whether fees structure and fees level need regulation will probably gain in importance in the near future. This is due to the fact that cross-border trade of energy with FTRs always involves energy exchanges and this will lead to a monopoly market position of these exchanges. Therefore the question who decides on the amount of fees and who is in charge of controlling or approving theses fees becomes crucial.

3.5 Market makers

Market makers exist at most exchanges – not only at energy exchanges. It is their task to place bids on the buy and sell side in order to guarantee the liquidity of the market. MiFID defines market maker as a person who holds himself out on the financial markets on a continuous basis as being willing to deal on own account by buying and selling financial instruments against his proprietary capital at prices defined by him (Art. 4(8) MiFID).

At some exchanges e.g. EPEX Spot, Nord Pool Spot and at the Italian IPEX there are no market makers. Several respondents stated that there have been market makers since the beginning of trading at their energy exchange. Most of the market makers at European energy exchanges were not officially appointed.

[3] ACER Framework Guidelines on Capacity Allocation and Congestion Management for Electricity. Draft for Consultation, Ref. DFGC-2011-E-003, 11 April 2011, http://www.acer.europa.eu/portal/page/portal/ACER_HOME/Stakeholder_involvement/Public_consultatations/Open_Public_Consultations/PC-03_FG_Electricity_CAM_and_CM/Consultation_document

However, the selection process of market makers seems to be improvable as regards the establishment of objective and transparent criteria for their appointment. This is particularly necessary in view of potential conflicts of interests possibly arising if a market maker (or an affiliated company) is also producer.

3.6 Transparency and information published

The transparency obligations listed in this chapter should not be considered as exhaustive.

3.6.1 Exchange information published by the exchange

Based on the information available, most energy exchanges are publishing traded volumes, price signals, membership fee, contact details and product/service list. In the electricity markets, traded volumes are in general published daily as MWh.

Moreover, most energy exchanges are publishing number of members, but less than half of them publish number of *active* members. Other information published by some exchanges is e.g. number of trades.

The exchanges for electricity derivatives publish settlement prices, highest price traded, lowest price traded and/or bid and ask prices. The spot exchanges for electricity publish hourly spot market prices daily. Exchanges also publish differentiated data between sell and buy activities (e.g. bidding curves or bid – offer spread information), and types of standard energy exchange contracts.

Since Italy has a zonal market system depending on the grid situation, the Italian IPEX publishes the following types of information: zones characterising the Spot Electricity Market; admissible hourly electricity transmission capacity limits between geographical zones and regarding zones interconnected with neighbouring countries; estimated hourly electricity demand in each geographical zone; data of offers/bids submitted into the Spot Electricity Market and data of offers/bids accepted in the Forward Electricity Market.

If relevant/applicable, the price formation mechanism of the power exchange for day-ahead auctions is publicly available for most of the investigated exchanges. The price formation mechanism of the power exchange for day-ahead continuous prices is publicly available only for some exchanges when relevant.

3.6.2 Other transparency information published by the exchange

A few exchanges charge data service fees for additional information (e.g. ICE, APX). Transparency information published is e.g. data on electricity generation and information from TSO on trading capacity.

In the Nordic Market the disclosure of relevant information is given electronically using an internet-based application Urgent Market Messages (UMM) at Nord Pool ASA[4]/Nord Pool Spot AS. The information shall be disclosed immediately, and no later than 60 minutes after the occurrence of the event which leads to the relevant information.

The contractual basis for UMMs at Nord Pool Spot AS is the following:

1. Disclosure of UMM information and power system fundamentals made by TSOs

There is a Data Publication Agreement between Nord Pool Spot (NPS) AS and TSOs within Nordel concerning continuous disclosure by TSOs and subsequent publication by NPS of primarily "price sensitive information" as further detailed in the Agreement.

In general terms though it primarily covers UMM reporting of planned outages, unplanned outages (failures) and special information linked to, primarily, the main transmission grid as well as continuous reporting of hourly power system data such as for example overall production, consumption, cross-border flows and Regulating Power Market data.

2. Disclosure of UMM information made by market participants

Participants in Nord Pool Spot's Physical Markets as well as participants in Nord Pool ASA's financial market are obliged to disclose via the UMM system "price sensitive information" regarding, primarily, production and consumption facilities as further explained in the respective rulebooks for trading.

As regards inside information, it is important to establish disclosure requirements. In the Nordic Market, the term "inside information" is defined as "any information of a precise nature which has not been made public relating directly or indirectly, to one or more Instruments, and which participants and clearing customers would expect to receive in accordance with accepted market practice."

According to the disclosure requirements, participants should disclose any information relating to the participant's own business or facilities (for production, consumption or transmission of electricity) that has not yet been made public and is likely to have a significant effect on the prices of the products traded at the power exchange if made public. The disclosure requirements should e. g. cover:

- Any planned outage, limitation, expansion or dismantling of capacity in the next 6-weeks period of more than 100 MW for one generator, consumption or transmission facility, or more than 200 MW for one production station, including changes of such plans;

- Any planned outage, limitation, expansion or dismantling of capacity of more than 400 MW for one production station, consumption or transmission facility for the current calendar year and three calendar years forward, including changes of such plans;

[4] Change of name to NASDAQ OMX Oslo ASA from 1.11.2010.

- Any unplanned outage or failure relating to more than 100 MW for one generator, consumption or transmission facility, and more than 200 MW for one production station, including updates on such outages or failures;

- Any other information that is likely to have a significant effect on the prices of one or more instruments if made public.

To achieve fair market conditions and reduce information asymmetries, all market participants should have access to all relevant information. Traded volumes and prices on all products should be published. Further, data on electricity generation should be published. This includes e.g. installed capacity, information on planned and unplanned outages, filling rate of water reservoirs and ex-post data on actual generation. Further, ex-ante information on scheduled unavailability of significant consumption units and ex-post information on unplanned unavailability of significant consumption units should be published.

In 2009, EEX and German TSOs created a new Transparency Platform for the Power Market covering German and Austrian data. On the EEX transparency platform market-relevant generation and consumption data is published at a central and neutral site, close to the market, in order to increase transparency on the wholesale market. The platform was established by the four German TSOs, Amprion GmbH, EnBW Transportnetze AG, transpower stromübertragungs gmbh and 50Hertz Transmission GmbH, which are legally obliged to publish power plant and consumption data, together with the European Energy Exchange AG (EEX). The platform is operated by EEX and it replaces the previous EEX transparency platform, where information was published on a voluntary basis.

The German energy regulator is responsible for examining whether the implementation of the publication requirements is carried out properly. In this context, it has to examine in particular whether a company providing data has made the data available on time and to the required extent. Usually, the transmission system operators provide this information to the Federal Network Agency upon request. The German energy regulator does not have a permanent right of access to the data platform.

As the operator of the platform, EEX discharges, in particular, the following tasks in processing the data:

- Plausibility checks;
- Anonymisation and aggregation;
- Publication.

The generation and consumption data intended for publication is divided into two categories:

1. Statutory publication requirements of the Transmission System Operators:

These publications are based on the “Congestion Management Guidelines“ (CM Guidelines, Annex to the EC Directive No. 1228/2003) and section 4.3 of the “Report on Transparency” which is interpreting the binding requirements of the CM Guidelines and was prepared under

the aegis of the German energy regulator for the Northern European region. These publication requirements are available at the website of the German energy regulator.

2. Voluntary commitment of the market participants:

This data was also published on the previous EEX transparency platform for generation.

3.6.3 Assessing the liquidity of the exchanges

Based on the received responses, market liquidity is assessed from one or more of the following indicators: churn rate, the Herfindahl-Hirschman Index, the variety of actors and traded volumes.

Moreover, according to NRAs, publishing of traded volume is sufficient to assess the market liquidity. All power exchanges except one publish traded volume.

3.6.4 Ex-post trade transparency requirements

As a general principle, NRAs share the view that the exchanges should be required to publish ex-post trade data.

4 Area of the regulatory oversight

4.1 The regulatory framework and the regulation of energy exchanges

Energy exchanges are normally either regulated by the government, by the national energy regulator and/or, by the national financial regulator. The energy exchanges of Spain and Portugal (OMEL and OMIP) are jointly supervised by the MIBEL council of regulators. The German EEX is regulated by the Exchange Supervisory Authority, the Nord Pool Spot AS by the Norwegian energy regulator and the Nordic derivatives market Nord Pool ASA is regulated by the Financial Supervisory Authority of Norway. Whilst the regulation of energy derivatives markets is harmonised at European level by MiFID, the regulation of energy spot markets differs from Member State to Member State.

Regulation of the exchange *normally* means in EU and national financial market regulation:

- The licensing (or right of closure) of the exchange;
- The supervision of the orderly function of exchange operations (including the price formation process) and the exchange transaction processing;
- The safe-guarding of the compliance with the exchange rules.

Regulation within the MiFID regime depends on the traded products and only covers financial instruments. Therefore, derivative markets at energy exchanges are regulated by national financial regulators.

For most energy exchanges, the question of separate regulation for spot and financial products is not applicable. At Powernext (gas, France) and CEGH (Austria) a different regulation concerning spot and financial products is provided. For many other exchanges no further differentiation in the regulation between physical and financial products exists.

None of the indicated exchanges is exempted from regulation by an external entity except EPEX Spot which is only subjected to an oversight regulation from the energy regulator. The French energy regulator, CRE does not have any explicit monitoring duties related to exchanges services.

The organisational structure of energy exchanges may foresee a regulatory role for an internal entity. This may involve market surveillance at the exchange.

Box 2: Tasks of a market surveillance department

A *market surveillance department* of an exchange normally continuously monitors all trading activities in the spot and derivatives markets *on a daily basis* and conducts investigations of possible breaches on laws and regulations. This monitoring is normally carried out under the systems of the exchange and covers all trading data of the exchange, i.e. matched trades *and* unmatched orders. It thus ensures the correctness of pricing mechanisms, the transparency of price relevant information and the integrity of the market. Its findings may not only involve breaches of exchange rules, but also disorderly trading conditions which may become a reason for amendments of the exchange / trading rules. Conduct that may involve market abuse has to be immediately reported to the competent regulatory authority. The proper functioning of the market surveillance is itself subject to the regulation through a regulatory authority, normally the exchange regulatory authority.

The supervisory board and the company management of the APX fulfil the obligation of a general market oversight and elaborate rules. An assigned Compliance Manager of the CEGH reports to the Austrian regulatory authority E-Control. At Nord Pool Spot the Market Surveillance monitors the market participants' orders and trades. Furthermore, the Surveillance may also request information about physical OTC-trades for market participants at NPS' markets. Further, the Norwegian energy regulator and the Norwegian Competition Authority are monitoring the Norwegian generators bidding at NPS. Similar rules apply to Nord Pool's derivatives market. At EEX, an independent market surveillance department collects and analyses all exchange and clearing data (including cleared OTC trades) and reports to the exchange supervisory authority. The Management Board of the EPEX Spot elaborates the relevant rules and regulations amongst the relevant agreements with the exchange members through an exchange council. A market surveillance officer collects and analyses the exchange data. At the Italian IPEX, market rules are prepared by the market operator (GME S.p.A) and approved by the Minister of Economic Development, after having heard the opinion of the Italian energy authority (AEEG).

Box 3: Regulation of Nord Pool Spot AS

Nord Pool Spot AS (NPS) runs the Nordic market place for physical power, offering both day-ahead and intra-day markets to its participants. In the preparatory work to the Norwegian Energy Act, the Ministry stated that the marketplace should have two main functions:

- Administration of the market place for physical power by facilitating daily bidding and price determination;
- Clearing of all contracts entered on the marketplace, i.e. enter as the central counter party in all trades, guaranteeing settlement for trade and anonymity for participants.

NPS is owned by the Nordic Transmission System Operators.

NPS is regulated by the Norwegian Energy regulator, Norwegian Water Resources and Energy Directorate (NVE). Since 1 February 2002 there have been guidelines on Nordic cooperation in the regulation of NPS. With the guidelines NVE wanted to facilitate a closer collaboration with the regulators in Denmark, Finland and Sweden. The guidelines are not legally binding, but considered as a memorandum of understanding. NPS operates within the framework settled by both the market place licence issued by NVE and the licence for cross-border power exchange issued by the Ministry of Petroleum and Energy. Both licences are issued pursuant to the Norwegian Energy Act of 1990.

The Market Place Licence states that the concessionaire shall:

- Contribute to efficient price formation and appropriate energy flows;
- Act in a neutral and non-discriminatory manner, e.g. ensuring all parties neutral and efficient access to information that is of importance to determining prices;
- Design a suitable infrastructure, regulations for trade and for contracts between parties, as well as systems for security and settlement that ensure confidence and predictability for the parties;
- Establish appropriate procedures to monitor the behaviour of parties in the organised market place (market monitoring);
- Have an advisory board with broad representation from the participants in the market;
- Inform NVE of changes to its organisation, ownership situation, or activities, about amendments to contracts with market parties or associated regulations and any changes the concessionaire is going to undertake that have or may have an influence on price formation. Material changes to the concessionaire's organisation, ownership situation, and activities or material changes that have or may have an influence on price formation must be approved by NVE before the changes are put into effect. The assessments of the advisory board and any comments from market parties must be presented to NVE.

Further, the market place licence regulates the concessionaire’s economic situation:

- The concessionaire’s revenue from the organisation and operation of the market place shall cover the costs and provide a reasonable profit through efficient operations;
- The concessionaire shall have adequate liable capital in relation to the activities being operated.

The market monitoring shall contribute to ensuring that the parties behave in accordance with the objectives of the Energy Act and regulations issued pursuant to this act. Further, the Financial Supervisory Authority of Norway requires the establishment of an internal market surveillance by Nord Pool ASA, and NPS’ Market Surveillance cooperates with Nord Pool ASA’s Market Surveillance in a joint function.

In order to become a participant at NPS, the market actor has to sign a participant agreement, and thereby accepts to be bound by the NPS Rulebook. According to the Rulebook, the participants shall not engage in market manipulation as defined in the Rulebook. Further, regulations lay down in the Norwegian Competition Act regarding misuse

of dominant position also applies.

The main task for market surveillance is to monitor the market participants' orders, trades and reporting of non-exchange trades in the financial market, as well as bidding in the physical market. The Market Surveillance NPS might ask for access to physical OTC contracts traded by participants at NPS' markets. The market surveillance also monitors possible abuse of the interaction between the two markets. Further, the market surveillance is in close and continuous dialogue with the Nordic Transmission System Operators with respect to their role in the information of trading capacities within the Nordic electricity exchange area.

In Norway, NVE and the Norwegian Competition Authority is monitoring the Norwegian generators bidding at NPS. NVE and the Norwegian Competition Authority have developed a model for monitoring of the competition in the market where the actual market price is compared to an expected price calculated by a model that simulates an efficient utilisation of reservoir-water (estimation of water values). Differences that can not be explained as price-taker behaviour should be investigated by looking at the different participants bidding on the market place. As a part of this process, NVE has the full mandate to collect information about the bidding from NPS. Within the Norwegian energy act and the market place licence the possibility of asking for data both for the Norwegian authorities and also for the authorities in the other Nordic countries are quite extensive.

While NVE is looking into the bidding of Norwegian generators only, the Market Surveillance at NPS is looking at the bids from all market participants at the Nordic market place.

Nord Pool ASA
The derivatives market is operated by Nord Pool ASA. Nord Pool was licensed as a regulated exchange and clearinghouse in 2002, and is regulated by the Financial Supervisory Authority of Norway. Nord Pool ASA is owned by Nasdaq OMX.

Box 4 : Regulation of the power exchange APX-Endex

The Dutch Electricity and Gas Acts authorise the appointment of an electricity and gas exchange by the Minister of Economic Affairs, Agriculture and Innovation of the Netherlands. APX BV – currently APX-Endex BV – has been appointed as an electricity exchange operator for the day-ahead market in 2006. In the appointment process the Minister has assessed and approved the request of APX BV and its Rules and Regulations on the basis of the criteria independency, impartiality, security of supply, financial solidity, confidentiality and feasibility. This was a once and for all appointment, but not of an exclusive character. Other exchanges may also be appointed. The Electricity Act at that time contained no provisions which would enable the Netherlands Competition Authority (NMa), which comprises the Dutch Office for Energy Regulation, to supervise whether APX-Endex behaves according to the provisions of the Ministerial Rule that forms the basis for the appointment as an electricity exchange or regulate directly the activities of the APX while in operation.

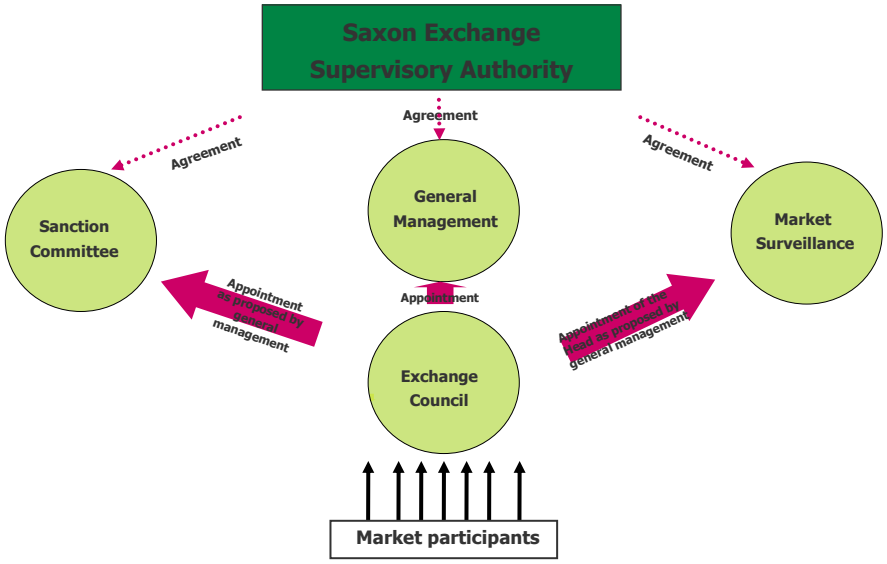
After completion of the approval procedure the Electricity Act has been amended, so possibilities have been created to add conditions in the form of regulations and restrictions in the approval procedure. These will enable NMa to supervise and regulate the activities of newly appointed power exchanges if necessary.

Nevertheless, NMa at the moment supervises a substantial part of APX-Endex activities on the day-ahead electricity market indirectly, since it has approved the power grid code which defines among others the obligations for APX-Endex with regard to the order matching functions it has to perform in the process of market coupling within the Central-West European region (which consist of the coupled markets of Netherlands, France, Belgium, Germany and Luxemburg), which has been launched in November 2010.

Box 5: Regulation of the energy exchange EEX

The European Energy Exchange (EEX) in Leipzig, Germany, is a public-law institution operated by the private law companies EEX AG and EPD GmbH licensed and supervised by the Saxon State Ministry of Economic Affairs, Labour and Transport (SMWA) as exchange supervisory authority under the German Exchange Act. EEX is a regulated market pursuant to MiFID. The German Exchange Act applies the MiFID-rules on regulated markets *mutatis mutandis* also for commodity spot markets. EEX is governed by its bodies, the exchange council as representative body of the market participants, the exchange management, the market surveillance and the exchange sanction committee.

The EEX bodies



Source: Exchange Supervisory Authority of EEX

In 2009, the power spot market of EEX was merged with the power spot market of Powernext to the common power spot exchange in Paris, EPEX Spot. In exchange, the French power derivatives market was transferred to EEX and forms a submarket of EEX. The prerequisites of the architectures of EEX and Powernext were partly transferred to EPEX Spot in a best-of-both-approach, particularly the presence of an exchange council and a market surveillance department.

In Germany, the regulation is threefold:

Firstly, there is a monitoring of all market activities (exchange and OTC trades) and of market abuse: The financial regulatory authority BaFin located at Frankfurt/Main is responsible for the monitoring of all trading activities, regardless whether carried out through an exchange or OTC, and the detection of market abuse pursuant to the German Securities Trading Act.
However, the monitoring practically does not cover commodities markets as the majority of market participants are either exempt by the MiFID exemptions or active solely in energy spot markets. But the provisions on market abuse go beyond the provisions of the Market Abuse Direcitive (MAD, Directive 2003/6/EC) and apply *mutatis mutandis* to commodities which are traded at an exchange.

Secondly, there is the regulation of the exchange: Pursuant to the Exchange Act, the State exchange supervisory authorities (ESAs) are competent for the regulation of the German exchanges situated at seven different sites depending on the exchanges' registered office. The competent ESA, located at the exchange's site or at least State, is responsible for the licensing of the relevant exchange, the regulation of the exchange and its bodies and the monitoring of the exchange trading activities through the market surveillance department.

Thirdly, there is the constant monitoring of the exchange trading activities: The market surveillance departments ("Handelsüberwachungsstelle") of the exchanges are responsible for the monitoring of the exchange trading activities pursuant to the Exchange Act and the exchange rules. This requires a systematic and complete surveillance and analysis of data of the exchange trading and clearing activities and the execution of the necessary investigations in case of a suspected breach of exchange rules or other legal provisions by market participants. The market surveillance department is located in the premises of the relevant exchange and is legally an exchange body.

This is why under the German Exchange Act, EEX was required by law to establish a compulsory Market Surveillance department. The market surveillance department has been set up and operates independently from the exchange management according to the requirements of the exchange supervisory authority, the Saxon State Ministry of Economic Affairs, Labour and Transport (SMWA). The SMWA can assign special investigations to the market surveillance department, but also take over investigations from it.

In order to fulfil its task the market surveillance department is allowed to record and analyse all trading data and to conduct investigation if necessary. Moreover, the market surveillance department can request the disclosure of information form market participants and, if necessary, information about the identities of their customers.

The main tasks of the market surveillance department are to make sure that all trading is conducted according to the rules and that the market results at the exchange are not manipulated. The market surveillance department is not authorised to enact sanctions. Nevertheless, in case the market surveillance department suspects any irregularities regarding the compliance of the exchange rules the Exchange Management and the SMWA have to be informed immediately. It is up to them to decide independently from each other whether the case should be filed to the exchange sanction committee which can impose administrative sanctions up to 250,000 EUR. In case of suspected market manipulation, it has to inform immediately the financial regulatory authority BaFin which would then carry out its own investigations.

4.2 Monitoring by national energy regulators

The actual monitoring activities of national energy regulators vary from one country to another. There is a more general monitoring of the energy exchanges in Austria (CEGH) and Spain and Portugal (OMEL, OMIP). In particular, price formation and market abuse are part of their monitoring activities.

The French energy regulator (CRE) supervises the proper functioning of electricity and natural gas markets. For that purpose, CRE monitors electricity and natural gas transactions between suppliers, traders and producers, transactions carried out on organised markets and cross-border trades. CRE ensures that proposals made by suppliers, traders and producers are compliant with economical and technical constraints. The energy regulators in Romania and France and the power exchange of Romania collect data in order to determine market trends, structure and performance indicators and publishes the relevant market data/indicators. Monitoring activities carried out by the national energy regulator of Italy are mainly aimed at verifying whether market participants unilaterally or collectively exercise significant market power. In this respect, the national energy regulator has standardised specific analyses (e.g. analysis of economic and physical withholding, what-if analysis, concentration indicators), which are implemented with the TSO and GME S.p.A.'s support.

Box 6 : Structure of energy markets monitoring in Italy

Monitoring structure of wholesale electricity and gas markets in Italy varies on the basis of market characteristics. It is consequently necessary to provide some details on Italian electricity and gas markets. At the moment two power exchanges are active, i.e. the Italian Power Exchange (IPEX) and the Italian Derivatives Energy Exchange (IDEX).

IPEX, which enables producers, wholesalers and final customers to enter into *physically-settled* contracts different from bilateral contracts, is managed by the Energy Market Operator (GME) and consists of the Spot Electricity Market (MPE; including the Day-Ahead Market (MGP), the Intra-Day Markets (MIs), the Ancillary Services Market (MSD) and the Forward Electricity Market with delivery and withdrawal obligation (MTE), where operators may sell/purchase future power. IDEX, which is a segment of the Italian Derivatives Markets (IDEM) managed by Borsa Italiana S.p.A., is dedicated to trading of *cash-settled* contracts (base-load futures). Bilateral contracts are over-the-counter contracts, but, in some circumstances, they are relevant for exchange results. In fact, if electricity bilateral contracts are physically-settled, their volumes are taken into account to define the system marginal price of the Day-Ahead Market.

With reference to the Italian wholesale gas market, every contract is bilateral, as no exchange is active in Italy so far. However, the gas exchange (P-Gas), managed by GME, will be operative by the end of 2010.

In the case of IPEX and physically-settled bilateral contracts, monitoring functions are shared among the Ministry of Economic Development, the Italian Energy Authority (AEEG) and the Energy Market Operator. After having heard the opinion of AEEG, the Ministry of Economic Development approves the electricity market rules prepared by GME, which verifies market participants' compliance with electricity market rules. The typical actions that are classified as misbehaviour in the electricity market rules are the following: late payment or redemption of financial guarantees; late payment to GME and failure to pay GME; negligence, imprudence and unskillfulness in the use of the systems of communication and submission

of bids/offers; disclosure to third parties of confidential information related to market participants.

According to the Law n. 481/1995, which instituted AEEG, the Italian Energy Authority promotes competition and efficiency in electricity and gas markets, in the light of EU law and general policies laid down by the Government. Moreover, according to the Ministerial Decree of 19 December 2003, AEEG defines and manages a mechanism to monitor prices and market power abuses in IPEX.

Therefore, monitoring activities carried out by AEEG are mainly aimed at verifying whether market participants unilaterally or collectively exercise significant market power. In this respect, the national energy regulator has standardised specific analyses (e.g. analysis of economic and physical withholding, what-if analysis, concentration indicators), which are implemented with TSO and GME's support.

In particular, in accordance with AEEG's decisions, both the TSO and GME have already instituted a markets surveillance unit and created electronic data warehouses that can be used through business intelligence tools by AEEG as well. The aforementioned data warehouses contain fundamental and trading data regarding IPEX and over-the-counter physically settled contracts, as well as large market participants' over-the-counter cash-settled contracts. These data, which are extremely detailed, are potentially suitable for satisfying a wide range of analytical needs.

In addition, AEEG must be informed by operators active in the Gas Virtual Trading Hub (*Punto di Scambio Virtuale*) on bilateral contracts stipulated in the hub and by the gas TSO on transport capacity utilisation and gas and capacity transactions.

AEEG shares the results of its monitoring activities with the Italian Antitrust Authority (AGCM), which can apply administrative sanctions and impose remedies to market participants. In addition, on the basis of its analyses, AEEG can propose measures to the Government to improve competition in energy markets.

The aforementioned tasks assigned to AEEG in the monitoring field imply that in the Italian law system the definition of misbehaviour also includes anticompetitive conducts in the form of unilateral or collective exercise of significant market power.

In the case of IDEX, monitoring functions are shared between the Italian Financial Services Authority (CONSOB) and the Italian energy authority (AEEG).

In general, CONSOB is responsible for supervising financial markets, but, as far as regulated markets of electricity and gas derivatives (cash-settled contracts) are concerned, the Consolidated Law on Finance provides that CONSOB implements some regulatory and monitoring measures in cooperation with AEEG.

In some cases it is necessary that AEEG agrees with CONSOB (e.g. authorisation to activate regulated markets), whereas in other cases the latter receives a non-binding opinion from the former (e.g. in case of request for suspension of financial instruments and market participants). At any rate, in carrying out its duties, AEEG pursues stability, efficiency and competition of energy markets and security and efficiency of energy networks.

According to the aforementioned Law, in 2008 CONSOB and AEEG established an Agreement, in order to coordinate their actions.

Box 7: French monitoring by CRE

The French energy regulator CRE has been entrusted with the task of monitoring the French wholesale electricity and natural gas markets since 7 December 2006. The law allows CRE to effectively fulfil this monitoring duty by providing for wide-ranging rights of access to information and sanctions in the event access is refused, and for referral to the Competition Council in the event an anti-competitive practice is detected.

The operations affected by market monitoring are those that take place on the French market in which a producer, trader or energy supplier is involved regardless of the nationality of the counterparts. CRE is entitled to monitor the transactions effectively entered into by a producer, trader or supplier, the proposals made by these wholesale market players, and the technical and economic constraints affecting these players and their proposals and transactions.

CRE's remit applies to all transactions carried out on the French market regardless of the mode of negotiation whether they are bilateral transactions with or without an intermediary, or transactions on organised markets.

It applies to transactions for physical delivery and transactions for financial settlement when one of the two parties involved in the transaction (purchase or sale) makes a physical delivery on the French market or a financial settlement in connection with the French wholesale price. Cross-border transactions, a single part of which takes place on the French market, are covered by CRE monitoring.

In order to limit the burden on market participants, CRE designed a process of transaction data collection where the brokers and the exchanges are in charge of transaction transmission. Monthly, they deliver data on spot and derivatives electricity and gas matched transactions. TSO's are also asked to give monthly information on nominative cross-borders flows. In addition the main producers are asked to transmit detailed generation data to the energy regulator.

4.3 The treatment of misbehaviour

The issue how to define misbehaviour and what kind of actions are to be considered as misbehaviour differs substantially across Europe. Some energy exchanges define misbehaviour very broadly. The Romanian energy exchange for example considers any behaviour which does not comply with ANRE (Romanian Energy Regulatory Authority) regulations and related procedures and could have a negative effect on market efficiency or system security as misbehaviour. Furthermore, any action that has negative influence on the competition is seen as misbehaviour.

The Spanish/Portuguese OMEL and OMIP have also a very broad definition of misbehaviour. All practices not under the trading rules are seen as misbehaviour. On the other side, there are several energy exchanges that follow a very narrow definition of misbehaviour.

At the EEX misbehaviour is understood as fictitious orders, misleading trading transactions, insider dealing, and non-compliance with transparency obligations. The rules are defined in the EEX Code of Conduct, which are harmonised with the Code of Conduct of EPEX Spot.

EPEX Spot (electricity, France) has also a clear list of cases which are considered as misbehaviour, stipulated in a Code of Conduct. These are dissemination of false information, deceitful acts intended to mislead the market, deceitful acts intended to reduce market liquidity, and orders with no economic justification.

The Austrian CEGH defines misbehaviour in the context of possible offenders. Misbehaviour is defined as market manipulation by market makers, largest traders, and by suppliers.

At the Italian IPEX, misbehaviour includes: late payment or redemption of financial guarantees; late payment to the market operator; failure to pay the market operator; negligence, imprudence and unskillfulness in the use of the systems of communication and submission of bids/offers; disclosure to third parties of confidential information related to market participants; anticompetitive conduct.

At Nord Pool Spot, market manipulation is defined in the Rulebook, and is understood as transactions or orders to trade which give, or are likely to give, false or misleading signals as to the supply of/demand for or price of a listed product, securing the price at an abnormal or artificial level by acting in collaboration, transactions or orders to trade which employ fictitious devices or any other form of deception or contrivance, and dissemination of information which gives, or is likely to give, false or misleading signals.

Box 8: CESR-ERGEG report on market integrity

Market integrity is an issue of highest relevance for wholesale market participants and end-consumers. As stated in the final report of the Commission's Sector Inquiry[5] "there [in the electricity markets] is a general perception that generation data of vertically integrated incumbents is first shared with affiliates and not necessarily at all with other market participants, which undermines confidence in the wholesale markets". This kind of information asymmetry is linked to a poor level of transparency and may lead to market abuse.

Generators may also be able to influence prices for electricity either by withdrawing capacity (which may force recourse to more expensive sources of supply) or by imposing high prices when they know that their production is indispensable to meet demand. Other abusive practices could be applied by market participants relating in some cases – but not always necessarily – to the existence of a dominant position.

The Committee of European Securities Regulators (CESR) and ERGEG were concerned about the potential for such abuses to take place. Directive 2003/6/EC ("Market Abuse Directive" - MAD) provides a common EU framework for the disclosure of information to the market and aims at the prevention, detection, investigation and sanctioning of insider trading and market manipulation. MAD only partly covers energy markets as it is designed for the financial markets. It applies almost exclusively to financial instruments admitted to trading on a regulated market.

[5] See Communication from the Commission Inquiry pursuant to Article 17 or Regulation (EC) No 1/2003 into the European gas and electricity sectors. COM(2006)851 final and DG Competition report on energy sector inquiry (SEC(2006)1724, 10 January 2007).

Physical products (e.g. spot market products) are not covered and derivatives market products are covered only if they are admitted to trading on a regulated market. Thus, the scope of MAD may not properly address market integrity issues in the electricity and gas markets.

As long as the necessary information is not available to regulators, actual abusive behaviour is difficult to detect. However, as long as regulators do not have the required data to evaluate the possibility for market abuse to take place and to take appropriate action to prevent it, it is likely that the conditions that currently exist could allow market abuse to go undetected and/or unprosecuted will remain unchanged.

There are different penalties that apply in case of misbehaviour of a market party. Several NRAs stated that misbehaviour of market participants can lead to an exclusion from the market. Furthermore, in several countries national authorities are to be informed in case of misbehaviour. Most respondents to the internal survey stated that in case of misbehaviour the financial supervisory authority or the competition authority is to be informed. Furthermore, there are several energy exchanges that can impose fines in case of misbehaviour.

The results of the internal survey showed that there is no common definition on what is to be seen as misbehaviour nor is there a common approach on how to deal with misbehaviour of market participants. These results back up the intention of creating a tailor made market regime on supervision for the energy sector. Such a regime would need to be based on a common definition and understanding of misbehaviour in energy markets and should comprise energy exchanges.

5 Recommendations

5.1 Regulation of energy exchanges and the role of energy regulators

The recommendations assess the potential role of energy regulators in the supervision of energy exchanges. They will particularly focus on aspects related to the regulation of trading short term physical products as these products are essentially important with regard to regulating network access. Furthermore, derivatives at least partly already fall under the scope of MifID and the remit of financial regulators. Regulators however stress the interrelation between physical and financial markets, which have been taken into due account during the elaboration of these recommendations. In most European transmission systems there is only one energy exchange operating where short term physical products are traded. Most European exchanges were developed without being prescribed by national law. However, as liquidity of the existing exchanges increases, the entrance of new exchanges in these markets will be more and more difficult. The reason is that liquidity normally attracts more liquidity. Competition between energy exchanges is thus limited.

Some new developments, such as market coupling, which requires the involvement of spot power exchanges and system operators, may create a monopoly of access to day-ahead cross-border capacity for the exchanges participating in the market coupling. These developments have to be addressed. Besides the potential introduction of a task for Member States to nominate and thus oblige one or more power exchanges to participate in the market coupling, there should be a proper European regulatory framework for power exchanges. The design of such a framework and the cooperation between Transmission System Operators and Power Exchanges will be provided by the Governance Guidelines (currently being elaborated by the Commission with the involvement of stakeholders), which are currently being elaborated. These guidelines shall establish clear roles and responsibilities for the exchanges participating in market coupling. When designing these rules, it has to be acknowledged that the existence of a market coupling backs up the strong market position of power exchanges as in this case day-ahead cross-border trading of electricity is only possible via the exchanges. The importance of exchanges for congestion management would require that exchanges get a clear legal mission for implementing market coupling and would require a stronger role of National Energy Regulators in the regulation of energy exchanges.

In case there is only one energy spot exchange operating for delivery in a European transmission systems, energy exchanges may be either natural or legal monopolies, and should be regulated as such.

In case energy exchanges are active over the national boundaries, there could be disparities in the national regulatory framework. The regulatory framework for these exchanges active under multiple national jurisdictions should be clarified.

Currently, there is no European regulatory framework for energy spot markets. They are not covered by MiFID or by any other European legislation. This is also why there may be no binding and harmonised legislation on market surveillance units and cross-country cooperation on market surveillance. Such a framework is needed as there are several exchanges operating in more than one national market, e.g. Nord Pool Spot and EPEX Spot and as the importance of cross-border exchange of electricity is increasing.

- The regulation of energy spot exchanges could be covered by the energy market integrity regulation or by an ad hoc Commission proposal. As market coupling is provided by exchanges and network operators, the regulation of spot exchanges is a key issue that must be considered when setting out the regulatory framework for non-discriminatory access to electricity grids and market integrity and transparency.

- **Energy regulators should be competent for the overall market design (e.g. market rules) of energy spot markets.** This does not necessarily mean that energy regulators should be responsible for supervising all energy (spot) exchanges, although it is considered beneficial if supervision of the market is in one hand. In case other regulatory authorities are involved, there should be a close cooperation between energy regulators, financial regulators, market surveillance departments of energy exchanges and possibly competition authorities (as envisaged in the proposals for REMIT). Experiences and competences of national energy regulators already supervising energy exchanges and their cooperation models could be an archetype for a future supervisory scheme.

Questions for public consultation
Question 1
In your view, is there a need to create EU level requirements for the organisation, functioning and regulatory oversight of energy exchanges not falling within the scope of MiFID? If yes, what should be the main goals and objectives to be fulfilled?

Question 2
In your view, what are the remits of national energy regulators in supervising energy exchanges and how could a beneficial cooperation between them be organised, in particular for exchanges active under multiple national jurisdictions?

Question 3
Should the regulation of energy spot exchanges in future be covered by the energy market integrity regulation or by a separate future legal proposal by the European Commission?

5.2 The definition of exchange rules (spot market)

The relevant rules and regulations of the exchanges are usually elaborated by an internal body, and usually approved by a governance entity. Exchange members may sometimes also be involved in the definition of those rules. Those rules usually specify the trading rules, clearing/settlement rules and IT requirements. They may contain very different specifications for the trading at the respective energy exchange, such as prerequisite to trade, which differ from one exchange to another.

- Given the differing energy exchange rules, it should be considered if harmonisation of legal and operational frameworks could enhance cooperation between European energy exchanges, and facilitate trading. The involvement of market/exchange participants is important. **To create a level-playing field the exchange rules should be approved by a regulatory authority taking account of the view of the participants in the energy exchange.**

Questions for public consultation
Question 4
How could in your view a harmonisation of legal and operational frameworks stimulate the cooperation of the European energy exchanges and what is the best way to involve the market/exchange participants?

5.3 Market makers

Market makers play an important role in ensuring liquidity at exchanges. Market making is usually done by market participants with a high market share. Thus, the selection process and the rules for market making are very important. This is particularly true in view of potential conflicts of interests possibly arising if a market maker (or its ancillary company) is also a producer.

- If market makers are needed there should be objective, transparent and harmonised criteria for the appointment and accepted behaviour of market makers. There should be a European framework for market makers at energy exchanges in energy legislation.

Questions for public consultation
Question 5
Which criteria should a European framework for market makers include to avoid potential conflicts of interests?

5.4 Transparency

Exchanges publish traded volumes and prices on all products. Furthermore, additional price relevant data such as electricity generation should also be published. This includes e.g. installed capacity, information on planned and unplanned outages, filling rate of water reservoirs and ex-post data on actual generation. Further, ex-ante information on scheduled unavailability of significant consumption units and ex-post information on unplanned unavailability of significant consumption units should be published. This is already foreseen within the ERGEG advice on Guidelines on Fundamental Electricity Data Transparency.

Exchanges provide important information about price signals in the market. Thus it is beneficial if price sensitive information is also published there.

Regarding the publication of additional transparency information (not required by MiFID but essential to achieve transparency in energy markets), regulatory requirements should be set to ensure that the energy exchanges establish satisfactory routines.

Questions for public consultation
Question 6
How could national energy regulators better work towards publishing of price sensitive information as e.g. foreseen in the ERGEG advice on Guidelines on Fundamental Electricity Data Transparency to increase the level of transparency?

5.5 Monitoring of energy trading

The monitoring activities currently performed by the supervisory authorities differ. Some collect data from both exchanges and OTC in order to determine market trends, structure and performance indicators and publish the relevant market data/indicators. A monitoring of the overall market (including the exchange trading) is important for ensuring market integrity in energy trading.

Within Europe most trading activities at the energy exchanges are monitored by a national energy regulator. Some exchanges are also supervised by the government (sometimes together with the national energy regulator) or by the national financial regulator.

The role of market surveillance departments at energy exchanges is considered crucial for a sophisticated monitoring of trading activities. This is why there should be an obligation for energy exchanges to install and maintain a market surveillance department, regardless whether the exchange is a regulated market, a MTF or a currently unregulated market under MiFID (see above point 5.1).

- A monitoring of energy wholesale markets is already covered by the 3rd Energy Package and has to be implemented in national legislation. The experiences and competences of national energy regulators already monitoring energy wholesale are highly relevant for the further development of the monitoring of energy wholesale markets across Europe.

- The Commission´s current proposal for a Regulation of Market Integrity and Transparency (REMIT) includes joint monitoring competences for energy regulators (Agency for the Cooperation of Energy Regulators and NRAs) and financial regulators.

- In order to further improve market monitoring in energy markets, there should be an obligation for energy exchanges to install and maintain a market surveillance department. Such obligation should be valid for all energy exchanges including spot exchanges. Such a market surveillance department should be sufficiently staffed to continuously monitor and analyse the daily exchange trading, the respect of market rules and the respect of other legal provisions. Any such market surveillance department of an energy exchange should cooperate with energy regulators. As the proper functioning of the market surveillance department is important for ensuring market integrity it should be supervised by a national regulator. In view of market coupling, there should also be an obligation for a close cooperation, for exchange of trade data and information between market surveillance departments of different energy exchanges and energy regulators.

Questions for public consultation

Question 7

Which measures could in your view lead to a sufficient cooperation of market surveillance departments of the energy exchanges and the national energy regulators?

5.6 The treatment of misbehaviours

Exchanges play a vital role for the market as they provide important price signals. Thus, exchanges need to be protected from market misbehaviour. Most exchanges have rules concerning the treatment of misbehaviour, however, the definition of misbehaviour and what kind of actions are to be considered as misbehaviour differs very much across Europe. Some energy exchanges define a wide range of different types of misbehaviour as abusive. The results of the internal survey showed that there is no common definition or a common approach on how to deal with misbehaviour of market participants and the definition of misbehaviour.

- Markets become more and more European and market participants are to a large extent active in more than one market and participate at more than one exchange. Thus it becomes increasingly important to foster the creation of a level playing field by harmonised exchange rules, including harmonised approach for the treatment of misbehaviour. The REMIT proposal provides important pillars for such a harmonisation and its final adoption and further definitions will provide guidance.

Questions for public consultation
Question 8
What are in your view minimum standards for a harmonised approach to protect energy exchanges from misbehaviours like market abuse?

Annex 1 – ERGEG

The European Regulators Group for Electricity and Gas (ERGEG) was set up by the European Commission in 2003 as its advisory group on internal energy market issues. Its members are the energy regulatory authorities of Europe. The work of the CEER and ERGEG is structured according to a number of working groups, composed of staff members of the national energy regulatory authorities. These working groups deal with different topics, according to their members' fields of expertise.

This report was prepared by the Wholesale Market Supervision Task Force (WMS TF) of the Financial Services Working Group (FIS WG).

Annex 2 – List of abbreviations

Term	Definition
CESR	Committee of European Securities Regulators
EFET	European Federation of Energy Traders
ERGEG	European Regulators Group for Electricity and Gas
EU	European Union
FIS WG	Financial Services Working Group
FTR	Financial Transmission Right
MAD	Market Abuse Directive
MiFID	Markets in Financial Instruments Directive
MTF	Multilateral Trading Facility (as defined in MiFID)
NRA	National Regulatory Authority
OTC	Over the Counter
RM	Regulated Market (as defined in MiFID)
TSO	Transmission System Operator
UMM	Urgent Market Messages (at Nord Pool)
WMS TF	Wholesale Market Supervision Task Force (of the FIS WG)