

**European Commission (DG ENER) Public Consultation on measures to ensure  
transparency and integrity of wholesale markets in electricity and gas  
31 May 2010**

**EDISON COMMENTS**

**GENERAL REMARKS**

Edison firmly believes in the intrinsic value of the proper functioning of the internal electricity and natural gas market and its **progressive development towards more liquid and transparent** features upon implementation of the current relevant European and national legislation and regulation.

For the time being electricity and gas wholesale markets, including companies' trading behaviour, are already subject to national (Competition Authorities, Energy Regulators) and European (DG COMP) oversight. The **new provisions and obligation as set out by the Third Energy Package** will further increase the degree of transparency requirement on market transactions thus adding confidence in market participants on price formation and **much needed undistorted price signals for investments**.

Edison is deeply aware of the relevance attached to price signals (be it for oil, electricity, gas and CO<sub>2</sub>) for future investment decisions in the energy sector and to successfully meet the challenges of Climate Change in a market based and cost-efficient way. For this reason we consider of the utmost importance the definition of specific measures aimed at reducing the risk of artificial distortion of these signals induced by market manipulation and misconduct, and for this to happen we favour the definition level of a robust and harmonised monitoring and reporting system within an EU regulatory oversight framework.

So far in our opinion ERGEG, CESR and the European Commission have correctly addressed in their consultation papers the **growing relevance gained by trading in commodity derivatives for risk management and hedging strategies in today's energy wholesale markets**, but as the current European legislative framework addressing market abuse and insider dealing (MAD Directive) doesn't cover specific contracts and products currently traded on energy markets, we do share the view that there is indeed a regulatory gap to be filled here.

**EDISON KEY MESSAGES**

1. Effective transparency and integrity requirements should avoid undue bureaucratic burden, which may lead to access barriers and therefore hinder competition and market participation, to the detriment of liquidity and sound market functioning.

2. A 'one-stop-shop' solution at European level is the most desirable outcome for data collection; otherwise a sufficient degree of coordination between competent authorities must be ensured to avoid a burdensome framework for market operators, in particular for those operating in several member States.

3. The specific features of energy markets shall be taken into the utmost account when defining a legislative framework for enhancing market integrity and transparency. The difference between non financial firms trading commodity-based derivatives and financial institutions on the other hand has to be duly taken into account when defining a tailored-made regime to reduce the risk of market abuse in energy trading, in particular:

- On wholesale commodity trading markets non-financial firms trade commodities to manage their own business risks;
- Commodity trading firms are less relevant than financial institutions from a capital structure point of view, and they consequently have a lower systemic importance and
- Commodity derivatives are normally underwritten by strong underlying physical markets, with prices driven by physical supply and demand;

4. The relation between commodity markets (electricity and natural gas) and oil / equity markets run to a larger extent by financial institutions needs to be carefully assessed and monitored against the systemic risk as regards commodity markets;

5. In order to define a consistent and harmonised framework across Europe a standardization of definitions is needed for terms such as "standardised contracts", "forward", "future" or "financial

derivative”.

**6. The overall framework for commodity based derivatives, including future revision of the legislation, need to be consistent with these premises in order to guarantee a sound reference framework and prevent uncertainties for market participants and impacts on market functioning.**

## **EDISON ANSWER TO THE PUBLIC CONSULTATION**

**Q.1 Are there particular developments in relation to oversight of energy markets national, European or global level that we have not properly considered?**

Lack of transparency and concentration as regards financial speculation by large investors has been envisaged as one of the leading causes of oil price volatility and disconnection from market fundamentals experienced in the last two years. As a consequence (and given the current natural gas price indexation to say the least) a higher oversight should be enforced as regards this market in particular.

Besides this market design and physical constraints associated to energy infrastructures (e.g. lack of interconnection and its implication on market liquidity) and the nature itself of the commodities in case should be duly taken into account when observing and assessing the dynamics on wholesale energy markets as regards liquidity and price formation. Furthermore the geographical dimension of the market is relevant to this end, and the difference between the state of regional integration between wholesale electricity and gas markets should also be considered.

At global level the need to safeguard European operators and companies' commercial interests – as higher transparency requirements, record keeping and reporting obligations may lead to competitive disadvantage should also be taken into account.

**Q.2 Do you agree that the current Regulatory Framework should be updated to include clear rules governing energy market oversight? Please justify your reply.**

As the Third Package and its relevant provisions for market transparency are not in force as yet, there will be the need to assess the effectiveness of these measures against the need for additional transparency requirements. A full and even implementation of the current legislation is thus a first important step towards a better monitoring of wholesale markets. Any further extension of the current provisions as set in the Third Package should be subject to an impact assessment.

As regards the need to fill the gap with the current scope of the Market Abuse Directive the measures have to be proportionate and sector-specific.

This process will need to evaluate as well the impact of a possible further legislation covering OTC trades not transacted through regulated markets and standard OTC (forward) transaction and in conjunction with the upcoming legislation on OTC introducing mandatory Central Clearing obligations for all standardized derivative products and trade repositories with notification of all operations in OTC derivatives, in order to guarantee the highest level of consistency with the energy sector-specific approach.

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

A legislative update should evolve towards a higher coordination between national competent authorities as regards cross-border or trans national issues. This coordination has to be guaranteed without causing overlaps in competencies or double burdens for operators. At national level there must be a robust and harmonized system established at EU level to avoid regulatory arbitrage. A tailor-made comprehensive energy regime is to be preferred, for this reason the complete integration with the approach towards the financial markets should be avoided.

**Q.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?**

The specific characteristics of non standardized products (provided that a harmonized definition at EU level is set out) should be duly taken into account when setting the rules for trading repositories. The relation between physical, financial markets is still sound in commodity markets and commodity based-derivative markets, for this reason they should be treated in a tailor-made approach when improving oversight.

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

Edison is in favor of a common European understanding of the concept of “energy market misconduct” in order to avoid regulatory arbitrage. The concept should be distinct from (neither an exception of nor a sub-definition of) financial market misconduct. Again there should be a sector specific approach. Sector and commodity-specific aspects (different physical constraints for electricity and natural gas, e.g. storage) should be duly taken into account.

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

The energy commodity markets are quite different from financial markets and definitions should not be required to follow the MAD/MiFID approaches.

**Q.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?**

The particular nature of energy commodities and the specificity of physical energy market should be taken in the utmost account when defining the legislative frame work to address market abuse and market misconduct. Market design, market constraints may lead to sub-optimal outcomes when it comes to price formation that may not necessarily be ascribed to operators’ behaviours in the first place. Especially for these reasons a specific legislative regime for energy markets is needed.

Guidance on the interpretation of that legislation may provide an added value to a sector specific legislation but no guidance should be issued for the simple purpose of integrating or defining further extensions of the MiFID or MAD Directive to the energy sector.

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

The highest degree of transparency has to be guaranteed in monitoring activities to detect market misconduct. For this purpose the requirements on record-keeping set by the Third Package are very extensive, and will allow competent national authorities to access the relevant data, thus facilitating the identification of market misconduct.

Still, reporting obligations on companies’ individual transactions would result in burdensome administrative procedures without increasing significantly the objectives of avoiding market misconduct, as the Italian system is already proving in the electricity sector. A single trade repository in absence of a standardization of OTC contracts on the other hand seems to be difficult to pursue.

The definition of market monitoring as well should be intended as the general market oversight exercised by a regulatory body, based on defined transparency requirements and access powers, and not the comprehensive reporting of all transactions.

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

The growing integration of electricity and gas markets and the presence of an EU wide carbon market make the rationale for a market monitoring at EU level. Data collection should also be centralized either at national (through better cooperation between competent authorities) or European level.

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

The nomination of ACER as competent oversight authority at European level would require an extension of competences and funds of the Agency.

**Q.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?**

Any EU monitoring body should facilitate the cooperation between competent authorities whenever there is the possibility of uneven application of the same harmonized rules established at European level. ACER already has a clear role in this sense as regards the areas of responsibility for fostering an effective implementation of market rules on cross-border issues. Therefore the question (also keeping in mind Q.10) for us is whether ACER should take on an additional monitoring or co-ordinating role, not - as could be implied by the question - that a still-to-be-identified body should duplicate what ACER could do in the first place.

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

The primary need is for appropriate enforcement actions to be taken at national level, on the basis of a sound and common understanding of what constitutes market misconduct in the energy market according to a clear set of harmonized rules at European level. Current procedures at European level to guarantee the enforcement of European legislation would add more certainty to the regulatory oversight.

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

However it is organized, the key requirement is that the responsible body should have the necessary expertise to manage the energy specific regime, and that national responsibilities are set in a clear and transparent way in order to avoid overlaps or duplications (e.g. between antitrust/financial/energy regulators). Italy has already implemented in 2008 a protocol of coordination between the energy regulator (AEEG) and Consob (Commissione Nazionale per le Società e la Borsa) to better guarantee a market oversight on electricity and gas derivative markets.

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

The European Commission is to date the competent institution at EU level to guarantee proper enforcement of EU legislation and compliance from member States. Infringement procedures are the best way to ensure compliance at EU level.

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

The current proposal of regulation for the EUA market until 2020 already identifies a specific monitoring body for carbon markets reporting to the European Commission and cooperating with the body operating the central auction platform and Member states. Maximum accountability should be guaranteed on this body and maximum transparency should be guaranteed on the operation of CO2 market in order to deliver sound price signals to market operators and sufficient liquidity first and foremost to enable ETS operators to comply with EU obligations. Transparent and non discriminatory access conditions to auction platforms will have to be guaranteed and speculative behaviors (even through the introduction of maximum bid sizes) should be foreseen. CO2 monitoring and other commodity markets monitoring should be duly coordinated.

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

Monitoring of traded carbon markets is already addressed in the proposal of Regulation for auctioning in phase III of the EU ETS scheme. Given the current possibility for Member states to set up national auctioning platform in a transitional manner it is of the utmost importance to guarantee that carbon markets and carbon price are monitored at European level for CO2 prices to actually reflect the supply and demand balance without speculation or arbitrage between national markets.

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

See Q.13

**Q.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?**

In Edison view, it is necessary to strengthen transparency and integrity across commodity markets other than electricity and gas. For instance, a lack of transparency and monitoring by the relevant authorities is envisaged in oil contracts as well as in the carbon markets. We therefore believe that the scope of the new legislative framework should be as wide as possible, in any case including at least electricity, gas and CO<sub>2</sub>. In particular, this latter commodity can count on a good degree of standardization at a contractual and market level, thus easily fitting into a new tailor made legislative framework on market integrity and transparency.

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

Exemptions and *de minimis* levels must be set out without causing distortions or asymmetries on the market thus leading to sub-optimal outcomes. Size-based exemptions can in fact generate this kind of problem. Any exemption should be also defined with the purpose of reflecting the energy market specificities. As a matter of consistency all actors should be in principle covered in a non-discriminatory approach. We understand the logic of having exemptions/*de minimis* rules, but this in turn raises the question of the threshold and the way they are set. In considering thresholds, it is of the utmost importance to focus on the entity and the nature of the market risks entailed rather than on the size as regards energy companies.

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

Record keeping obligations codified by the Third Energy Package can ensure an adequate and harmonised monitoring at European level. Further transactions reporting requirements would lead to an undue increase of administrative and bureaucratic costs charged on market operators, especially when imposed by different national regulatory authorities. However, we wish to highlight the need to ensure consistency between record keeping requirements on spot wholesale markets and future markets through a unique set of guidelines applicable in all Member States.

**The introduction of a European trade repository collecting all transactional data, if additional to the obligation already in place, risks to be excessively burdensome to market participants**, besides being of no use for market transparency. We strongly believe that the publication of data regarding single transactions, notably non-standardized products, is of no value to wider markets, while implying the disclosure of commercially sensitive information.

Thus, **as far as the current proposal is concerned, regulators should rely on the already existing sources of data, included exchanges and other MTF, and on the current legal framework on report keeping**. Furthermore, records disclosure from market participants to the relevant authorities should occur case by case on Regulator's specific request, in order for market oversight to be consistent with streamlined and efficient market procedures.

**The highest degree of confidentiality should be granted for commercially sensitive information.**

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

Edison shares the EU Commission proposal to rely on the Third Package for the codification of disclosure obligations for fundamental data (guidelines approved by comitology). Nevertheless, the definition of a common and harmonised list of the information for any commodity subject to publication at European level should fulfil the following criteria:

- Harmonised timing and pattern for publication
- A single platform for the acquisition of information
- Standard quality levels.

We support the list of fundamental data prepared by ERGEG. Still, we think that a unique format for delivery and use of the same categories of data (transactional data included) would be useful in order limit expenses born by market participants to comply with market monitoring obligations.

## **EDISON - WHO WE ARE**

Born in 1881, Edison, one of the oldest energy companies in Europe. When the national monopoly on electricity was established in Italy in 1963, Edison had to diversify its business, but thanks to the first wave of EU Directives in 1996, it could re-focus its business on energy once again. Today Edison is the leading new entrant in the Italian energy market, with 50,2 billions kWh produced in 2008 and a market share of 16,4% of national output. Thanks to 7.000 MW of new highly efficient and low emission plants (CCGT thermo plants, as well as hydro and wind power plants), the Company has now a total installed capacity of more than 12.000 MW. In 2008, Edison reported revenues of 11.066 mln €.

Thanks to one of the most ambitious investment plans in Europe, Edison aims at becoming the second largest electricity company in Greece through the recently established joint venture with Hellenic Petroleum. As shown by the recently approved Business Plan (2009 – 2014), Edison will invest 7.2 billion euro in natural gas (exploration and production activities, in major gas import infrastructures, such as the Rovigo LNG offshore re-gasification terminal and the ITGI-Poseidon and GALSI pipelines) and in power generation sector, with a particular focus on renewable energy sources (hydro and wind power, allow the Group to cover over 40% of the green certificate requirement with its own production). Other investments will constitute strategic developments in fast-growing markets, such as Greece, Romania and Turkey. As from 2009 the new offshore LNG terminal in Rovigo will contribute to the diversification of the country's supply sources with its re-gasification capacity of 8 bcm of natural gas a year, equal to 10% of Italy's demand for natural gas. In 2012 there will be the start up of Galsi and ITGI pipelines, which will connect Italy and European markets to Algeria and Caspian Sea, two areas rich in hydrocarbons.

More info on <http://www.edison.it/edison/site/en/index.html>