

Comments to the Preliminary Report in the Sector Inquiry

DG Competition has invited different stakeholders to comment upon the Preliminary Report during the consultation period that runs until May 1st.

Vattenfall limits its comments to the electricity part of the report.

In Vattenfall's opinion, the Sector Inquiry and the Preliminary Report point to several important issues where improvements have to be achieved to reach a fully competitive market. The findings in the Sector Inquiry and the conclusions we have seen will, if dealt with in a constructive manner by national governments, regulators, the EU and market participants, improve the functioning of the market and contribute to restoring and strengthening trust in energy markets.

We do not aim to cover all the issues in the report in our comments but focus on what we see as the most important ones and what we think is of major importance in the effort to create a well-functioning market.

Unbundling

Unbundling is important to guarantee fair access to networks, to promote competition and to avoid cross subsidies between regulated and competitive activities. Vattenfall agrees that it is necessary to implement the unbundling provisions from Directive 2003/54 EC in all member states, and not just to the letter but also in spirit.

At the same time, we would like to stress that one should not focus on ownership unbundling as the key solution to the remaining problems. In our opinion, it is far more important to discuss the development of regional markets,

the role of regulators and the role of transmission system operators (TSOs) and cooperation between them.

Market Concentration, Regional Markets and the role of TSOs

The development of regional markets is the most efficient way to decrease market concentration and to get more actors on the market. However, we believe that regional markets cannot be developed without the active participation of TSOs and regulators.

The core role of TSOs must be defined and implemented. This core role can be defined in the following way:

- ☐ Ensure the operational security of the power system
- ☐ Ensure and maintain the adequacy of the transmission system in the long term
- ☐ Enhance efficient functioning of the electricity market
- ☐ Maintain the momentary balance between demand and supply.

In order to ensure that we have an optimal grid in the long term, grid investments must be made from a society economic perspective, which is why regulators have to be involved and agree on how companies shall recover the money spent. The grid has to be planned for the market it is going to serve. Earlier, it was totally natural that the grid was planned for the national market it served. If we are now aiming at regional markets then of course the grid has to be planned for such a larger market. The reason for this is that inside a regional market costs and benefits do not automatically arise within one and the same country. Investments made to remove a bottleneck in one country can certainly have benefits in another country. Similarly, delayed grid reinforcements in one country may be to the disadvantage of another. The rather static goal of 10% interconnector capacity in relation to installed generation capacity can serve as a guideline, but it also gives the impression of 25 different national markets interconnected with 10% of total capacity. 10% may be too little in systems dominated by hydro/wind power and too much between fuel-based systems with equal generation cost structures. The harmonization and integration of TSO activities on a regional market is, as shown here, much more complicated.

In the Preliminary Report implicit auctions are preferred compared to other congestion management models. Vattenfall agrees that implicit auction/market coupling is preferable when there is a structural bottleneck. However, implicit auctioning requires a liquid spot market. Therefore, the use of implicit auctioning is related to what we have said above about development in regional markets. Market transparency, which we comment on below, is also important to improve liquidity.

In the report, the importance of improving and harmonizing balancing markets is pointed out. Vattenfall agrees on the need to improve balancing markets. We have, for example, taken an initiative to submit a proposal on how to implement a balancing market in Poland to the Polish Regulator.

We would also like to stress the importance of introducing intraday markets. With developed intraday markets the costs of balancing would decrease, especially in systems with a lot of wind power.

The TSOs, if appropriately supported by the regulators, have a role to play in harmonizing balancing markets involving both balance control and balance settlement. The harmonization of balance settlement over a regional market is a necessary prerequisite for the development of retail markets that are larger than a single country.

Regional Markets and the Role of Regulators

TSO cooperation and integration can, however, not take place without a new role for regulators. The pure national mandates that regulators have today have to be complemented by regional and European mandates to enable market integration. Without regional and European mandates regulators will not be able to provide TSOs with clear incentives to invest in interconnections. Regulators have to agree on an appropriate sharing of costs and benefits. In systems with increasing amount of wind power it becomes even more important to be able to reinforce the network. Regulators have a role to play in enhancing licensing procedures. However, most of the problems with the lengthy licensing procedures we see all over Europe lie purely in the hands of governments and national parliaments and how they steer national and local authorities.

Transparency

The report identifies the lack of transparent market information as a big problem in many markets. Vattenfall's opinion is that all market participants shall have access to the same information at the same time. Relevant information is such information that is important to price formation. We fully understand customers and other market participants who complain about the lack of transparency and believe that a major increase in transparency will help to restore trust in the market and boost liquidity. With increased transparency we expect large consumers to play a more active part in the wholesale market. Vattenfall would welcome such a development.

Vattenfall has in Germany taken an initiative to voluntary disclosure of market information. The largest power companies in Germany will start to publish information on a platform of EEX.

Both Eurelectric and ERGEG have presented proposals to improve transparency. The two proposals are quite similar. We would support coordinated work, including consultations with power exchanges, to present a common proposal to the Florence Forum in the autumn. After an agreement at the Forum, the proposal could be implemented all over Europe as a minimum standard.

Regulated tariffs for end users

The report sees the existence of regulated tariffs below market prices as a problem in many markets. Vattenfall agrees that such regulated prices effectively hinder competition and new entrance into a market. We find it difficult to understand how such price regulation can be in line with article 3.2 in Directive 2003/54 EC with respect to the right of any European firm to have access to all European customers. This is simple, because as a new entrant on a market you have to rely on the wholesale market for your power purchases. If end user prices are regulated below these market prices then you can hardly be competitive. Vattenfall proposes that DG Competition should supervise such price regulation.

Terms and contracts to energy-intensive users

The report states that support schemes for large energy-intensive users – which are currently being considered in a number of member states – need to be compatible with antitrust and state aid rules.

Vattenfall welcomes this statement since anticompetitive offers in one member state can harm both industrial customers and the electricity industry in another member state. Vattenfall proposes that DG Competition shall supervise this to ensure that terms and conditions are compatible with antitrust and state aid rules.

Vattenfall is grateful for the opportunity to take part in the consultation process. We are also prepared to respond to any questions you may have regarding our comments.



Lars G. Josefsson
President and CEO
Vattenfall AB