
**CEER position paper on the European Commission's Communication
'Making the internal energy market work'
May 2013**

1 Background information

This paper provides comments of the Council of European Energy Regulators (CEER) on the European Commission's Internal Energy Market Communication (IEM) (COM/2012/0663).¹

The paper underlines issues of key importance to energy markets. It also emphasises issues of relevance to energy regulation, in particular emphasis on the role of effective and independent energy regulation; the central importance of full implementation of the Third Energy Package; the impact of regulated energy prices; the fundamental priority of consumers' interests; the role of distribution system operators and the critical need to ensure generation adequacy. The Annex of this document provides a more detailed commentary on the Communication's Action Plan for those measures which include energy regulators as an involved "actor".

2 General remarks

European energy regulators agree with Council views on the need for a fully consistent approach to energy policy – climate change goals; competitive markets; and consumer protection and social welfare must go hand in hand when developing the framework for our energy sector, lest we create incompatible and conflicting requirements between them and ultimately frustrate their individual and collective achievement.

Energy regulation has an important part to play in ensuring we can deliver these achievements, in particular by overseeing market developments and providing sound and predictable regulatory policy. Efficient energy markets - at national, regional and international levels - are a prerequisite for energy security and sustainable development. Competitive energy markets must provide a secure, reliable and affordable energy supply which is essential for efficient economic and social development.

¹ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52012DC0663:EN:NOT>

3 Completing IEM and achieving the 2014 deadline

Regulators firmly believe that timely and comprehensive transposition of the Third Energy Package is essential for allowing electricity and gas markets to reach their full potential. Coordinated efforts at all levels, including implementing the Electricity and Gas Target Models, tapping the goodwill of market participants through the Regional Initiatives and supporting investments in needed infrastructure are also critical to achieving our overall goals (see Actions 1, 4 and 11 in Annex). Indeed, we agree with Mr Buzek, Member of European Parliament (MEP), as rapporteur on the European Parliament's draft report on the IEM Communication, that lack of full implementation remains the main obstacle for the completion of the internal energy market.

Regulated prices: We welcome the Council's interest in this issue and we would like to stress the possible distortionary effect of regulated end-user prices. Even though in some cases the regulation of prices may have been instituted to keep companies from abusing their market position (rather than relying on enforcement of competition law). However, different price setting rules and methodologies in place in the Member States with regulated prices could have differing effects on retail market conditions, these kinds of regulations interfere with the basic rules and principles of the IEM. They can exacerbate or perpetuate market foreclosure if set at a level which does not allow costs to be recovered. Removal of this and other market barriers (price caps, absence of a level playing field for all generation technologies) are essential for ensuring that energy markets can function properly. National Regulatory Authorities (NRAs) can play an important role to ensure fair prices by executing their monitoring tasks. The Commission could consider developing guidelines on the interpretation of abusive behaviour in retail markets in order to promote competition. Meanwhile, the phase-out of regulated prices should continue, while giving due consideration to lack of adequate infrastructure connecting remote areas and "energy islands" and designing targeted tools to support and protect vulnerable consumers. On this particular issue, we welcome a similar call made by Mr Buzek MEP, who notes the threat that regulated prices can represent for future investment signals.

Subsidies and market functioning: NRAs promote and support the development of competitive markets, with minimal interventions and distortions to price formation. While interventions to address identified externalities can be beneficial, we believe that going beyond this into support for specific energy sources distorts the energy markets (with either positive or negative effects on investments). For example, this could result in different types of generation benefitting from so-called "windfall profits". In a truly competitive market, all energy sources would participate on their own merits and decisions would be economically efficient and consistent (see Action 20 in Annex). The existence of support schemes may induce non-negligible impacts on generation investment decisions, which, in turn, could increase the risks of jeopardising generation adequacy. In addition to financial impacts, recent CEER reports on renewable support schemes confirm our view that we must encourage the evaluation of the wider implications of integrating renewables into the system; not only from a financial support perspective but also from the perspective of system security and market design.

Target models: Meanwhile, fast implementation of the European target models for electricity and gas will enhance the internal market, by stimulating efficient cross-border use of existing generation and creating incentives for new investments. Efforts to establish widely integrated day ahead, intraday and balancing markets (e.g. market coupling, implicit intraday cross-border allocation and coordinated re-dispatch, flow-based capacity calculation) should lead to better price formation; reinforced security of supply across borders; more efficient use of existing infrastructure and generation; and clearer signals for the need for additional investments.

Integrity and Transparency of Energy Markets: Regulators firmly believe that the integrity and transparency of energy markets are essential to promote a level-playing field for all market participants and consumers' confidence that prices in the internal energy market correctly reflect the interplay of demand and supply conditions and are not the result of abusive practices. It is therefore essential that the Regulation on wholesale energy market integrity and transparency (REMIT)² is implemented effectively in parallel to the integration of the internal electricity and gas markets. Both at national level and working through the Agency for the Cooperation of the Energy Regulators (ACER), regulators are preparing the groundwork to meet their responsibilities in this area.

Effective regulatory framework: Regulators firmly support statements regarding the need for a predictable and reliable regulation. This is a key factor in building investor confidence in a stable and fair framework in which to undertake long term and costly commitments. The widespread implementation of affordable and accessible clean energy technologies and a shift towards new and smarter technological solutions means that energy regulators must continue to develop their own regulatory framework and approaches to ensure continued effective regulation. Sound regulation provides a much needed service of oversight and review of the energy sector, to ensure proportionate and necessary investments, fair pricing and a level playing field for all market participants. Whether investments are due to replacement of ageing infrastructure; expansion of our networks to meet increasing (or changing) demand; or a move towards new (sustainable) technologies, independent regulation aims to provide market certainty, predictability and clarity to ensure fair and adequate solutions are implemented. In order to foster sustainable development, including the integration of renewable generation into the networks, regulation must promote consistency of rules, market-based mechanisms whenever technically and economically feasible, fair and reasonable tariffs, decision-making processes based on widespread consultation and involvement of stakeholders and transparent monitoring. With this in mind, we strongly support the transposition and implementation of existing legislation, which provides a full set of tools for delivering competitive energy markets, before developing any additional policies.

Unbundling: Through CEER, regulators advocated the need for effective unbundling of energy utilities, to the benefit of competition and consumers. Many of us are currently in the process of certifying our Transmission System Operators (TSOs) at national level in line with the Third Energy Package requirements. In addition, we have published a report reviewing the status of Distribution System Operator (DSO) unbundling and we are planning a second report on both DSO and TSO unbundling later in 2013. We welcome the Council's invitation for the Commission to present an analysis and guidance on institutional investors that wish to invest in both energy generation capacity and energy infrastructure.

² <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:326:0001:0001:EN:PDF>

4 Improving rights and roles of consumers

Through CEER, Europe's energy regulators aim to promote well-functioning and competitive EU energy markets so that consumers get fair prices, the widest choice of supplier, the highest quality of supply and are given simple, transparent information about their energy consumption. Our work ranges from providing guidance and developing advice on best practices to sharing experiences and conducting a resolute market monitoring to ensure that Europe's markets are delivering benefits to energy consumers.

Key to this work is understanding what customers want and need; ensuring that the market and services are in tune with their priorities. As explained in the Annex, under Actions 6 – 8, regulators have developed a 2020 Vision for Europe's Energy Customers, outlining four principles governing the relationship between the energy sector and its variety of customers: reliability, affordability, simplicity, protection and empowerment. Our on-going and future work starts with this objective and calls upon energy market actors to join and commit to achieving this Vision through their scope of activity. Included in this work is a recognition of the particular needs of vulnerable customers (see Action 2 in Annex). Regulators agree that energy sector specific measures as well as wider social policies have an important role to play, especially for the poorest and more vulnerable.

CEER agrees that demand response is an area that can deliver benefits both to consumers and to electricity systems. Demand response can change electricity usage over time as well as reduce consumption when security of supply is in danger. The change of consumption patterns has the potential to decrease costs over the longer term due to reduced requirements for investments in generation capacity. However, building a smart distribution network capable of dealing with fluctuations in usage could entail additional investments.

Member States can support the active participation of consumers in electricity markets by setting a regulatory framework that fosters:

- Customers' understanding of information on the electricity market and increased provision of information to customers (through smart meters for example);
- Customers' awareness of new marketing opportunities (e.g. participation in balancing markets) or new contracts reflecting actual market situations in an appropriate way (Time of use prices, dynamic prices, critical peak prices, interruptible contracts), etc.;
- Customers' trust in the market and thus wanting to participate;
- A non-conflicting grid tariff to stimulate energy efficiency and demand response;

5 Contributing to transition to IEM of the future

Smart networks: As responsibilities shift and consumers are increasingly expected to become more active in energy markets (through developments such as demand response, smart metering, micro-generation or energy efficiency measures), our Customer Vision recognises their right to choose by whom and how their energy is to be provided and charged. This also means we must ensure that the tools and services make sense from a customer perspective and that their use is transparent, simple and interoperable. Regulators have produced an extensive body of work on functionalities for smart meters; the roles and responsibilities of various market actors in a smart meter (and demand response) environment; data management; incentivisation of smart grids, and more. Most immediately, we are working on an assessment of the roll-out of smart meters and of regulatory approaches to enabling smart grids (see Action 14).

Distribution System Operators: The role of the DSO in Europe's evolving markets is of central importance. As a regulated entity, the DSO is supervised, monitored, guided by regulation – which also ensures a certain degree of quality standards and practices (see Action 15). We agree that a thorough assessment should be undertaken to understand the implications of any change in roles, including taking into account that national or local networks have particularities associated to their market, geography, energy mix, etc. In the evolving smart network scenarios, where many new functionalities and technologies are coming into play, DSOs will have to move from a passive to an active role. Regulation should support and govern the above process while ensuring a level playing field also for other – independent – suppliers of the services.

Generation adequacy: Regulators believe that assessing and ensuring generation adequacy is essential for effective system operation and security of supply. Currently there is limited coordination of these assessments at European level. A full definition of generation adequacy is still needed, whilst at the same time recognising the differing (and unique) characteristics of Member States' electricity systems. There is scope to improve existing methods and identify best practices. The Commission could undertake an impact assessment to benchmark existing methods and standards in order to understand better where enhanced coordination and cooperation would be beneficial (see Action 19). Here again we welcome Mr Buzek MEP's appeal to consider cross-border solutions and to analyse the cross-border implications of such mechanisms. Certain issues would merit particular attention:

- Developing a comprehensive understanding of the role of interconnectors and the impact of transmission constraints across and within Member States;³
- Assessing the arrangements in place between TSOs for close to real-time exchanges of electricity;
- Assessing the probability that maximum peak load periods coincide in adjacent Member States which would prevent cross-border generation capacities from contributing to security of supply at national level.

Taking stock and planning for the future: Regulators stress the importance of evaluating how the framework is working and whether the rules deliver, as intended, more competitive,

³ For example, constraints exist between all Member States, except for the German-Austria border, but also within some Member States.

integrated and affordable energy markets. We will need to review and, if necessary, update the Electricity and Gas Market Models to ensure they remain relevant, consistent and effective. Indeed, CEER is currently working on an additional building block for the gas model, through a “Blueprint on incremental capacity” (i.e. market-based investment procedures) in gas which was discussed at the Madrid Forum on 17 April 2013.

The Commission could be invited to discuss how far the regulatory framework can go; is it sufficient to implement a set of market rules or do we need to consider additional tools to help foster competition which should ultimately help to deliver a low carbon economy and secure energy supplies at the most efficient possible cost?

Annex: National Regulators for Energy as “actors” in the IEM Communication Action Plan

Action 1: Member States must transpose and implement the Third Energy Package in both the detail and in the spirit of the law. Full transposition of the legislation is a prerequisite for allowing the electricity and gas markets to reach their full potential, involving customers at the heart of the internal market.

Action 2: We agree that vulnerable customers need consideration and we welcome the Commission’s intention to provide guidance to Member States on helping to define the concept. In this time of change, there will be particular challenges for vulnerable customers. Final customers have to be protected, while Member States may choose different approaches to achieve this goal. Some Member States may find it appropriate to perform targeted assistance; some may find it appropriate to use social policy frameworks, avoiding possible distortions to energy markets. Some Member States may choose a combination of both. A one-size-fits-all solution would be difficult especially given that social systems within the European Union are not harmonised.

Action 3: Regulators derive their powers and responsibilities from this proper implementation by policy makers. Their independence and empowerment is essential to allowing them to play their role in achieving the internal energy market. Adequate and comprehensive regulatory powers, resources and independence remain essential to provide for an effective implementation and enforcement framework. We look to the Commission to monitor closely the effective implementation by Member States of the NRA provisions in the Third Energy Package and of the major provisions of the evolving REMIT regime.

Action 4: We support the Commission’s call for enhanced effectiveness of the Regional Initiatives. Along with making further progress through the list of network codes and their subsequent - and early - implementation, the Regional Initiatives are a sound basis for meeting the 2014 target and provide valuable input for the rule-making process. We consider that the full involvement of stakeholders and the support of Member States and the Commission remain essential to deliver a voluntary platform to test and apply the rules we have been developing.

Action 6: Building on its longstanding commitment and activities in the area of energy consumer rights, in 2012, CEER launched a Joint Vision with the European Consumers Association⁴, BEUC, throwing open the debate on energy customer participation in EU energy markets. We strongly consider that customers play a key role for a competitive energy market. Providing the services and information they need may increase their activity and enhance market competition. (CEER has recently launched a dedicated [customer section](#) on its website.) We are committed to developing our 2020 Vision with concrete actions. In 2013, we also plan to host our second interactive customer conference and a joint inter-regional workshop with the Energy Community Regulatory Board and European

⁴ http://www.energy-regulators.eu/portal/page/portal/EER_HOME/EER_PUBLICATIONS/CEER_PAPERS/Customers/Tab3/CEER-BEUC%202020%20VISION-joint%20statement_Long_v130513.pdf

Regional Regulatory Association colleagues. Both will continue the sharing of best practices, inform the development of customer-oriented energy policy and convey consistent and clear messages to customers across Europe. We take very seriously the new role for regulators in the Energy Efficiency Directive and were pleased to provide the Commission services with our feedback on the interpretative guidelines for the Energy Efficiency Directive. CEER is also preparing a review of customer access to the information on the cost and sources of energy and efficiency schemes.

Action 7: CEER welcomes the Commission's plans to set the scope for research, data collection and reporting on energy retail markets. We are ready to help (as we are with ACER) with the provision of data on markets, using our long-established database for collating national facts and figures. We are also collaborating with DG SANCO on its survey activities (and their use) to evaluate better the levels of awareness and satisfaction amongst Europe's energy customers.

Action 8: Through a number of our 2013 deliverables (status review of the involvement of customers organisations in the regulatory process; status review of customer access to the costs and sources of energy and efficiency schemes; and advice on green electricity offers), we intend better to understand the customer's situation. While providing the correct information and services is a good first step, we consider that understanding what customers perceive, acknowledge and want is equally essential. Indeed, excess information can have the opposite effect, making sensible choices even harder for customers. Therefore, we welcome the opportunity to share our experiences and to work with the Commission on these issues.

Action 9: Regulators are committing significant resource to their work in ACER to develop framework guidelines and review the corresponding network codes which will provide the tools for delivering an internal market. The regulator-led working groups in ACER are dedicating their full expertise and efforts to defining this new framework.

Action 11: As regards energy infrastructure, whilst we welcome the early steps taken through the TYNDP process and cost-benefit analysis, it is clear that substantial improvements are needed and we have provided constructive proposals and will continue to advise on this. We are equally conscious of the regulatory challenges of coordinating investment decisions and allocating costs. Regulators will continue to work within ACER to develop best practice in this area.

Actions 14: Smart grids will have a significant impact on the way our grids are function and how consumption can be managed. Demand response, distributed generation, home automation, etc. will require careful treatment to ensure they deliver for consumers and develop in a fair, transparent and efficient way. CEER is working on advice for data management for better retail market functioning; a status review on the roll-out of smart meters (in line with our previous recommendations on the functionalities they should have); a status review on regulatory approaches to enabling smart grid solutions; and guidelines of good practice on demand side management.

Action 15: CEER fully agrees with the Commission that the role and potential of DSOs should be better recognised and reconsidered. In addition to its recent status review on the unbundling of DSOs, CEER will also analyse DSO services for consumers, acknowledging that energy efficiency and customer activity are two key areas in which DSOs play an essential role. In addition, reliability and quality of service and the manner in which these services are defined and carried out is an important part of market design. We recognise the key challenge as being to provide a smart regulatory framework which encourages access to the benefits that smart grids and meters can provide for capabilities including demand

response. Given our responsibility in regulating these natural monopolies, we are keen to contribute to the Commission's reflection on the future roles and responsibilities of DSOs.

Action 18: CEER supports the Commission's plans to address the continued use of regulated prices in many Member States. While we favor the phase out of these price controls, at the very least, regulated prices should be set at a level which avoids stifling the development of a competitive retail market and should be consistent with the Third Energy Package provisions. Indeed, regulated prices may prevent consumers from receiving appropriate price signals and they can suppress competition if set at a level which does not allow costs to be recovered. Regulators will continue to report on prices in the annual ACER-CEER Joint Market Monitoring Report due at the end of 2013.

Action 19: In terms of capacity assessment and generation adequacy, we welcome the Commission's initiative and believe that a careful assessment of impacts is needed when looking at new complementary market design policies and that cross-border effects should be thoroughly considered in order to understand possible consequences on the internal market. CEER recently participated in the DG ENER consultation on this issue. In 2013, CEER and ACER are collaborating to contribute to the debate that the Commission is leading by assessing the impacts of electricity capacity market developments at national level together with their potential impact on the electricity market and market integration.

Action 20: CEER looks forward to working with the Commission on its guidance on renewable support schemes. However, we encourage the evaluation of the wider implications of integrating renewables into the system; not only from a financial support perspective but also from the perspective of system security and market design. CEER will continue its regular activity in reviewing national support schemes for renewable energy sources and adds to its repertoire in 2013 with specific deliverables to conclude a: Status Review of customer access to the cost and sources of energy and energy efficiency schemes; Guidelines of Good Practice on Demand Side Management; and a Benchmarking Report on flexibility tools for future electricity markets. We are well aware of the substantial impact that these topics will have on market functioning and overall design going forward.