



Response by EnBW on the CESR and ERGEG advice to the European Commission in the context of the Third Energy Package

Draft Response to Question F.20 - Market Abuse
Consultation Paper (Ref: CESR/08-509; July 2008)

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General remarks

Generally, we are glad to see that there has been a joint approach by CESR and ERGEG to work on the draft advice to the European Commission on this important issue which deals with the interlink between physical energy markets and financial markets and their potential supervision.

We also fully support that the joint group of regulators have recognised that electricity and gas markets have specific characteristics that need to be taken into account when looking at the issue of market abuse. The pure application of the provisions of a regime that has been designed to predominantly address the traditional financial markets will cause major disturbances in the power and gas markets if transferred without adjustments to these markets.

In their draft advice, CESR and ERGEG propose a tailor-made energy specific regime with respect to disclosure obligations, insider trading and market manipulation. Although we do not fully share the analysis the draft advice is based upon, we would see the general direction of the draft advice as being a good basis for further evaluation. Particularly, we see a close link between market transparency/disclosure and the issues raised in the context of the application of the MAD regime to the power and gas markets.

We fully support improved transparency that is relevant for the market (i.e. price relevant), but at the same time like to stress that it must be ensured that no commercially sensitive data is to be disclosed. In turn, this means that any regime being developed needs to clearly differentiate between information relevant for the market and those data that the competent authority may need for supervision purposes. In this context we like to refer to the already ongoing transparency initiatives that are based on e.g. Transparency Guidelines drafted by ERGEG.

Generally, in terms of disclosure obligations of market-relevant information, we believe that a European-wide harmonised approach is necessary as energy wholesale markets are of European nature.¹ Also, if specific disclosure obligations are implemented (including a properly-defined sanction mechanism), the concerns regarding market abuse (insider dealing and market manipulation) will be significantly reduced if not even fully erased.

If, however, the European Commission comes to the conclusion that the above mentioned disclosure obligations would not be sufficient, we believe that a basic tailor-made specific regime for the power and gas markets can be an approach that could be evaluated. However, we like to emphasise that the development of such a tailor-made regime would then need to be extensively evaluated with a proper drafting and consultation process.

Generally, there are numerous issues that have to be addressed and carefully evaluated in such a process besides the fundamental discussion regarding content and coverage:

¹ Wholesale power price, e.g. between F, DE and Benelux are highly correlated.

- European harmonised approach needed in respect to energy-specific transparency
- Any regime regarding energy-specific disclosure obligations should be based on existing guidelines
- Proper process evaluation and consultation process needed for any energy-specific transparency regime
- Differentiating between market-relevant information and authority-relevant data when designing regime regarding disclosure obligation
- No release of commercially sensitive data into the public domain
- Disclosure obligations implemented in energy regulations will significantly reduce /erase the need for additional market abuse regime
- Additional market abuse regime will raise major concerns regarding:
 - potential problems of conflict of laws (no double regulation of the same business)
 - question of responsibilities (relevant competent authority)
 - costs attached with additional requirements
 - potential barrier of entry

In the following we like to provide detailed comments on the specific questions raised by CESR and ERGEG in their draft response.

1) Do you agree with the analysis of the market failures in the electricity and gas markets as described above? If not, please provide reasons for your disagreement.

The analysis provided is predominately based on the final report of the Commission's Sector Inquiry. However, we like to state, that although the Sector Inquiry describes some potential problems, it has not identified any market failure resulting from a lack of information transparency concerning trading in the wholesale energy markets and the energy derivatives market. Furthermore, as the draft advice by CESR and ERGEG, which would bring fundamental changes for the power and gas industry, is strongly based on the analysis of the Sector Inquiry, we see the necessity to also realise that the Sector Inquiry does have specific shortcomings particularly in respect of the issues also relevant for this consultation. Generally, the analysis often refers to hypothetical aspects (e.g. "abusive practices that could be applied") rather than being based on hard facts. Additionally, significant progress has been made since the launch of the Sector Inquiry in general (e.g. consolidation of market areas in German gas market as well as establishment of numerous gas trade hubs) and particularly in terms of transparency (see response to Q 4). Thus, we are of the opinion that particularly regarding market abuse, one should be very cautious in transferring the often theoretical analysis/results one to one to a potential new regime.

In particular, we like to comment on para 29 where it is stated that balancing the portfolio of a generator is considered to be a harmful process for the market; we strongly disagree with this statement as covering an unplanned loss of generation is a vital procedure making sure that the system stays stable (security of supply) at minimal economic cost. Generally, power plants are commercial positions and having to disclose the shortage before balancing the position will lead to higher cost which would lead to higher prices for end customers. As this issue is an often discussed point we strongly support the statement in para 82 which recognises the specifics of the power market. Again, we are not against a transparent market, but advocate to recognise the complexity of the physical system and its economic relevance.

2) What is your opinion on the analysis provided above on the scope of MAD in relation to the three different areas: disclosure obligations, insider trading and market manipulation?

Generally, the provided technical analysis on the scope of MAD in relation to disclosure obligations, insider trading and market manipulation in the power and gas sector seems to be correct.

3) Do you agree with the conclusion above that greater pre- and post trade transparency would not be sufficient in the context of market abuse?

Generally, we do not see the need for greater pre- or post-trade transparency requirements in power and gas derivatives markets. This has also been confirmed by a recent advice provided by CESR to the European Commission on this matter (CESR/07-284b). We like to stress that the profile of investors in energy wholesale markets is of professional nature; there is no retail participation in energy and energy derivative markets.

Additionally, there are several information platforms that provide post-trade information; energy exchanges publish e.g. traded volumes and bid and ask prices while additional information are published with specialised information providers. We consider this to be sufficient.

4a) Do you agree with the analysis above on the importance of the transparency / disclosure of fundamental data?

Generally, we agree with the analysis and the aspect that disclosure of *specific* fundamental data is important for the market participants to understand price formation. However, we strongly emphasize that this transparency has to be clearly distinguished from information that competent authorities may need for market surveillance purposes. Thus, before any disclosure obligations are established, it is vital to clearly define the specific content. Also, a European-wide harmonised approach should be the aim (e.g. in terms of format, timing, platform); individual and possibly uncoordinated initiatives by national competent authorities are counter-productive.²

Although CESR and ERGEG raised some doubts regarding the voluntary transparency approaches taken by electricity generators, we still believe that this is a productive approach and a good basis for further developments, particularly as these initiatives are based on ERGEG guidelines (and thus on the result of intensive consultations with all relevant stakeholders). Currently, the EEX initiative is being put on an even more structured basis (with close involvement of the Federal Ministry of Economics and Technology (BMWi) and the Federal Network Agency (BNetzA) as well as the market participants), which will improve the data coverage and quality even more. Therefore, if new tailor-made regulations with respect to transparency are discussed, we strongly recommend to build upon the solutions that have been already developed in this process; not at least as significant resources have already been assigned to this project, and still are.

² Current examples include varying approaches by TSOs in respect to Open Seasons as well as an initiative by the French regulator in respect to the reporting of power trading data).

4b) If yes, would you consider it useful to set up at the European level a harmonised list of fundamental data required to be published?

As energy wholesale markets are of European dimension, we support an European approach in respect of transparency / disclosure obligations. In our view, it would be counter-productive to have several national approaches possibly differing in terms of content, quality, format etc. This would not only bear the risk of regulatory arbitrage between Member States, but also of unnecessary higher cost for the obliged stakeholders. Therefore, we support the view expressed in para 63 that it is important that data publication requirements are concrete and uniformly interpreted and applied throughout the Member States.

Again, we like to point to the already ongoing voluntarily organised transparency initiative at EEX, which should serve as a basis for any further specification on this matter.

4c) Is an exhaustive list conceivable or is it necessary to publish additional data on an ad hoc basis if it is considered to be price sensitive?

We like to point out that the transparency issue regarding market relevant data in the electricity and gas markets is not a new topic. Besides the already existing legal requirements, there have been exhaustive consultations by the regulators in relation with the drafting of the “transparency reports” (ERGEG Guidelines of good practice on information management and transparency; GGPSSO; GGPLNG; GGPOS). Additionally, in the framework of the so-called Regional Initiatives there have also been detailed transparency reports published by the relevant energy regulators after thorough consultations of all relevant stakeholders. Therefore, we do not see the necessity to start an entirely new process, but rather advocate to use these reports as a basis. Furthermore, based on the above mentioned reports, several initiatives have been started to implement the reports on a volunteer basis (e.g. EEX initiative; ETSOVista; GIE; EASEE Gas). Therefore, we do not see the need to start an entirely new round of discussion on this, but rather suggest to build upon the measures already in place.

As it is important to have a harmonised European approach, we feel that an exhaustive list as it already exists (e.g. ERGEG Guidelines) is sufficient; this would give all stakeholders a sufficiently reliable basis. Therefore we do not see the need to publish additional data on an ad hoc basis. We are concerned with the generally giving authorities competence to request data on an ad hoc basis in addition to listed fundamental data, as thereby the actual scope will be left to the discretion of the authority, with a lack of legal certainty for the market participants.

5) Which information retained by specific participants of the electricity and gas markets (e.g. generators, TSO) should be published on an ad hoc basis if it is price sensitive?

As mentioned under Q.4, we do not see the need to publish additional information on an ad hoc basis if the list of market information mentioned above is implemented (with clear rules regarding who should disclose which information, where at, what time). We support a common harmonised approach, while additional ad hoc requirements at the discretion of the individual competent authority may lead to regulatory failure.

6) What is your opinion on the proposals of CESR and ERGEG in the three different areas: disclosure obligations, insider trading and market manipulation?

CESR and ERGEG propose to consider developing and evaluating

- to implement disclosure obligations in specific energy legislation, as well as
- a basic, tailor-made market abuse framework (insider trading and market manipulation) in the energy sector legislation for all electricity and gas products not covered by MAD.

Although we do not fully support the market failure analysis in the consultation paper, we can support the approach proposed by CESR and ERGEG from a general point of view. Meanwhile, we also like to stress that the proposal of CESR and ERGEG in the three areas of disclosure obligations, insider trading and market manipulation needs to be carefully evaluated (impact assessment) as the specific details may have significant impact on both the involved companies and the markets in general.³

Transparency/disclosure obligations

CESR and ERGEG propose the evaluation of the implementation of disclosure obligations in energy sector regulations (option 3). As already stated before, we fully support a harmonised approach in terms of disclosure obligations in term of market-relevant data. At the same time, we find it extremely important to recognise the specific characteristics of the power and gas markets when it comes to obligations to disclose particular data to the market. Therefore, we strongly advocate that no commercially sensitive data is to be disclosed into the public domain;⁴ neither directly by the energy company nor indirectly via the competent authority. This is why it is significant to differentiate between information relevant for the market and those that may serve supervision purposes. The latter should be designed as an event-based approach, rather than an obligatory permanent transaction reporting process, which we strongly object to.

3 Also, we consider the aspects of potential costs related to any new regime to be an important point to be considered.

4 E.g. this would include specific data at gas connection points where only a small number of participants are active; otherwise the strategic behaviour of the market participants could be derived from the disclosed data.

It is important that the specifics of the power and gas markets need to be recognised while taking the content and experiences of already available reports and ongoing initiatives into account. In this context we like to point out that the mentioned NordPool regime is one approach particularly designed for the Nordic market with its specific characteristic that the main volume of traded power being hydro-generated. We therefore advocate to implement an open process following the observation made in para 82, rather than simply transferring NordPool provisions as a blueprint for the entire European market.

In general, as correctly stated in para 60, energy companies are already subject to sector specific transparency requirements including provisions in the 3rd package; and the Regulations 1228/2003 and 1775/2005. One approach could be to use these regulations as the basic framework to make the obligations legally binding. Alternatively, one could evaluate whether it would be sensible to consolidate all provisions regarding transparency in one single regime/legislation, if such a specific regime is to be established following the draft advice of CESR and ERGEG.

In any case, aspects such as the responsibility and place of disclosure need to be clear (including timing, format, platform) as well as a properly defined sanction mechanism (this cannot be on individual regulator's discretion).

Insider Trading

CESR and ERGEG propose to consider developing and evaluation proposal for a basic, tailor-made insider trading framework for products not covered by MAD in a specific sector legislation (option 3).

We are of the opinion, that with the implementation of a sector-specific disclosure obligation on certain fundamental data (as mentioned above), the acclaimed information asymmetry will be levelled. Therefore the concerns regarding insider trading will be erased, particularly if a sanction mechanism is built into the disclosure obligation. Therefore we doubt whether an additional insider regime is actually needed.

If, however, the European Commission is to decide that a basic tailor-made framework for insider trading for specific electricity and gas products is to be developed within the energy sector legislation, it is vital that any proposal is properly evaluated including a proper impact assessment analysis (with a proper cost-benefit analysis), as well as consultation procedures (i.e. respecting the Better Regulations Principles). Simply "copying" existing market rules (such as NordPool) will in our view not properly account for the specifics of the entire European markets. We also understand that a one-to-one transfer of insider provision from MAD to the new energy sector legislation is not an option, neither should it be an extension of current financial rules (para 106 gives the hint that this maybe considered). Naturally, all related specific characteristics of the potential sector legislation for specific electricity and gas products need also to follow a sector-specific approach. Additionally, one could then also assess the general scope of power and gas transactions currently covered by MAD and examine to what extent there is a need for those to be treated in the same manner as other power and gas products (and thus exclude them from the scope of the MAD).

In the case of designing a specific regime we ask for a properly defined legislation process in which a clear and well-defined scope of the potential application of such a regime is designed. It is to be ensured that there is no overlapping double regulation of the same business and that there are clear responsibilities, i.e. supervision by

which competent authority, to avoid conflicts of competence. In such a case it should also be investigated whether energy derivatives that currently fall under the MAD regime should also only fall under this new energy sector legislation and thus be excluded from the scope of the MAD.

Market Manipulation

CESR and ERGEG propose to consider developing and evaluating a proposal for a basic, tailor-made market manipulation framework for physical markets in a specific energy sector legislation. However, with the introduction of a sector-specific disclosure obligation on certain fundamental data, the acclaimed information asymmetry will be levelled. Therefore the concerns regarding market manipulation will be erased, particularly if a sanction mechanism is built into the disclosure obligation. Therefore, we doubt whether an additional insider regime is needed. Additionally, we would like to stress that abuse of market power - though not in an energy-specific manner - is already dealt with by competition legislation.