

E.ON proposals to amend

Draft Response to Question F.20 – Market Abuse

CESR and ERGEG advice to the European Commission in the context of the Third Energy Package

The E.ON Group considers the functioning of physical and derivative markets as one of the cornerstones for an Internal Electricity Market (IEM) and an Internal Gas Market (IGM) and, thus, welcomes the opportunity to comment on the joint CESR/ERGEG draft response (Ref.: CESR/08-509 and ERGEG E08-PC-30).

Questions to market participants

- 1) Do you agree with the analysis of the market failure in the electricity and gas markets as described above? If not, please provide reasons for your disagreement.**

E.ON has strong doubts how the general conclusions are derived from some single text findings of the Commission's sector inquiry where the extent across Europe has not adequately been proven. This applies even more as the Sector Inquiry is mainly based on data from 2005 and does not take into account recent developments in market liquidity, congestion management, as well as voluntary transparency initiatives. Furthermore, the statements of the sector inquiry describing the potential market failure (26 et seq.) predominantly relate to the market role of generators and the electricity market. These findings are not generally transferable to the gas market which is highly depending on imports from outside the EU on the basis of long-term contracts.

Nevertheless, we agree that market integrity issues in electricity and gas markets can generally arise due to asymmetric information but disagree with the same assumption for market power (26, 27). We will refer to it further below when discussing para 32 etc.

We appreciate that the analysis highlights the value of public information of fundamental energy market data (27). This is why E.ON started an own transparency initiative on electricity generation and network data in 2006 and has frequently contributed to several transparency fora in the framework of Electricity and Gas Regional Initiatives. Furthermore E.ON regularly provides data to transparency platforms such as ETSO (www.etsovista.org) and European Energy Exchange (www.eex.com/de/Marktinformation/Kraftwerksdaten). Even if we cannot judge the quality and reliability of other participant's data we share the wish of CESR and ERGEG to define precise definition and publication requirements addressed to and binding for everybody (30). The implementation of the already existing transparency requirements under the EU Regulations 1228/2003 and 1775/2005 varies throughout the EU. Therefore, E.ON supports all measures to standardise and harmonise these transparency requirements in order to avoid information asymmetry within the EU (see our answer to question 4).

E.ON does not share CESR and ERGEG view on market power (32, 33). E.ON has successfully grown over the recent years and become a European undertaking. As such we do not feel a lack of competition in general but see insufficient regulatory frameworks for competition when imposing price caps in retail markets or when not enforcing all kind of European regulatory requirements nationally. This is detrimental to competition and does not provide a level playing field.

Moreover, we doubt the adequateness of CESR's and ERGEG's correct understanding of market power and market abuse. Market power as such is not detrimental to competition per se if undertakings behave according to the existing competition and cartel rules. Just the abuse of market power should therefore be in focus. In this light we draw your attention to a study from Cologne University (Prof. Ockenfels) where the potential impact of single undertakings on spot market prices at German EEX has been investigated and denied.¹ A further analysis from Stuttgart University investigated the price fixing mechanism in the German electricity market. According to this study, the functioning of the wholesale market, especially regarding price fixing methods, cannot be doubted.²

The evaluation of the aforementioned studies should be also quoted in your analysis to safeguard a more balanced view (34, 35, 38). Please also note that the conclusion of your quoted study (40) related to the electricity market is to some extent misleading. It would be more correct to conclude that in a tight supply situation, where 250 MW has a large impact on the wholesale price, all market participants with a small to medium size power plant have the opportunity to influence the wholesale price. This is clearly not a case of market abuse.

We agree that structural tightness of energy supply usually attracts new investors in electricity generation (41). However, the significant local opposition against certain types of generation as well as insufficient political support and the absence of a consistent energy policy hinders new investments or delays them significantly. Rising investment costs also play a major role. E.ON cannot see how market power can have an impact on new investors as stated in (41) and footnote 11. This argument is rather contradictory to those in (40) where the European market is structurally tightening, the wholesale market is becoming a seller's market, and logically prices rise. The structural tightness for certain timeframes and regions can be proven, among others, by ETSO und UCTE generation adequacy and winter/summer outlook reports.³

Finally, we request to adjust para 1 of the draft response to Q1 which we find not sufficiently balanced according our statement above and not reflecting the still existing differences between the gas and electricity market.

2) What is your opinion on the analysis provided above on the scope of MAD in relation to the three different areas: disclosure obligations, insider trading and market manipulation?

E.ON generally agrees with the analysis and would also like to stress that MAD is principally designed for financial market and the confidence therein.

¹ http://www.eex.com/de/document/35282/gutachten_eex_ockenfels_e.pdf.

² http://www.ier.uni-stuttgart.de/publikationen/pb_pdf/Ellersdorfer_Preisbildungsanalyse.pdf.

³ http://www.etsa-net.org/activities/securityofsupply/e_default.asp.

3) Do you agree with the conclusion above that greater pre- and post trade transparency would not be sufficient in the context of market abuse?

E.ON does not agree with the general conclusion as indicated in question 3 and para 57. The analysis provided here lacks of a stringent argumentation and where evidence is shown (57, sentence 1) we have no opportunity to follow it.

This applies to the answers of CESR and ERGEG to the questions E 18 et seq. raised by the Commission in Section E which were not published at all. Moreover, the answers of CESR and ERGEG to the questions E 12 to E 17 raised by the Commission in Section E which were published most recently (Ref. CESR/08-527) only describe the status quo in the Member States. CESR and ERGEG do not give any answer to the question whether greater pre- and post trade transparency would contribute to a more efficient market.

In general, a binding disclosure of all fundamental data by generators and operators of transmission, storage and LNG systems which are considered being price sensitive would to a very large extent limit or, if sanctions are completely deterrent, exclude the opportunity for insider trading by definition. There is no more private information which has an impact on market price formation. We describe in detail in our response to question 4 how such a list can be elaborated and how this list should be made legally binding for everyone.

4) Do you agree with the analysis above on the importance of the transparency/disclosure of fundamental data? If yes, would you consider it useful to set up at the European level a harmonised list of fundamental data required to be published? Is an exhaustive list conceivable or is it necessary to publish additional data on an ad hoc basis if it is considered to be price sensitive?

E.ON completely confirms the urgent need for a binding disclosure obligation of fundamental data (58). We also appreciate all recent actions to reach a common understanding what kind of data should be published and in which manner.

Finally, an insufficient definition of data and time frames for publication has led to a wide range of practices across Europe (63, 64). Therefore E.ON recommends to define a comprehensive list of data which

- contains all information that are considered price sensitive subject to a proper consultation
- defines in detail data's definition, time frame for publication (periodically or on ad-hoc basis by an Urgent Market Message), duration of availability on a central platform, responsibility to provide data
- is binding to the relevant data providers such as TSOs, generators, storage and LNG system operators.

We accordingly propose for electricity to use the report on transparency from the Nordic region⁴ which has been the first available report and serves for the time being as a model for the other regional electricity markets.

⁴ http://www.energy-regulators.eu/portal/page/portal/EER_HOME/EER_INITIATIVES/ERI/Northern/Final%20docs/Report_on_Transparency1.pdf.

Concerning the gas transmission system operators we suggest implementing the TSO transparency project of the GRI North-West for all regions. Balancing-relevant data (e.g. linepack, balancing action) shall be published in real-time. Furthermore, the transparency obligations of the GGPSSO and GGPLNG should become legally binding. In addition to the disclosure of the amount of gas in each storage or LNG facility possible information advantages by vertical integrated companies should disappear. With respect to the so called 3-Minus-Shipper-Rule E.ON supports the deletion of the 3-Minus-Shipper/User-Rule in the proposed 3rd Package for transmission, storage and LNG systems. The data disclosed shall be standardised and harmonised to the greatest possible extent throughout the EU.

Data lists and related detailed requirements as described above should be made legally binding in the framework of Regulation 1228/2003 for electricity and 1775/2005 for gas and the affiliated guidelines. TSOs shall be responsible to arrange the publication of all data as contained in the data lists whereby a close cooperation with power exchanges would be beneficial. An ideal solution would allow to distinguish between original data from market participants and network data from TSOs and to retrieve information on different aggregation levels (EU-wide, regional, national, balancing zone). Integration into the homepage of power exchanges would make traders generally better off as they can inform themselves before raising their offer and demand bids.

Generators, storage and LNG system operators should be obliged to provide data to TSOs or directly to the central platform, if reasonable. ENTSO-E and ENTSO-G shall be in charge of coordinating the set-up of such a central platform with the power exchanges. Costs for the platform should be incorporated into national grid tariffs without any reservation from national regulators in order to avoid lengthy discussions.

The respective revision of 1228/2003 and 1775/2005 should be done as soon as possible in order to allow the release of all data on one single platform by 1 January 2010. Sanctions in case of withholding data should be adequate, deterrent and effective and shall be addressed to those who are responsible for data provision.

5) Which information retained by specific participants of the electricity and gas market (e.g. generators, TSO) should be published on an ad hoc basis if it is price sensitive?

According to our response on question 4 E.ON thinks that all information shall be published regularly. Unexpected technical disturbances (e.g. outage of power plants, network ruptures) should be communicated on an ad hoc basis and on a precisely defined short notice by the respective entity (e.g. generator, TSO) at the central platform.

6) What is your opinion on the proposals of CESR and ERGEG in the three different areas: disclosure obligations, insider trading and market manipulation?

a) disclosure obligation

E.ON agrees with CESR and ERGEG that both options, to keep the status quo and to amend MAD, are not reasonable (76-79) because the current situation would either not be improved for the energy markets or would most likely create unintended consequences for the regulated financial market.

We also agree that it would be the best way to integrate legally binding disclosure obligations into the existing legal framework as described under question 4 that take into account the specific needs of the energy market and energy-specific requirements (80 et seq.). Against the background of existing legislation it is not recommended to create a new Directive or a new Regulation, because too much legal frameworks get out of hand and open new room for interpretation. It should be in the interest of the authorities as well as the relevant entities to keep the legislation simple, clear, and manageable.

b) insider trading

We object to the conclusion derived from the consideration of CESR and ERGEG that disclosure obligations do not ban trading activities or hinder to disclose this information to 'a preferred third party' (90). It depends only on the obligation within the comprehensive list of data at which point of time specific information has to be made public and the implementation of completely deterrent sanctions. If this point of time is adequate and as early as possible there is almost no room for informing any preferred third party and thus very limited room for insider trading. Even in the theoretical case of any earlier information of a third party the advantage will be marginal. Therefore we advocate obliging all data provider to release the information at the earliest possible point of time and to impose adequate sanctions which market participants completely deter from any misuse. This would make a new tailor-made legislation dispensable, avoid significant costs as CESR and ERGEG themselves admit (101) and be in line with the Commission's goal to lower the administrative burden.⁵

c) market manipulation

The implementation of disclosure obligations including sanction mechanism opens a highly extended opportunity to detect and punish market manipulation. Therefore the effect on deterrence has to be considered. It is also worth noting that under today's framework national competition and financial supervisory authorities and the Commission already have sufficient legal competences to investigate potential market manipulation and market abuse as the practice shows. Thus, E.ON disagrees with the need for a tailor-made new legislation.

We also explicitly refuse para 2 and 3 in the draft response to Q 3 where the conclusion is drawn that such a new legislation would increase confidence in the market. This is simply an assumption without any proof. In this light, CESR and ERGEG should consider that the immediate disclosure of price sensitive data would have indeed such an effect. Assumed that such information is correct and is controlled by ERGEG or NRAs confidence will increase and more efficient trading decisions can take place leading finally to higher liquidity. Furthermore, increasing liquidity and harmonization of European trading points would disallow single actions of market manipulation as described in the single example from Nord Pool.

⁵ http://ec.europa.eu/enterprise/admin-burdens-reduction/home_en.htm.