The European Union of the Natural Gas Industry

14th July 2011

ERGEG DRAFT ADVICE ON THE REGULATORY OVERSIGHT OF ENERGY EXCHANGES
REF: C10-WMS-13-03

General comments

Eurogas appreciates the objective to identify best practice in the supervision of energy exchanges and hubs, against the background of converging national markets, particularly in electricity. As the development of REMIT demonstrates, energy markets are different from financial markets, and thus we recognise the need to consider regulatory oversight of exchanges not covered by MiFID.

While welcoming this opportunity to review ERGEG's thinking, Eurogas believes <u>it is essential to be clear what problem the advice is intended to address</u> and how it is intended to be progressed. In this context, <u>a clear definition of what constitutes an energy exchange must be provided</u>.

Eurogas is also concerned that the ERGEG survey supporting this advice has tended to focus on power rather than gas, against the background of power market integration and advanced thinking about market coupling. <u>It is essential that the final advice recognises where there are differences between the two markets</u>, in particular, the work on the gas target model, which is at an earlier stage of development, the importance in some markets of bilateral trading and in the case of LNG, the possibility that there will be trading on one exchange by reference to prices on another e.g. Henry Hub.

Eurogas does not see any need to pursue harmonisation just for the sake of it – there are Member State differences reflecting differing market circumstances and maturity. <u>The focus should be to determine only what needs to be harmonised and for any regulatory initiatives to be proportionate and related to the benefits identified</u>.
Since the advice was published, the text of REMIT has now been agreed. <u>In order for Eurogas to be able to comment fully on this advice, there must be clarity about how it relates to REMIT and to the implementing acts envisaged in REMIT</u>.

Eurogas also notes that MiFID is due to be revised shortly, with proposals expected this autumn. As yet therefore, the extent of exchanges to be covered / overseen by MiFID II is unclear, although we expect the results of this ERGEG consultation will contribute to the debate in this area.

Answers to specific questions

1. In your view, is there a need to create EU level requirements for the organisation, functioning and regulatory oversight of energy exchanges not falling within the scope of MiFID? If yes, what should be the main goals and objectives to be fulfilled?

Only to a limited extent.

Eurogas endorses the need for regulatory oversight of exchanges and for market surveillance teams within exchanges. To this end, a clear definition of what constitutes an energy exchange must first be provided.

Transaction reporting in accordance with REMIT is also needed, although Member States vary in which body has responsibility for oversight obligations under REMIT and the scope of REMIT itself is not yet fully clear. Given that an exchange may include both physical and financial products, MiFID and MAD could also be involved.

Eurogas does not see any need for regulators to go further than this, and does not believe exchange organisation or governance structures should be standardised. It is not clear there is a single best model – models vary, markets evolve and exchanges are developed as appropriate to their circumstances, in consultation with stakeholders and in competition with each other.

There is no evidence that a lack of harmonisation generally is a major regulatory problem, or that regulatory intervention beyond the above would be justified. Some convergence around good practice regarding exchange/trading rules can be expected to arise naturally, as required by the market.

2. In your view, what are the remits of national energy regulators in supervising energy exchanges and how could a beneficial cooperation between them be organised, in particular for exchanges active under multiple national jurisdictions?

Under the 3rd Package, the role of energy regulators is to supervise energy markets overall, focusing on the development of competition generally and in particular third party access arrangements. Energy exchange oversight by energy regulators should therefore be seen in this context. However not all energy regulators have responsibility for energy exchanges and depending on national market competences, oversight of energy spot markets may be shared or led by another national body.

The REMIT framework for an EU trade repository will allow energy regulators & ACER to conduct investigations into market participants suspected of insider dealing or market manipulation. However REMIT does not give regulators any powers over exchanges themselves, just over market players where there is suspected misconduct.

Where the necessary competences exist and exchanges operate across borders, it should be straightforward for energy regulators to co-ordinate their activities. As markets integrate, it is likely that ACER will play a more important role.

For all stakeholders, it is important that any procedural aspects associated with supervision by more than one regulatory body, both within a MS and across borders, are formalised and published so that monitoring arrangements and investigation roles are clear. Recognising the difference in the financial and physical regimes, it is also important that there is a high degree of consistency and co-ordination between authorities involved in investigations and the processes they have to follow.

3. Should the regulation of energy spot exchanges in future be covered by the energy market integrity regulation or by a separate future legal proposal by the European Commission?

To the extent that this is deemed justified, Eurogas believes that REMIT and related implementing acts would be the best means of covering energy exchanges and would be sufficient. We certainly do not see a need for further EU legislation in this area, which would only introduce further timing and co-ordination problems to what is already a complex legislative process.

However, because an exchange may be a monopoly does not mean that its operating rules have to be determined by regulators or that it has to be subject to very detailed regulatory provisions. Exchanges are dynamic and respond to market needs, with stakeholders typically involved in 'Advice Boards'. Flexible self-regulation in this area is generally preferable to EU-level legislation. An exchange can adapt to local market conditions, whereas a prescriptive EU-level regime is likely to be suboptimal for individual markets and market needs.

Energy regulators and ACER are already involved with stakeholders in market integration initiatives and the development of shared platforms and this in turn will result in changes to energy exchanges and greater convergence across Europe.

In addition regulators can evolve general good practice guidelines, in conjunction with stakeholders (see Q4 below) but these should not be binding. If suitable, they will be promoted by stakeholders in their individual exchanges.

Where a Member State's legislation requires energy exchange rules to be approved by their national regulatory authority, it is essential that these rules have been considered by market participants and after proper consultation.

4. How could in your view a harmonisation of legal and operational frameworks stimulate the cooperation of the European energy exchanges and what is the best way to involve the market/exchange participants?

Eurogas does not believe legal/operational harmonisation should be pursued as regulatory goal and we do not see any justification in the draft advice for this.

As we noted in Q1, it is not clear there is a single best model and we do not see a need to impose a standard organisation, governance structures or the same operational arrangements e.g. exchange/trading rules. Markets will evolve more harmonised approaches as appropriate, in consultation with stakeholders. Operational requirements are already covered in some detail in existing energy exchange rules and as noted in Q3, some convergence of these rules is likely to result over time.

While there is in our view no need for such harmonisation at EU level, we can see a value in drawing up good practice guidelines in certain areas e.g.

- consultation by energy exchanges, involvement of market participants in rule changes, keeping participants aware of future business plans etc.
- clear reporting obligations and processes in the event that potential issues are discovered by energy exchanges

Such guidelines can be used as a benchmark for both new and existing exchanges.

5. Which criteria should a European framework for market makers include to avoid potential conflicts of interests?

This question goes beyond the scope of the advice and the oversight of energy exchanges.

The concept of market maker as defined in MiFID applies to financial markets. In energy exchanges, there is no general requirement for market makers. They have been used mainly to encourage competition in newly liberalised markets and are therefore subject to national requirements related to particular national circumstances.

In Eurogas's view therefore, no EU-level regulation is required concerning market makers in energy exchanges, and harmonised criteria for their appointment and conduct are not applicable.

6. How could national energy regulators better work towards publishing of price sensitive information as e.g. foreseen in the ERGEG advice on Guidelines on Fundamental Electricity Data Transparency to increase the level of transparency?

This question also goes beyond the scope of the advice and the oversight of energy exchanges.

In Eurogas's view, market participants should have access to all relevant ex ante and ex post information as it may be defined. This includes fundamental data (e.g. as specified in the

ERGEG electricity guidelines) and transaction data on an aggregate and anonymous basis. Energy regulators should define what fundamental data should be published and work to evolve a single point of access for such data. In this context, the results of the ERGEG consultation on gas transparency in November 2010 are still awaited.

We do not see it is necessary to introduce a formal requirement that exchanges publish transaction data on their websites. Most energy exchanges surveyed publish traded volumes, price signals and other information and exchanges will respond to the needs of their participants. While some may charge data service fees for additional information services, such charges should not be excessive.

7. Which measures could in your view lead to a sufficient co-operation of market surveillance departments of the energy exchanges and the national energy regulators?

Irrespective of the kind of exchange, it is essential that each has a market surveillance department, with clear rules on what to do in the event that reportable issues become apparent in the course of their work.

Co-operation between the surveillance department(s) and the national energy regulator is of critical importance. Formalised arrangements must be in place for the reporting of suspected misconduct to the appropriate regulatory authority or authorities.

8. What are in your view minimum standards for a harmonised approach to protect energy exchanges from misbehaviours like market abuse?

It is in the interests of energy exchanges to protect themselves from market abuse, and they have thus evolved their own detailed rules in this area. Eurogas does not see the value of developing minimum standards for a harmonised approach at EU level for this.

At a regulatory level, misconduct/market abuse should be clearly defined within the framework of REMIT and implementing acts, and this will ensure a common approach to reporting.

In practice, energy exchanges will report suspected instances and leave it to the regulatory authority to pursue investigations. REMIT includes joint monitoring competencies for ACER/NRAs and financial regulators. To help ensure a level playing field, the reporting of outcomes by the regulatory authority and sharing between regulators will further encourage a commonality of approach.