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2. April 2008
MW / BW

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Committee of European Securities Regulators
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Sir
John Mogg
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CESR/ERGEG Call for Evidence on record keeping, transparency, supply contracts and derivatives for electricity and gas (Ref: 08 - 140)

Dear Mr. Wymeersch,
Dear Sir Mogg,

BDEW welcomes the opportunity to contribute to the Call for Evidence on record keeping, transparency, supply contracts and derivatives for electricity and gas issued by CESR and ERGEG following the Call for Technical Advice the EU Commission has issued related to Articles 22f and 24f and Recitals 20 and 22 respectively in the two proposals for Directives amending Directive 2003/54/EC and Directive 2003/55/EC (The Third Energy Package).

Following our contributions to several consultations regarding transparency issues we are happy to submit our detailed response to the questions contained in Annex I of the Call for Evidence (**encl.**).

Generally, BDEW fully supports adequate and harmonised rules for market transparency in the energy market as they promote liquid and competitive energy wholesale markets. However, it is important to differentiate between requirement regarding transparency from those for record-keeping purposes. The fundamental difference between which information should be released to the market for the understanding of price formation (market transparency) and what information shall be kept for the need of the competent authority for the understanding of market behaviour.

Concerning the specific issue of record-keeping raised in the Call for Evidence, BDEW advocates, that if record-keeping arrangements are being introduced, they should be installed in a proportionate manner which minimise the administrative burden placed on market participants. In any case, it is of utmost importance that the confidentiality of sensitive data is provided at all time.

For any further questions, please do not hesitate to contact Dr. Bernhard Walter (Bernhard.Walter@bdew.de; phone ++49 / 30 72 61 47 – 470) or myself.

Sincerely yours,

Dr. Michael Wunnerlich

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Position Paper

Response of the German Association of Energy and Water Industries (BDEW) on CESR / ERGEG Call for Evidence on Record Keeping, Transparency, Supply Contracts and Derivatives for Electricity and Gas (Ref.: 08 - 140)

STN 04.004.08
30 March 2008

www.bdew.de

BDEW Response

CESR/ERGEG Call For Evidence on Record Keeping, Transparency, Supply Contracts and Derivatives for Electricity and Gas (Ref.: 08-140)

General Remarks:

We fully support clear and harmonised rules for market transparency throughout the European Union. In our view, the main purpose of transparency requirements is to identify the relevant price determinants which should be publicly available, thereby ensuring a level playing field for all market participants.

We also like to raise the issue that it is very important to differentiate between transparency requirements and the issue of record-keeping for market surveillance purposes.

With regard to permanent transparency obligations, we would also like to raise the concern that it is important to limit these obligations solely to those that are relevant for the market players in order to ensure a level playing field in the market. They must not serve market surveillance purposes.

Data needed and kept for surveillance purposes should as a basis of principle be kept confidential as it is the relevant authorities' task to supervise the market and not the task of the market itself.

A. Introduction

As the mandate for advice to ERGEG and CESR seems to be based on the assumption that wholesale energy markets are currently not well-functioning, we would like to make some specific remarks concerning alleged “market failure” in energy wholesale markets. In this context the Introduction under Annex I refers to the Sector Inquiry launched by the European Commission.

Although, the Sector Inquiry has outlined specific problems relating to vertical foreclosure, market concentration, lack of market integration or price level, these are not related to the lack of transparency on supply contracts and derivatives for electricity and gas.

Therefore, we would like to state that there is no basis for the mistrust against the proper functioning of energy wholesale markets that has been raised also in relation to the mandate. Thus, it would be inappropriate to base the need for further regulation of the energy wholesale markets on an alleged market failure as this is likely to distort the market rather than “cure” the alleged failure.

C. Fact-Finding

1. *How many of the following also fall under the definition of investment firms under Article 4(1)(1) of Directive 2004/39/EC (MiFID):*
   (a) *undertaking active in 'supply' of electricity within the meaning of Directive 2003/54/EC (Art 2.19)?*
   (b) *undertaking active in the 'supply' of natural gas with the meaning of the Directive 2003/55/EC (Art. 2.7 and 2.8)?*

In general, almost all undertakings referred to in question 1a) and 1b) may fall under the definition of investment firms under Article 4(1)(1) of MiFID. However, most of them, currently fall under the exemptions of Article 2 of MiFID. Hence, only the respective competent authorities do have the full overview of the actual number of investment firms, which have obtained a licence according to the MiFID requirements (and the respective national requirements), including those undertakings active in supply of electricity and natural gas. However, due to differing national implementation of the MiFID provisions, the absolute number of investment firms under article 4(1)(1) of MiFID may not be a relevant indicator at all (with the current review of MiFID, this may change again in the future).

2. *What are the existing record-keeping obligations with respect to transactions in electricity and gas derivatives to which investment firms are subject by reason of MiFID? Consider both the transaction reporting obligation of firms under Article 25 of MiFID as well as the record-keeping obligations under Article 13(6) of MiFID.*

The main addressees of these questions are the relevant competent authorities. Generally, in the case where energy trading companies are investment firms according to the MIFID requirements (and national requirements, respectively) they also have to comply with the respective provisions regarding record-keeping of the MiFID.

3. *What (regulatory) authority oversees activities in energy markets in EU Member States?*

The regulatory supervision varies from Member State to Member State. In Germany there are several authorities overlooking the energy market:

- *Regulatory Authorities: Federal Network Agency (BNetzA) and Regulatory Authorities of the States (Landesregulierungsbehörden)*

In the field of energy as defined by the German Energy Industry Act (Energiewirtschaftsgesetz, EnWG) they secure

- as far as possible, a secure, cost-efficient, consumer-friendly, efficient and environmentally compatible grid-bound provision of electricity and gas to the general public;
- working and undistorted competition in the provision of electricity and gas and ensures the efficient operation of energy supply networks on a long-term basis;
- the implementation and enforcement of Community law in the field of grid-bound energy supply.

- *Financial Regulatory Authority (BaFin)*

A main function is the banking supervision. If undertakings active in energy derivatives trading fall under the provisions of the German Banking Act and no exemption applies they need to obtain a respective license and are being supervised by BaFin.

- *Federal Cartel Office (Bundeskartellamt)*

In Germany the task of protecting competition is undertaken by the Bundeskartellamt and the competition authorities of the respective states (Bundesländer). Cartel Offices are not in charge where a specific regulation is provided in the EnWG, which is being executed by the *BNetzA* and the *Landesregulierungsbehörden* (see above).

- *The Saxonian Ministry of Economy and Labour (supervisory authority of the European Energy Exchange)*

The European Energy Exchange is located in the State of Saxony. Hence, according to the German Exchange Act, the Saxonian exchange supervisory authority is - amongst other tasks - in charge of supervision of

the exchange markets and the participants. Its tasks include supervision of the companies licensed to trade on the exchange in co-operation with the market surveillance department of the exchange as well as the investigation of potential violations of provisions and orders under the exchange law.

This indicates that it is essential to harmonise the activities of regulators in this area within Member States and on a pan-European scale. In particular, any overlap of regulation, for instance between financial regulation and energy regulation, should be avoided. Market oversight in cartel matters should be clearly separated from network regulation.

D. Record-Keeping

4. *Do regulators believe that there should be a difference between the proposed record-keeping obligations under the proposed amendments to the electricity Directive and gas Directive and the existing record-keeping obligations with respect to transactions in electricity and gas derivatives to which investment firms are subject by reason of MiFID (Articles 25 and 13(6))?*

Generally, there are clear differences regarding the potential addressee between the obligations by reason of MiFID and the proposed amendments to the electricity Directive and gas Directive. While the existing record-keeping obligations with respect to transactions in electricity and gas derivatives under MiFID only apply to investment firms and are limited to financial instruments, the proposed amendments to the electricity Directive and gas Directive are aimed to address all supply undertakings with a wide range of data relating to all transactions in electricity/gas supply contracts and electricity/gas derivatives with wholesale customers and TSOs.

However, although the aims of the respective Directives vary considerably, there should be a harmonised approach regarding record-keeping. Particularly, only one set of data should be required to be kept, that can be used for different purposes, as befitting the different directives' aims.

We believe that proportionate record-keeping arrangements should be designed and operated in a harmonised European fashion as a way to minimise the administrative burden placed on market players. In addition,

they should be practical, consistent with commonly-used IT processes and should not incur disproportionate costs. They should also not duplicate the large amount of data already available from exchanges, brokers and other information providers. Likewise, it is also of vital importance that any relevant authority asking for those data has in place adequate arrangements to protect confidentiality of data from individual market players.

5. *Pending the outcome of the legislative process in respect of the proposed Directives amending Directives 2003/54/EC and 2003/55/EC (the Third Energy Package), what methods and arrangements for record-keeping do CESR and ERGEG consider the Commission should specify as guidelines under this legislation for:*

   (a) transactions in electricity and gas supply (spot) contracts? (To the fullest extent possible this should be a harmonised specification.) If there are any deviations from obligations relating to commodity derivatives already applicable to investment firms, these should be justified;

   (b) transactions in electricity and gas derivatives contracts? (To the fullest extend possible this should be a harmonised specification.) If there are any deviations from the recommendations in a), these should be justified.

   In answering this question, CESR and energy regulators are asked to consider specifying a single transactions record format based on the content and data to be provided as per Table 1 of Annex 1 of Regulation EC 1287/2006.

If any future regulatory guidelines or arrangements are considered, they should clearly distinguish between market transparency aspects and monitoring aspects. Potential record-keeping arrangements must be cost-effective and should not lead to a publication of competition-sensitive information (see also answer to question 4).

Furthermore, it should be clarified which specific types of transactions mentioned in the question should primarily be investigated by the competent authorities. As many contracts are already traded at exchanges, competent authorities can have easy access to the relevant information

directly from the exchanges, thus sparing the need to keep records on the level of the individual company.

6. *How would this information be most efficiently kept at the disposal of authorities as mentioned under paragraph 1 of Article 22f/24f in the case of spot transactions and non-investment firms?*

Generally, we believe that there should be a common agreement on data content, standardised formats and electronic storage of the data on a European level. For reasons of cost-efficiency, the actual method of data keeping based on these standards should be left to each individual company.

7. *How would securities regulators most efficiently provide information to energy regulators pursuant to paragraph 7 of Article 22f/24f?*

A general provision of data exchange between securities and energy regulators to become an end in itself should be avoided; i.e. only such data should be exchanged that is essential for the work of the competent authority in individual cases. Most importantly, provision of information should only take place when safeguards concerning the confidentiality and security of (individual) data are in place. Any provision of information should avoid duplication of efforts, especially for the involved companies.

8. *Which securities regulator would most efficiently be responsible for such provision in the case of investment firms with more than one branch?*

Following the MiFID provisions, the securities regulator responsible for the Member State in which the investment firms' main branch is located should be responsible for the provision of the relevant data to the energy regulator. In this context, it should also be clarified which energy regulator can ask for the recorded data (in respect of investment firms with more than one branch).

9. *Would this be feasible and efficient to employ the Transaction Reporting Exchange (TREM) or a similar electronic system to exchange this data?*

Our understanding is that this provision concerns record-keeping and an exchange of data only on a case by case basis (i.e. no permanent exchange of data). Therefore, the deployment of the Transaction Reporting Exchange Mechanism or a similar electronic system is not necessary. We think that the relevant authorities should agree upon a standardised format for the data to be stored, so companies need only once to implement the respective IT-structures for record-keeping.

10. *Is there a case for data to be forwarded from energy regulators to securities regulators on an automatic basis? If so, what data?*

Firstly, it should be clarified, if there are any data, which need to be forwarded from energy regulators to securities regulators. We do not think this is the case in Germany. In our opinion, the logical flow of data would be from securities regulators to energy regulators,

If there are any data which need to be exchanged, the respective information should not be forwarded on an automatic basis. It is our understanding that data should only be provided to the respective regulator on a case by case basis. Also an automatic transfer of data may compromise confidential business strategies of market participants and the publication of these data may distort the energy trading market. Therefore, regulators should refrain from any automatic transfer of commercially sensitive data.

In addition, the provision (and holding) of data should be proportionate to the potential needs for market monitoring by the regulators. For instance, the obligation to keep details concerning bidding policies in different markets for different generation units is not an adequate measure.

E. Transparency

11. What guidelines and arrangements do energy regulators propose for the making available of aggregate market data by them under paragraph 3 of Article 22f/24f?

Generally, we like to state that the proposed Articles 22f/24f is aimed to establish obligations for 'record-keeping' and data that can be requested on an ad-hoc basis by regulators. They do not (and should not) introduce obligations regarding the type of data or information issued to the market. However, it is important to clearly differentiate between the two aspects. Hence, any potential guidelines and arrangements should clearly distinguish between transparency purposes and monitoring purposes. The information needed for market transparency purposes (understanding of price formation) and information to suit regulators needs (monitoring of the market) are substantially different. While improved market transparency generally increases trust, the publication of commercially-sensitive information would bear the risk of market distortion. Hence, the type of data released to the market should be aggregated data relating to the use of infrastructure (i.e. data on the transmission network and interconnectors) or the status of generating units as these information are important to understand price formation (for details we like to refer to the EURELECTRIC report as well as the ERGEG Guidelines for Good Practice on Information Management and Transparency in Electricity Markets).

In addition, as noted in the proposed Article 22f (4), there is also a strong need for uniform application of guidelines and arrangements throughout the Member States, be they for record keeping or transparency purposes. If the regulators see the necessity to release information to the market, this should not be arbitrary but follow prescribed and EU-wide harmonised rules.

12. What requirements, deriving from national law, are currently put on energy traders, brokers or exchanges to publish information 'post-trade', for example on publishing traded volumes, prices etc.?

This question can only be answered on a country by country basis. In Germany, publication of post trade information (such as volumes and prices) are compulsory for exchanges but not for brokers or energy traders.

Voluntary publication of OTC-data is discussed in the context of the ERGEG regional initiatives and the respective regulators´ reports on transparency in regional markets. Additionally, several energy companies voluntarily publish generation data such as actual production or unplanned outages for the purpose of market transparency.

In this context, we would also like to state, that - due to standardised trading agreements - energy trading companies are liable for data confidentiality (e.g. §20.1 and 20.2c; EFET contract electricity).

13. What requirements, deriving from national law, are currently put on energy traders, brokers or exchanges to publish information 'pre-trade', for example on publishing bids to organised markets?

The publication of pre-trade information varies from country to country.

14. Is there a difference in transparency requirements for spot trading compared to future and forward trading? If so, why?

In Germany, there is no difference in transparency requirements for spot trading compared to future and forward trading.

Again, we like to stress that the Commission's Sector Inquiry has not provided any argument for additional transparency requirements for spot trading or forward/futures trading in energy. Generally, transparency on exchanges is ensured by the exchange itself, where market players can see e.g. the traded volumes, bid/ask curves, number of players and clearing prices. Regarding OTC-trading the broker screens in use in modern trading rooms allow for market players to see e.g. the bid and ask prices and the traded volumes. Additionally, a range of further detailed ex-post information is provided by brokers and information providers. In this context we also like to point to the ERGEG Guidelines for Good Practice on Information Management and Transparency in Electricity Markets (Ref: E05-EMK-06-10) which clearly concludes that information needed to be released to the public should be aggregated information provided through respective exchanges and brokers platforms.

15. Is there a difference in transparency requirements for exchange trading compared to OCT trading? If so, why?

See answer to question 14. The German Exchange Act (Börsengesetz) contains transparency requirements for trades concluded at exchanges. There are no transparency requirements for trades being concluded OTC.

16. What information, other than required by law and regulation, is made public by energy traders, brokers, information services or exchanges?

Besides information required by law and regulations, market related information can be obtained through various additional channels. There are several independent information service providers (e.g. Platts, Bloomberg, Reuters) that offer a range of market data and information. Such information include for example market related news, analyses, weather data, exchange / benchmark prices, or data on generation. Additionally, exchanges also offer information e.g. on prices and volumes (including open interest).

Beyond the regulations for exchanges and the services of information providers several market participants in the energy sector voluntarily publish market relevant data; this is particularly data concerning the status and actual use of generation units. To mention is here the voluntary initiative to publish generation-related data via the website of the EEX. Other energy exchanges also publish a range of market relevant data. Additionally, grid-related data can be found at ETSOvista website.

17. Is access to information on traded volumes and prices equal for all parties active in that market?

See answer to question 16.

18. If not, is unequal access to or general lack of information on trading causing distortion of competition?

n/a

19. In light of the findings in the Commissions Sector Inquiry on energy and the subsequent study of the electricity wholesale markets, please consider:

(a) whether, pending the outcome of the legislative process in respect of the proposed Directives amending Directives 2003/54/EC and 203/55/EC, greater EU-wide pre- and/or post-trade transparency rules for electricity and gas supply contracts (physical and spot trading) and electricity and gas derivatives would contribute to a more efficient wholesale price formation process and efficient and secure energy markets;

Although the recent Commission's Sector Inquiry describes a number of problems affecting wholesale markets (such as vertical integration, lack of integration of national markets), it does not indicate any problem regarding commodity and commodity derivatives trading. Particularly, it does not propose additional measures concerning transparency or supervision of energy commodity markets in the context of the Sector Inquiry.

In February 2006 the European Association of Power Companies, EURELECTRIC, issued a list of transparency requirements which are considered to be needed by market participants to better understand price formation in energy trading (i.e. data on grid status and interconnectors, generation data and data on prices / volumes at energy exchanges). Inter alia, this position paper calls for harmonised publication rules on a regional and, ultimately, pan-European level, thereby creating a level playing field for all market participants. Therefore, any data published should:

- be made available under similar conditions to all market participants. In particular, they should be authoritative, issued at the same time and be easily accessible;
- as far as possible use standardised definitions and formats to facilitate processing and analysis by market participants and allow harmonisation across national borders;

- enable market participants to operate with a sufficient degree of confidence.

(b) whether such transparency arrangements could be expected to effectively mitigate the concerns identified in the Sector Inquiry above;

Although the Sector Inquiry does identify some problems it does not demonstrate evidence of a market failure regarding transparency in wholesale supply contracts and derivatives contracts in electricity and gas. Thus, it would be inappropriate to base the need for further regulation of the energy wholesale markets on alleged market failure. Again, regarding data that is important for the market, we like to refer to both the aforementioned EURELECTRIC paper and the ERGEG guidelines.

(c) whether uniform EU-wide pre- and post-trade transparency could have other benefits;

Efficient energy wholesale markets are a fundamental part of the EU-wide energy market. As electricity and gas are network-bound commodities, transparency about the use of the physical infrastructure is elementary. EU-wide harmonised transparency rules, especially concerning transmission and generation data therefore:

- promote market liquidity and enhance market efficiency;
- facilitate new entry;
- engender market confidence; and
- facilitate regulatory oversight.

However, with regard to the promotion of liquidity, a balance must be sought between the burden of having to provide information and the potential benefit that this information has for the market. The requirement to provide too much information could be perceived as being counter-productive (see answer to 19d).

(d) whether additional transparency in trading could have negative effects on these markets, for example could liquidity in these markets be expected to decrease? Is there a risk that trading could shift to third countries to escape regulation?

Generally, we do see the danger that additional transparency in trading could have negative effects particularly on liquidity. If requirements are too high, potential market participants may see this a barrier to entry. Particularly, smaller and medium-sized companies may not have the necessary resources to comply with additional transparency requirements and hence will leave the market or not enter the market as a new entrant.

Also, if too detailed information is needed to be disclosed, market participants may appear as behaving in a collusive and anti-competitive manner, even if the opposite is true. Therefore, the implementation of market transparency rules should also involve the relevant competition authorities as part of the dialogue with all relevant stakeholders.

In this context one should also be aware, that the higher the demands from regulation, whether financial regulation or transparency requirements as discussed here, the more likely trading activities will be moved outside the jurisdiction of the European Union. As this is only a feasible option for larger players, smaller players may be disadvantaged.

(e) If you believe that there are risks arising from additional pre- and post-trade transparency requirements, how do you believe that these risks can be mitigated (e.g. aggregation, delay in publication, anonymity)?

In determining transparency requirements, specific attention should be paid to carry out an informed and balanced assessment as to the level of market transparency needed. It is therefore essential that the degree of detail is determined by the range of data relevant to price formation. The costs of collecting data have to be proportional to the benefits this information will bring to market transparency and market functioning. Market participants in energy market, as in every other market too, must be able to operate in wholesale electricity markets without revealing commercially sensitive information concerning their purchasing, sales, production, or other trading or contracting strategies.

Thus, due regard needs to be paid to ensuring that the arrangements proposed for market transparency do not undermine or distort competition, reveal commercially confidential data, place undue burdens on market participants or incur excessive cost relative to the benefits.

Depending on the required information, the best form to mitigate risks can be to present *ex ante* information in an aggregate way (e*x-post* information can be disclosed with more detail, with some delay). The aggregation level will be dependant on how sensitive is the required information from a commercial point of view. As the relevant aggregation level for information in energy wholesale markets is the price zone, an aggregation per bidding area seems to be appropriate. Therefore, this should be the aggregation level as it is the relevant standard concerning price formation. The additional publication of certain data, which is relevant for evaluating security of supply, per country, should only be disclosed with the regulators.

Another important issue we like to mention is the risk that may result from uneven implementation of transparency rules. Thus, informational asymmetries within and between Member States must be avoided. Hence, the data should be made available under similar conditions to all market participants. In particular, they should be authoritative, issued at the same time and be easily accessible. The data should as far as possible use standardised definitions and formats to facilitate processing and analysis by market participants and allow harmonisation across national borders.

F. Market Abuse

20. Is the scope of *Directive 2003/6/EC on insider dealing and market manipulation (market abuse) such as to properly address market integrity in the electricity and gas markets? Would the assessment be different if greater transparency obligations in line with the analyses above were adopted? What suggestions do regulators have to mitigate any shortcomings?*

Generally, we think that the review process of the Market Abuse Directive is the adequate process to consider the need of further regulation of commodity firms concerning issues of insider dealing and market manipulation. Generally we are of the opinion, that the competent authorities should be able to investigate, if irregular behaviour is evident

and, additionally, may enforce adequate market standards. A practical solution in this context could be to apply the regime of the Market Abuse Directive also to commodity MTFs (this would avoid the need for an extensive revision of the MAD).

Besides, in respect to the question of greater transparency obligations energy companies are already subject to sector specific transparency requirements according to existing national and European law. In Germany this is mainly the Energy Industry Act (Energiewirtschaftsgesetz, EnWG) and its subsequent regulations. Additionally, harmonised energy-specific transparency requirements are discussed in the ERGEG Regional Initiatives and may soon to be applied. Additionally, several energy companies voluntarily publish generation data such as actual production or unplanned outages for the purpose of market transparency.

G. General

21. What timelines should be build into the implementation of any of the above recommendations?

After the outcome of the current consultation process (and respective recommendations) an appropriate timeline for an adequate implementation of the respective recommendations for energy trading companies should be ensured. In our view, an implementation time-span of at least one to two years would be appropriate. Again, a European-wide harmonised approach should ensure optimal implementation.