

<p style="text-align: center;"><b>E.ON's response to</b> <b>Public Consultation by the Directorate General for Energy on measures to</b> <b>ensure transparency and integrity of wholesale markets in electricity and gas</b></p>
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**23 July 2010**

**Introduction**

E.ON is in favor of a tailored regime for energy markets and supports transparency measures to improve oversight of energy markets.

E.ON strongly believes that an effective and consistent framework for market integrity would improve trust in energy markets and allow development, e.g. increase of liquidity and European market integration. Markets that are more integrated would benefit consumers due to competitive advantages. Greater confidence in price formation is also important for future investments and greater appetite to enter the market. E.ON believes that such a tailored regime would create a sound basis for enabling market results to reflect fundamentals and for delivering secure energy at fair prices. However, E.ON believes that price caps, position limits and other administrative measures for controlling energy prices, are detrimental to competitiveness and do not provide a level playing field. It must be emphasized that financial markets differ greatly from energy commodity markets and have not shown any failure to date.

A tailor-made regime for ensuring market integrity in the energy sectors should be defined comprehensively, promoting market integration and compliance and define:

- *what* shall be considered “misconduct” by definition on *insider dealing* and *market manipulation*;
- *what* data and information is to be associated with such a regime, both *fundamental* and *transactional*
- *who* is best placed to perform the *monitoring* and the *enforcement* role and at which level will this take place (national vs. EU-level)
- *how* the *monitoring role* will be carried out

Furthermore, E.ON believes the regulation of fundamental data disclosure to be one of the cornerstones in the approach to a tailored regime, in order to ensure market integrity for the energy sectors. All *measures* should be non-discriminatory and cost effective, not consisting of laborious mechanisms or duplicating reporting requirements.

<p><i>1. Are there particular developments in relation to oversight of energy markets at a national, European or global level that we have not properly considered?</i></p>
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**E.ON is of the opinion that the paper considers major legislative developments, which are relevant to the oversight of energy markets. There could, however, be more emphasis on specific energy sector requirements including physical commodity trading, specific hedging measures and market misconduct.**

E.ON understands that the **Third Energy Package** introduces measures to make data available to different supervisory bodies. Aside from these measures, benefits could be seen in defining a clearer framework to detect market abuse and market misconduct. In addition to the third energy package provisions, trading at European level is subject to numerous jurisdictions with oversight by several bodies in different countries and with different legal requirements (on, for example, reporting, licensing

and oversight of market developments). There is clearly a need for a specific framework to tackle gaps and promote compliance, creating an EU-wide level playing field.

E.ON is supportive of a regulation regarding energy trading integrity ideally for physical spot and forward products and financial derivatives. If such a comprehensive framework cannot be achieved, a proper coordination between energy and financial regulators must be sought to exclude overlaps.

As advised in the consultation paper, **MiFID** and **MAD** are specifically designed to deal with financial markets and instruments. Underlying physical commodities widely influence market outcomes, thus requiring a tailored approach. E.ON agrees that the general MiFID objective of ensuring “financial stability and investor protection” is not deemed suitable for energy markets, where the objective of ensuring “public trust and integrity of markets” must be key driver of the regime.

The Commission’s initiative of adopting legislative proposals that require eligible **derivatives to be cleared through CCPs** for non financial undertakings with positions above a certain threshold is considered a disproportionate measure to ensure safety in energy markets. It would increase market player costs for hedging assets against commodity price volatility and have a negative impact on electricity and gas markets, hindering the development of integrated and efficient European markets by reducing liquidity and the number of competitors, with the inevitable effect of increasing prices. E.ON considers specific rules for a tailor-made regime for the market integrity of gas, electricity and carbon markets an appropriate measure to ensuring the security of energy markets.

The draft Auctioning Regulation within the **Emission Trading Directive** should include provisions on insider dealing and market manipulation in the primary carbon market. E.ON believes that the secondary market should also be subject to oversight by including the development of Emission Allowances in the same work stream for energy markets. Although some aspects differentiate carbon markets, interdependencies within the electricity market in the price formation processes are strong, supporting a proposal for including carbon under the same regime.

E.ON wishes to make specific reference is to **national transaction reporting requirements**, which are on the increase throughout European countries and for which prompt intervention proposing a replacement of national requirements by EU level standard is urged. These are typically only in the national language, with variations in contents and format, making automated processes impossible. More importantly, these reporting and licensing requirements are rapidly becoming a major barrier influencing market players about not entering or exiting some national markets.

<p><i>2. Do you agree that the current Regulatory Framework should be updated to include clear rules governing energy market oversight? Please justify your reply.</i></p>
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**E.ON is in favor of a suitable framework governing energy market oversight.**

E.ON believes that the actual regulatory framework suffers due to certain gaps relating to physical forward and spot markets and more general over-the-counter

transactions in physical markets. It is therefore suggested to update this to determine clear rules governing oversight, which should provide a comprehensive framework that determines the precise definition of misconduct, the extent of data and information to be disclosed and/or analyzed, what is the most suitable supervisory body for monitoring and how this monitoring role is to be performed. Any extension to Third Package measures on reporting requirements should be subject to an impact assessment to ensure cost-efficient measures.

E.ON fundamentally agrees with CESR and ERGEG analysis that the Commission should evaluate and develop a basic tailor-made market abuse framework in the energy sector. An effective and consistent framework on market integrity would encourage confidence in energy markets and would promote development, i.e. increase liquidity and European market integration. Greater confidence in price formation is also imperative for securing future investment and be a motivating factor for potential participants to enter the market.

*3. Do you agree that this update should ensure integrated/coordinated oversight between financial and commodity markets and across borders.*

**A coordinated and integrated oversight approach is essential.**

E.ON believes that coordination in oversight across borders and between commodity and financial markets is necessary. This coordination should result in a clear regulatory framework on roles and activities subject to oversight. Obligations and responsibilities must be clearly defined in any legislation. Coordination should preclude overlaps that may, for example, result in duplicating efforts with the collection of data in different formats on request or notifying/reporting information on the activity performed in certain sectors or geographical areas.

With regard to commodities being part of a tailor-made regime for oversight, E.ON believes that it is necessary to include gas, electricity and carbon markets. All of these are emerging markets at EU level and, although the carbon market is integrated at EU level by definition, whereas electricity and gas are on heading for full integration, the interaction between these markets justifies the inclusion of all of these within one oversight regime. Minor differences between them should be addressed within the regime.

*4. Do you agree that the overlap of physical, and financial (derivative) markets, and the cross border nature of the market currently leads to sub-optimal oversight of energy markets?*

**E.ON agrees that in the current framework, oversight over physical markets leads to a sub-optimal outcome.**

There are both gaps and overlaps in market supervision with the current framework. Nevertheless, E.ON believes that a sub-optimal outcome is mostly due to a lack of coordination and is aware of an insufficient definition of market manipulation and insider dealing with regards to the energy sector. The current, almost national approach results in an inefficient use of both resources performing oversight for supervisory bodies and efforts from market participants in order to fulfill numerous data/information requests.

5. Do you agree that definitions of market misconduct for gas and electricity markets should be consistent across EU? If not, why not?

**E.ON is in agreement with this statement.**

The definition of market misconduct should not only be *consistent*, but *identical* across the EU, as this would facilitate market integration and create a level playing field at EU-level. This would also provide stability to regulatory frameworks across the EU, which currently still suffers due to an obvious lack of compliance. When determining the sector-specific approach to energy markets, it is necessary to deal with this independently of financial regulation.

6. Do you agree that market misconduct should follow the MAD definitions? If not, why not?

**E.ON is in disagreement with this statement.**

Energy commodity markets are very different to financial markets. The specifics of wholesale energy and carbon markets must therefore *be* taken into account. Underlying physical systems and rules on how such markets interact with one another are part of the energy regulatory framework and impact market outcomes. E.ON therefore recommends consideration of energy and carbon market characteristics. Merely extending MAD scope and definitions would not reflect the complexity and interactions in the developing energy markets.

E.ON is of the opinion that the definition of inside information for commodities within the Directive 2004/72/EC suffers due to generalization and fails to consider the characteristics of energy markets. Therefore, both the Insider Dealing and market manipulation definitions require tailoring, with a requirement to precisely define what each constitutes, based on the definition of fundamental data that is to be made available to market participants.

Of particular importance is the definition of the *fundamental* data and events, including relevant *thresholds*, which are subject to mandatory *timely* disclosure to the market. This type of information must be considered insider information and no trade action is permitted for the affected market player, i.e. outage of a power plant above 100MW, before disclosure of the relevant information to the market. The timing of publication is to be determined by individual market function.

*7. Do you agree that specific account of the specificities of the physical energy markets should be taken of energy markets through guidance rather than in legislation? If not, why not?*

**E.ON only agrees in part with this statement.**

Consistency across Europe is achieved by means of an aligned application of rules on physical energy markets. Thus, where possible, specifics of energy markets should be set out in the regulatory framework according to explicit principles contained in legislation and with guidelines to ensure adequate application. It is essential that the overseeing body has the necessary skills with regards to the energy markets in order to be able to perform as required. E.ON does not agree, however, that guidance should be linked to the MiFID and MAD Directives.

*8. Do you agree that regular market monitoring is an essential function to detect market misconduct?*

**E.ON agrees with this statement.**

E.ON is of the opinion that market monitoring is one of the core functions for detecting abuse. As a first step, a framework should be set up and market data made available to such supervisory bodies. The analysis of this data should then be applied to the rules governing each market, which must be aligned at EU level. Duplication of existing rules, i.e. the record-keeping obligation, is to be avoided.

When considering suspected misconduct, the market participant should be given opportunity to justify deviations between expectations and real outcomes in order to avoid any misjudgements.

*9. If yes, given the characteristics of wholesale energy markets, do you agree that market monitoring is best organised on EU level?*

**E.ON agrees that market monitoring is best organized on EU-level.**

E.ON believes that there is a need to develop market monitoring on an EU-scale. Therefore E.ON supports a market monitoring activity performed at EU level. This approach would reduce the data burden (i.e. aligned data and format requirements), which would improve the reliability of the oversight framework, reducing information deviation which is usual when entering national markets, thus ensuring an aligned approach. As a consequence, this would encourage market integration and alignment, liquidity and efficiency.

Setting a clear responsibility for market monitoring regime at EU level would also ensure an aligned approach for the definition of market misconduct across Europe, also supporting enforcement.

A *national cooperation* approach would result in a stalemate, causing an increase in overlapping and multiple requirements throughout Europe.

*10. If yes, do you believe that ACER should be given the role of an EU level monitoring body for wholesale energy markets?*

**E.ON is not convinced that ACER is the most suitable body on EU level to perform this task.**

E.ON believes that the role of the EU monitoring body must go to an organization with the required competencies. As ACER is only just being established, its main focus should be regulated infrastructure business with cross-border character. E.ON believes however that a supervisory body on EU-level is essential in order to deal with specificities and interactions between markets and borders. With this more transparent framework, market participants would play a role in the day-to-day monitoring of the market, which means that concerns and complaints could be directed at a special supervisory body on EU level.

*11. Do you agree that the EU level monitoring body for energy markets should have a coordinating role to ensure effective application of EU level rules for energy markets? If not, why not?*

**The EU-level monitoring body should have a coordinating role.**

The EU-level monitoring body should also be responsible for ensuring that, where competent national authorities are entitled to oversee energy sectors, these authorities have been granted access to relevant data in order to be able to perform this role in accordance with national legislation. Cooperation is essential whilst overlaps on information requests should be instead avoided.

*12. In your view, would enforcement of market misconduct rules be best organised on national level or EU level?*

*a. If on national level, would national energy regulators or national financial regulators be better placed to enforce compliance?*

*b. If on European level, which institution would be best placed to enforce compliance?*

**E.ON believes that responsibility for enforcement depends on the violation type.**

Enforcement should be decided by type of suspected misconduct at monitoring stage. The increased integration of gas and electricity wholesale markets and the monitoring role performed at EU level would, more often than, not lead to enforcement at equal level, i.e. EU-level.

National energy regulators may be involved in an advisory capacity. Finally, if an investigation confirms infringement of competition laws, national and European competition bodies must be entitled to perform as intended.

*13. Do you agree that the market monitoring body for energy markets should also be able to monitor EUA transaction?*

**E.ON agrees with this statement.**

EUA markets are directly related to European energy markets and these markets closely interact with one another.

This particularly applies to carbon markets, which have the same EU-wide scope as energy markets go. Energy and carbon products are usually traded by the same market participants and there are linkages in the price formation and interaction between these markets. Numerous trading venues are available both for energy and carbon.

*14. Would monitoring of traded carbon markets be best organised on national or on EU level?*

**Market monitoring for traded carbon markets would be best organized on EU-level, as carbon markets are EU-wide by definition.**

Carbon markets have been created through the “cap and trade” principle in the Emission Trading Scheme Directive. Even if carbon markets are still developing, they are indeed EU-wide by definition, which means that there is no alternative but to consider this when developing the monitoring functions.

*15. If on EU level, do you believe that ACER could be an appropriate monitoring body?*

**E.ON is not convinced that ACER is the most suitable body on EU level to perform this task.**

As ACER is only just being established, its primary focus should be cross-border issues related to regulated infrastructures. E.ON is not convinced that ACER is the best-place to monitor energy and carbon markets at EU-level and ensure coordination with other competent bodies. Nevertheless, it is clear that a supervisory body at EU-level is essential in order to deal with specificities and interactions between markets and borders. This body should not be *an additional* organization with a supervisory role, as this is already split between different bodies without any clear definition. A clear definition of roles and responsibilities is, however, imperative in order to provide clarity on the regulatory framework to market players.

*16. Do you agree that it is not appropriate, at least at present, to consider coal, oil and other commodities along with wholesale gas and electricity markets? If not, why not?*

**E.ON agrees with this statement.**

Coal and oil influence the price formation process of energy markets. Nevertheless, E.ON understands that these are more global markets and the definition of a suitable oversight regime would go beyond EU-boundaries and affect the timeframe in which results are achieved. They are also not based on networks, which would require even

more specific treatment. We therefore agree that, for the time being, they should not be part of a tailored regime.

E.ON would, however, like to emphasize the importance of working towards this, albeit at a different priority level and with an adjusted timescale.

*17. Do you agree that it is appropriate to apply exemptions and de minimis levels? If not, why not?*

**E.ON agrees with this statement.**

E.ON believes that such a tailored regime should not cause significant burden or result in competitive disadvantage to smaller traders. These exemptions should be limited to reporting requirements and other activities that may be considered barriers to market entry and permit discrimination (e.g. capacity threshold above which outages have to be publicized to be applied to all market players). Misconduct should not be judged on *quantitative* levels, but on *severity*.

*18. Do you agree that market data relating energy market transactions should be reported centrally? If not, why not?*

**E.ON agrees that energy market transactions on standard products should be reported centrally.**

Regulated Markets, Regulated Multilateral Trading Platforms (MTFs) and OTC-Markets (broker platforms) are best-placed to ensure *timely* reporting on deals on standard products in a standardized format to a central body. As mentioned in the consultation paper, transactions for *standard* products concluded on a purely bilateral basis could be combined with a regular reporting obligation (i.e. monthly/quarterly/annually). The solution must, however, be proportionate and cost-effective.

*19. Do you agree the body with an oversight role requires full access to fundamental data relating to carbon?*

**E.ON agrees with this statement.**

E.ON believes that a better overview on physical underlying emissions should be enforced for carbon. The introduction of a periodical (monthly or quarterly) release of individual emission data for larger installations would appear most suitable.

With regards to the fundamental data for electricity and gas markets, E.ON believes that the proposal should be strengthened in order to achieve a consistent approach. The third energy package contains rules to permit the introduction of legally-binding guidelines in relation to data on physical production, transmission and consumption. ERGEG has been appointed to develop guidelines on this issue for the electricity sector.

Fundamental data will impact the price formation process for electricity, gas and carbon markets, such as information on generation flows, grid and production facilities availability, transmission, storage, consumption and CO<sub>2</sub> emissions. E.ON



believes that such guidelines must be considered part of the market integrity regime for the energy sector.

One of the expected outcomes of a tailored regime is a closer connection between market results and fundamentals. One of the outcomes from this regime should be the definition of the fundamental data to be released to the public and what is considered to be *insider information* before public release.

Transparency of fundamental data, which is a framework of disclosure of this type of information to the public, should be a cornerstone of the tailored regime. This requires explicit and comprehensive definition *relevant fundamental data*, like *who* has the duty of publication, the *manner* in which it is published (i.e. aggregate vs. individual basis) and the *timing* (i.e. close-to-real-time vs. other deadlines) of the publication to ensure consistency with relevant timeframes for commercial and operational decisions. This will provide market participants with relevant information about when to buy, when to sell and at what price and volume, thus emphasizing the need for transparency of fundamental data, both to create a level playing field for market participants and to ensure that market mechanisms operate in the most efficient manner.