

23 July 2010
European Commission
DG Energy - ENER.DDG1.B.2
'Market Integrity'
Rue De Mot 24-26
B-1049 Bruxelles
Belgium

Dear Sir/Madam,

Public consultation by the Directorate General for Energy on measures to ensure transparency and integrity of wholesale markets in electricity and gas

Liquid traded wholesale energy markets are very important to ensure that liberalised gas and electricity markets provide efficiently determined market prices i.e. prices which reflect supply and demand fundamentals. This is how consumers ultimately benefit from liberalisation. Liquid wholesale markets also provide efficient investment signals to market participants as well as efficient signals for market entry and exit. As a result liquid wholesale energy markets reduce unduly prohibitive barriers to entry which ultimately results in lower prices for consumers. As such we agree with the European Commission that liquid wholesale markets are a necessary requirement in today's energy markets.

In the GB energy market there has been a material lack of trading in the wholesale forward electricity market; the forward market can be characterised as being illiquid. We believe this is due to the market structure in that the six largest electricity companies are vertically integrated owning both generation and supply businesses. This view is shared by many market participants and commentators including HM Treasury and the Department for Energy and Climate Change¹. Their ability to trade electricity internally between the two businesses has reduced the amount of physical electricity available to trade on the wholesale market. As a result there is some doubt as to whether wholesale forward electricity prices reflect supply and demand fundamentals. The barriers to entry and organic growth in both electricity generation and supply which the illiquid forward market is perpetuating has led to a lack of competitive pressure on the six incumbent energy companies. There are also concerns about the adequacy of these wholesale prices in encouraging investment in conventional generation plant.²

Furthermore, concerns about the state of the GB gas wholesale market were articulated by the Business and Enterprise Select Committee in 2008³. As such the effective monitoring and

¹ Energy Market Assessment, HM Treasury (March 2010).

² Further details on our view of the current state of the GB wholesale electricity market can be found in our response to the latest Ofgem consultation on liquidity in the GB wholesale electricity market. Please see <http://www.consumerfocus.org.uk/assets/1/files/2009/06/Consumer-Focus-response-to-Liquidity-proposals-for-the-GB-wholesale-electricity-market.pdf>.

³ House of Commons Business and Enterprise Committee, Energy prices, fuel poverty and Ofgem

oversight of wholesale energy markets is crucial to ensure consumer confidence in the final price they pay.

We are particularly interested in the data the Commission intends to collect and how this can improve the transparency of wholesale energy markets. We have not commented on its proposed use for the monitoring and enforcement of market integrity. There are two reasons for this. The first reason is that in discussions we have had with market participants the issues concerned with market integrity (insider trading, market manipulation etc.) has not been considered a major problem. The major issue has been related to a lack of physical trading especially in the forward electricity market. Secondly, we do not have the market expertise and experience to comment authoritatively on issues of market integrity, including issues related to the Market Abuse Directive for example.

The information we believe that the Commission wishes to collect would be helpful for NRAs (including Ofgem) in determining whether wholesale energy markets are sufficiently liquid or not and also help determine the cause for any potentially illiquid market. We are particularly interested in the possible data collection requirements contained in Article 40 of the Electricity 3rd EU energy liberalisation package directive. This states that "Member States shall require supply undertakings to keep at the disposal of the national authorities... for at least five years, the relevant data relating to all transactions in electricity supply contracts and electricity derivatives with wholesale customers and transmission system operators". Furthermore, "The data shall include details on the characteristics of the relevant transactions such as duration, delivery and settlement rules, the quantity, the dates and times of execution and the transaction prices and means of identifying the wholesale customer concerned". We hope this will go some way to identifying the degree to which vertically integrated electricity companies trade between their generation and supply businesses internally and on what terms these contractual arrangements are settled. In fact we have already highlighted to Ofgem the potential to make use of Article 40 of the 3rd EU energy liberalisation package in our response to its latest wholesale electricity market consultation. If the Commission was to collect and publish the data required to ensure market integrity it should also assist NRAs in their monitoring of their national wholesale energy markets. We note that the Commission's ability to adopt binding guidelines with regards to Art. 40 and Art. 44 in electricity and gas markets respectively could ensure that these record keeping obligations are adhered to in a uniform fashion.

Aside from the direct benefits to the NRAs of increased access to data that they can use to diagnose and tackle problems with the functioning of their own wholesale markets there is a wider cross EU benefit in allowing effective cross border comparison between the efficiency of markets in different Member States. Relatively few of the challenges that Member States face are genuinely novel and unique to their territory and there may be material benefits in improving cross border understanding of what has worked, or failed to work, in different territories. Credible, informative public reporting would be crucial to delivering this and in ensuring that the NRAs can be held accountable by their stakeholders. Given the materiality of energy markets, even minor

(16 July 2008).

incremental improvements in a subset of Member States might generate significant consumer benefits across the EU.

I hope these comments are helpful. If you would like to discuss our response in more detail, please contact my colleague Cem Suleyman on 0207 799 7932 or via email at cem.suleyman@consumerfocus.org.uk .

Yours faithfully,

[Sent electronically]

Richard Hall
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