Commodity access – enhancing wholesale market liquidity?

Rozeta Karova, Ph.D.
Senior Energy lawyer, Energy Community Secretariat
Background

Market integration - central aim of the Energy Community

Liberalization & reforms at national level taking into account the regional and pan-European integration objective

  “based on harmonized set of rules with regional market mechanisms that would operate as supplementary mechanisms of the national electricity markets, with suppliers and generators who could operate on a larger on an equal basis in a wider regional energy market instead of a narrow national market and where electricity will flow among the countries of the region as it was flowing within a single country”

- combining bilateral physical contracts & spot market

- **2008 – first retail market opening for large customers, for which wholesale competition & capacity allocation was precondition**

**2018 status quo**

- national markets (still) dominated by incumbent undertakings with exclusive access to energy resources

- bilateral contracts main instruments

- not all CPs participating to a joint capacity allocation

- vertical foreclosure through regulated agreements

- generation price regulation still persisting

- number of traders - not negligible

- **BUT organized DAM - Serbia PX, others (AL, MNE..)**

- several regional integration projects - market coupling
ECS Policy Guidelines 2015; need for new guidance on concrete measures

- 2015 PG on *Promotion of Organised Electricity Markets in the Contracting Parties*
  - removal of the legal and factual barriers to electricity market integration and liberalization
  - the need for establishing electricity markets that would allow market coupling

**Coupling of the DAM of small, illiquid & incumbent-dominated markets of the CPs => single best means to bring liquidity into the SEE region and allow for competitive price formation.**

- 2018 ECS to recommend practical steps necessary for creation of coupled (regional) electricity market:
  - which preconditions would have to be fulfilled at national level in order for the Contracting Parties to comply with the European electricity target model by recommending different market designs for organizing national electricity markets taking into account the need for their harmonization (WB6 national projects)
  - **legal and regulatory measures for introducing competition at national level + measures for introducing liquidity in power exchanges**
Ex-ante regulatory measures that may be imposed on certain operators in order to promote effective competition at wholesale level, in markets characterized by high and non-transitory barriers to entry as well as directly enhancing PX liquidity

Barriers to be addressed:
- structural
- legal or regulatory
- combination of both.

NRA (and other authorities) competences
Measures of intervention

Based on EU Member States‘ experience...

1. designed to limit the influence of operators with significant market power eliminating the barriers to entry / cost advantages, or to reinforce small players;

2. aiming to eliminate cross-subsidies, margin squeezes or concerted actions between vertically integrated undertakings;

3. directly enhance liquidity on organized markets;

4. aimed at preventing abuse of market power on the PX or by the PX
Measures 1

- Measures that are designed to limit the influence of operators with significant market power or to reinforce small players [Could allow customers to benefit from advantages of the historic investments, while at the same time allowing liberalization by transferring cost advantage to suppliers/new entrants]
  
  ✓ regulated access to historic nuclear in France (ARENH);
  Price & volume of regulated products are set administratively: incumbent EDF was obliged to sell up to 100 TWh of its nuclear production (approx. 25% of its production) to its competitors, upon demand, on annual basis.

  ✓ Virtual Power Plants auctions;
  Regulated volume-based mechanism, which only set the volumes of the regulated product and allocate the products to those who value them most. Requirement / commitment imposed on generators (usually dominant) to sell proportion of their output of a power plant through a specified auction process, mostly to competitors. [FR: 5400MW in 2001; BE – 1200MW in 2004]

  ✓ access to lignite or big hydro designed by the Greek regulator; [combination of ARENH and VPPs]

  ✓ direct-trading obligations.
  Large generators imposed an obligation to trade on equivalent or comparable fair terms with eligible suppliers (usually small suppliers meeting pre-determined transparently set criteria) [Market Supplier Access in UK; ref price – telecom]
Measures 2

- Measures that aim to eliminate cross-subsidies, margin squeezes or concerted actions between vertically integrated undertakings

... in addition to the measures 1 most of which are also suitable for VIU ...

- self-restriction obligations;
  - Imposing obligation to purchase a certain portion of their wholesale needs through the market, preventing being fully supplied by their own integrated undertaking / group – may be set as a % of total sales on a monthly basis.
- non-discrimination obligations;
- requirements for accounting separation.
Measures 3

- Measures that directly enhance liquidity on organized markets:
  - obligation to offer for sale or
  - obligation to trade certain volumes of electricity on organized markets,
  - market-maker obligation

✓ symmetrically or asymmetrically;
✓ on seller’s side, on buyers’ side or on both seller’s side and buyer’s side;
✓ could be imposed for ex. on: **RES producers** as a pre-condition to benefit from support; generators’ that are to benefit from compensation funds **for stranded costs**; as a precondition for **access to cross-border capacity** – if allocated via implicit auctions; **TSO/DSO** for losses…

✓ obligations imposed for overall volumes traded on a PX without pre-determining specified volumes for specific segments/market or targeting one specific platform which is less liquid than other market segments;
Measures 3 contd.

✓ By setting for instance:
  - max offer price at DA auctions covering variable costs of the producers;
  - volumes to be offered - equal to certain pre-determined % of overall volumes generated or traded or supplied (over 1-year period).

✓ Proportionality principle – measures to be limited in time, for a period long enough for the PX to establish itself and become a recognized and liquid market;

✓ Should allow for a flexible review clause, and should designate competent authorities that may adopt modifications or revoke the mandatory sales or auctions;

✓ Significant impact on the development of wholesale market and PX liquidity in countries where those were introduced.

  PL: PX trade - 2009 = insignificant; 2010 = 4.2%, 2011 = 58.7%; 2012 = 61.8%;
  OTC bilateral contracts – 2010 = 89.8%; 2011 = 40% and OTC in-group electricity trade - 2010 = 72,2% of overall sales, 2011 = 18,9%
Measures 4

- Measures aimed at preventing abuse of market power on the PX because of:
  - manipulating price-formation by way of modifying volumes;
  - false or excessive bid pricing;
  - collusion of market participants on the PX...

- Measures
  - max numbers of coupled offers (price/quantity) that a certain undertaking may submit, or an obligation to trade on the PX with a max offer price could be imposed
  - Transparency and integrity (price setting principle / pre-trade or post-trade transparency requirements)
  - Supervision of PXs (by the PX market operator and by the NRA).

- Measures preventing abuse of market power by the PX itself indirectly affecting access and liquidity at the PX [EU case law: OPCOM, Dutch PX, EPEX Spot-Nord Pool …]
Monitoring and enforcement powers of NRAs (and NCAs)

Electricity Directive recitals:

39. The internal market in electricity suffers from a lack of liquidity and transparency hindering the efficient allocation of resources, risk hedging and new entry. [...] Trust in the market, its liquidity and the number of market participants needs to increase, and, therefore, regulatory oversight of undertakings active in the supply of electricity needs to be increased.

37. NRAs should have the power to issue binding decisions in relation to electricity undertakings and to impose effective, proportionate and dissuasive penalties on electricity undertakings which fail to comply with their obligations .... NRAs should also be granted the power to decide,...., on appropriate measures ensuring customer benefits through the promotion of effective competition necessary for the proper functioning of the internal market in electricity. The establishment of virtual power plants - electricity release programmes whereby electricity undertakings are obliged to sell or to make available a certain volume of electricity or to grant access to part of their generation capacity to interested suppliers for a certain period of time - is one of the possible measures that can be used to promote effective competition and ensure the proper functioning of the market.

Article 37(4)

...(b) to carry out investigations into the functioning of the electricity markets, and to decide upon and impose any necessary and proportionate measures to promote effective competition and ensure the proper functioning of the market. Where appropriate, the regulatory authority shall also have the power to cooperate with the national competition authority and the financial market regulators or the Energy Community Secretariat in conducting an investigation relating to competition law.
Thank you for your attention.