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Agency for the cooperation of energy regulators
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# European Energy Regulation: A Bridge to 2025– PC_2014_O_01

The Finnish Energy Industries (ET) is a trade organisation for producers, suppliers, transmission, distributors and sales of electricity, for district heating and district cooling, and for design, implementation, operation, maintenance and construction of networks and power plants.

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**Finnish Energy Industries welcomes the opportunity to respond to the public consultation paper entitled "European Energy Regulation: A bridge to 2025" launched by ACER. Finnish Energy Industries is pleased that ACER has taken the initiative to identify the key challenges and regulatory actions that should be undertaken moving towards 2025.**

**Our answer is divided according to categories used in consultation paper, namely:**
**A. Electricity wholesale markets**
**C. Infrastructure investment and**
**D. Consumers, retail markets and the role of DSOs**

**In general we welcome and support ACER's findings and proposals. However we emphasise that ACER's focus should be on issues that either already have European regulation or have cross-border effects. Especially many consumer-related issues are characteristically national, and we find little benefits for European intervention in those issues. It may be very difficult to find common models that would benefit consumers in different countries. Rather, ACER could give advice to national regulators and be an information sharing platform for best practices.**

**We very much welcome ACER's statement in the introduction that "the purpose of energy regulation is to deliver a level playing field in which competition can flourish and provide a sound investment climate that is based upon a stable and predictable regulatory framework."**

## A. Electricity wholesale markets

*1. Have we identified correctly the issues and trends within each area of the energy sector?*

We consider that ACER has rightly identified the main issues and trends in the electricity market where technology development is facilitating new power generation resources, increasing demand-side market participation and strengthening European-wide market integration. Especially we agree with the finding that policy interventions are the main source for challenges currently faced in the European energy markets.

As additional emerging trends in power generation and wholesale electricity markets we would like to highlight the following points that also need to be taken into account when determining the future regulation needs:

- Electricity wholesale trading is and has been moving from physical bilateral contracts to power exchange trading and financial hedging contracts. Financial regulation is increasingly affecting the energy market
- The increasing share of intermittent generation from wind and solar power is weakening frequency and voltage stability and reducing the system inertia, which in some synchronous regions is already requiring specific measures. The TSOs should be required to use market-based procurement (from both domestic and cross-border resources) of all the needed system services for guaranteeing the system operation without limiting the possibilities for grid connections and operation of either existing or new generation or demand facilities. The possibilities for customer appliance standards (e.g. through the Ecodesign Directive) for automatic frequency response could also be studied.
- New energy storage solutions, in addition to distributed generation and new flexible demand like electric vehicles, are increasing the possibilities for market-based system optimisation providing high security of supply also with reducing conventional generation resources. Also the existing energy storages, namely electrical heating, can be used for flexibility services. The energy market regulation should enable smooth utilisation of these possibilities.

*2. Have we identified an appropriate regulatory response?*

The regulatory response to market needs to be consistent and cost-effective, enabling market-based solutions with active customer participation. Based on ACER's consultation document, we emphasise the following points:

- The configuration of bidding zones is important for all market participants. Large enough bidding zones are essential for adequate retail market competition, foreseeable investment conditions, and customer trust in the market functioning. Grid congestions should primarily be removed through grid investments. Market-based redispatching, with adequate balancing reserves contracted in advance by the TSOs, can also be used.
- National support mechanisms for RES generation and capacity adequacy can and should be gradually phased out with a stronger role for CO2 emission trade, European-wide market integration, widening market-based demand response resources, and adequate balancing reserves contracted by the TSOs.

*3. Which regulatory actions are most important and should be prioritised?*

The following measures need to be urgently implemented in order to secure reliable and affordable electricity supply to all European citizens:

- Implementing the integrated day ahead and intraday market in Europe. Where European solutions seem difficult to achieve, at least regional solutions, compatible with neighbouring regions, must be implemented as a priority. The long lasted debate on intraday-solution is seriously affecting the RES-producers. In Nordic countries we fortunately have enjoyed already for a long time for a robust intraday settlement.
- To ensure that adequate resources are in use for finalising the Network Codes for the EU electricity and gas markets. We however express a concern for the level of details that is being written in the Network Codes. Indeed, instead of requiring more content, ACER should focus on ensuring that ENTSO-E doesn’t propose too extensive requirements for other market actors. Network Codes of special concern related to this are the RfG and DCC.
- Possibly the greatest achievements in NC-process have been, that TSOs were forced to discuss and share information on a detailed level. We welcome ACER’s target to promote cooperation between TSOs.
- Securing the functioning and development of liquid financial power markets
- Removing regulated prices and bidding restrictions
- Continue to address issues having cross-border effects. We welcome ACER’s notice on the CRMs and that they have to be designed so that the potential negative effects on electricity markets are minimised.

*4. Are there other areas where we should focus?*

The amount of financial regulation aimed at financial institutions is increasing and increasingly affecting energy markets. ACER should focus on interacting with Commission and financial regulators in order to advise them on energy markets differences from investment instruments' markets and how to implement financial regulation without negative impact on energy markets efficiency.

The trend towards efficient trading arrangements is threatened by rigid application of tightened financial sector rules without recognising the asset/demand-backed characteristics of the energy market. Without possibilities for affordable financial hedging, incl. the use of bank guarantees in the trading of financial electricity contracts, the trading liquidity in both physical day-ahead trading and in financial products would severely suffer, resulting in added costs for the customers.

Harmonising the level playing field with the means of Network Codes should be done more carefully. There is a threat that some aspects of national or regional models are promoted to become parts of a European model without appropriate analysis on system coherence and applicability to the Target Model. Special concerns are related to NC FCA and NC Balancing. The NC FCA is focused on one market structure being used in CWE-area. The products used in the Nordic market are however different, and the market well developed. In NC Balancing there is a proposal to limit settlement period to 30 minutes or less. We find this requirement potentially a major threat for the implementation of demand response that typically is based on hourly prices and hourly metering.

The CRM discussion is largely based on concerns about Security of Supply. However in different countries SoS seems to be understood in very different ways. We encourage ACER to work with ENTSO-E for to find a common way how assess Security of Supply.

**C. Infrastructure investment**

*1. Have we identified correctly the issues and trends within each area of the energy sector?*

New power transmission technologies enable the construction of multi-terminal DC grids and reduced costs for underground or tunnelled high-voltage lines. The TSO regulation should allow adequate grid investment cost recovery through grid tariffs and market-based procedures for power trading and generation connection in international multi-terminal links.

We very much welcome ACER's notice that infrastructure projects must be executed in a timely manner and encourage ACER to interact and comment different regulations that are causing or enabling the unacceptably long permission processes.

We agree with ACER's notice in 2.21 that "it is far from straightforward to allocate the investment costs of a cross-border project between individual countries". We consider that cost allocation shall be based on TSOs' agreement on cost sharing. What ACER could do, is to give guidance for NRAs to accept investment taking place also outside individual TSO's control area to this TSO's tariff basis, when the investment is beneficial for this TSO's customers.

*2. Have we identified an appropriate regulatory response?*

The power transmission grid investments should be driven by total socio-economic benefits based on market-wide cost-benefit analysis, not only by market signals showing profitability for the investing TSOs who are also receiving congestion revenues. Thus the regulators need to monitor the grid planning and secure adequate transparency and stakeholder involvement in the grid development plans and decisions.

*3. Which regulatory actions are most important and should be prioritised?*

Enabling transmission grid investments through fast licensing and adequate tariff financing.

ACER should take a closer look on how different TSOs use congestion incomes. As grid investments should be financed with tariff incomes, the congestion incomes should be used, as

a rule, to ease the congestion on borders where congestion occurs. We very much encourage ACER to give an opinion on this.

*4. Are there other areas where we should focus?*

The implementation of smart meters is lagging in Europe. These are the prime tools for to ensure active demand side participation into to market. As the share of intermittent generation increases, the more important it becomes that end-users have a real possibility and motivation to adjust their electricity usage according to hourly prices of electricity.

As the energy efficiency develops and micro-generation becomes common, the energy input from grid decreases while the needed power may even increase. This is leading to situation, where energy based distribution tariffs are no longer applicable, and we see a need to adjust DSO tariffs accordingly in the whole Europe. For example GEODE has done analysis on this subject.

DSO infrastructure investments must be ensured in order to maintain security of supply. We have commented DSO investments more thoroughly under the part D.

**D. Consumers, retail markets and the role of DSOs**

We broadly agree with the assessment made by ACER of the main trends shaping retail markets and the future role of consumers.

However, we would like to point out three issues that in our view deserve further attention.

- Retail markets should have a possibility to function on a competitive and level playing field. This means phasing out price regulation in European retail markets. Price regulation is one of the main barriers against customer empowerment and the foundation of well-functioning retail markets. Social security measures should be the main measures for protecting customers against all poverty including energy poverty. Energy efficiency measures financed from the governments budgets can be also used to reduce poverty.
- The energy sector's performance towards its customers is sometimes reported as being one of the worst compared to other utility sectors. It should be noted that according to a customer survey (answered by 1,004 full-aged Finns) carried out by YouGov Finland in July 2013 for the Finnish Energy Industries, 3 out of 4 people who have switched electricity supplier felt the process completely unproblematic/swift. Up to 9 out of 10 felt supplier switching completely unproblematic or almost unproblematic. Hence it needs to be noted that at least in some Member States the electricity sector is very much focused on customers and has succeeded in providing customer satisfaction.
- Also it needs to be noted that one of the most common complaints by consumers is about rising energy prices – for which the industry is only responsible to a very limited degree, a big part of the increase coming from taxes and levies.

ACER generally acknowledges the investment and revenue challenge at the DSO side. However, we would like to see more clarity with respect to some of the issues.

- The main investment drivers for DSOs include "smart" investments, but also a number of "conventional" investments to traditional grid solutions (lines and cables, transformers, etc.). These investments are crucial to maintain security of supply. ACER correctly identifies the need for regulation to develop in order to encourage investments both on DSO and TSO level. The need for DSOs' investments will dramatically increase within the following years as a result of bringing intelligence to the grids, but also renewing the old network assets. Regulation must enable and support these substantial investments.
- ACER correctly recognises as a trend that increasing amount of non-programmable RES requires more coordination and information exchange between a DSO and a TSO. Many Member States' example shows that most of the new NP RES is installed in distribution networks. The DSOs will thus have an even bigger role in system operation and management. DSOs' traditional mission of managing the distribution grid however will

not fundamentally change; DSOs will just need new tools in order to fulfil it. This is one important priority in regulation also.

- Besides cost recovery, the regulators should also focus on revenue recovery, i.e. design of network tariffs. Transparent and more cost-reflective network tariffs are essential in the future. Network costs are mainly capacity driven. Network tariff structures should incentivise both efficient investments and efficient use of the network while providing a stable framework for both customers' bills and DSO revenues. Appropriate approach would be a suitable power based tariff structure.

*Detailed comments on ACER's findings and proposals on Consumers, retail markets and the role of DSOs*

**2.29**

ACER states that micro grids will develop in specific areas as a consequence of the growth in embedded micro-generation and the developing need for greater service quality. This issue needs more clarification. It is hard to see that micro grid, operating as a separate island, would be able to provide greater service quality to the customers in terms of electricity quality and security of supply.

**2.23**

ACER correctly states that "*The European Commission has noted that energy prices have increased in recent years. Significant increases in taxes/levies (including RES subsidies) and the anticipated growth in other costs will also impact on consumer prices. Policymakers will need to ensure that the impacts of their policy changes are applied as cost-effectively as possible*." We fully support this.

**3. D REGULATORY IMPACTS: Consumers, retail markets and the role of DSOs**

In the beginning of this chapter ACER states:
*"Stakeholders strongly argued for protection and empowerment of consumers so that they remain at the heart of retail markets. They explained the need for greater transparency of consumption information whilst protecting and securely managing consumers' personal data and envisaged a role for suppliers to act as a single point of contact for consumers thereby facilitating easier, speedier switching.*
*A core role for DSOs is that of a 'neutral market facilitator' responsible for distribution networks' system and possibly data management. When considering unbundling, the importance of the full implementation of the Third Package rules was highlighted, arguing that regulators should define clearly the relationships between DSOs, other service providers and consumers and develop a clear framework that supports new market players, such as aggregators."*

We support these key principles and further emphasize the following;

- The supplier centric model (where a supplier is a main point of contact, but all issues that are strictly network related, should be handled by the DSO) is of key importance for a customer driven development of customer service and products, forming the foundation for improvement of the customers' perception and trust for the industry. Smarter use of energy will need packaging of customer friendly services that are easy to buy and use.
- The DSOs should not participate in commercial operations, competing with stakeholders on the competitive market. Also, full compliance to the unbundling principles should be guaranteed in all relevant areas, to ensure a level playing field and to avoid confusion in the customer interface.

**3.26 1st bullet point**

ACER: *Enhancing transparency through clear and trusted information. Companies should present price information so that consumers can effectively and readily evaluate competing offers between suppliers and other market participants (e.g. aggregators). Offers should easily be comparable (for example, by presenting all costs as a projected unit price).*

We don't see any need or possibility to present customers cost as a projected unit price. There are too many inaccuracies in these calculations. It is impossible to present costs of dynamic, market-based products (e. g. hourly wholesale market price + margin) as a projected unit

price. These kinds of products are even more important in the future to promote demand response and customers' activity. Prices in offers, contracts and bills should be presented as a unit price.

**3.26 2nd bullet point**

ACER: *Regulators will require that suppliers are the main point of contact for each customer with regard to the majority of processes in the retail market (including for switching from one provider to another; and for billing).*

Finnish Energy Industries have for the time being not a common view on the main responsibility for billing, thus we cannot support that the regulators will require that the suppliers are the main point of contact for billing.

**3.26 3rd bullet point**

ACER: *The target we set is that, by 2025, the supplier switching period should fall from its present maximum of three weeks to within 24 hours.*

The difference between the supplier switching process and the data exchange process as a part of the supplier switching process must be understood. We don't see any real customer need nor benefit to shorten the whole supplier switching process to 24 hours. The supplier switching process must respect the notice period, which is 14 days in Finland. The customer (or a new supplier on behalf of a customer) must terminate the present contract at least 14 days in advance. Totally different thing is the data exchange process. It can, depending on the chosen technology, be as short as possible, even minutes if a central supplier switching hub is in use. The shortest possible supplier switching period is two weeks.

**3.26 4th bullet point**

It is very important to ensure customers' rights to all the services within the scope of the consultation. However, we urge caution regarding the methodology of setting such guaranteed service standards at the EU level. First a thorough assessment of how current standards for these services are fulfilled across Europe should be undertaken.

**3.26. 8th bullet point**

We agree that guaranteeing minimum quality standards along with compensation arrangements will protect consumers and help to improve their perception of the energy market. However, we emphasize that in many cases it may be beneficial to develop these standards and arrangements on a national level. At least, EU-level regulation, if preferred, needs to take into account the differences and individual needs of each member state.

**3.27 and 3.28**

We agree that the case for full harmonization of the retail markets isn't as strong as for the wholesale markets. Harmonised detailed rules all over Europe should not be targeted. In order to lower the entry barriers, the main roles and responsibilities should be the same. In areas with relatively small national markets with large similarities, such as in the Nordics, a higher degree of harmonization and integration may be targeted and facilitated, to achieve advantages of scale.

**3.29**

ACER correctly recognizes that cross-sectorial impacts have to be considered in enabling demand response. As an example the sharing of communications infrastructure for smart meters across different sectors is mentioned. And it is correctly noted that in such case data separation and consumer protection need to be taken fully into account. In addition to data protection, also division of costs from data handling needs to be taken into account. The cost should be borne by the originator of costs, not by other customers e.g. via DSO tariffs.

**3.32**

We agree on the principles and would further emphasis the DSOs' role as neutral market facilitator;

- leaving the supplier with the main responsibility for the customer interface (however DSOs may have responsibilities in the customer interface in purely grid related issues),
- not participating in commercial activities on the competitive market,
- ensuring a level playing field for all commercial players.

**3.35**

ACER: *The size of DSOs is of relevance given that many DSOs are at present exempted (in the Third Package) from unbundling (required only when integrated electricity or natural gas undertakings serve more than 100,000 connected customers). Thus, customers connected to small distribution networks may not benefit to the same extent as those connected to larger systems. Indeed, small DSOs often have limited (or zero) interactions with TSOs as they may only be connected to a larger DSO. Regulators will, therefore, consider whether to recommend to the European Commission the possible revision of the current de minimis limit (of 100,000 customers) and whether (and how) to encourage further consolidation of distribution systems.*

We don't see reasoning why customers of smaller DSOs would be in worse position and find it very problematic if ACER would take a position how DSOs in different countries are organised. It may be that requirements and new tasks will lead to development where both large and small DSOs find it useful to cooperate more or to merge. However, it is not a task of an Agency to take a standpoint how many customers a DSOs should have as a minimum.

**3.37**

ACER finds that reductions in energy consumption during peak periods can reduce the need for additional infrastructure investment and thus reduce prices to consumers. ACER also recognizes possible costs and as a solution offers to consider the implications for consumers of time-of-use or locational distribution network tariffs.

The distribution grid cost structure is mostly (over 90 %) based on fixed costs. We believe that a power based network tariff structure would be more suitable for all future needs, both from the network, but also generations and supply perspective.

We believe that the following principles should be taken into consideration when rethinking the current DSOs' tariff structures

- Current energy based network tariff structures is inadequately cost reflective and provides weak incentive for both customers' savings and DSOs' investments.
- The target of the network tariff structure development should be to establish a pricing that encourages the end-users to behave so that the overall efficiency of the energy system, including generation, transmission and distribution, is maximised, and the total costs to the national economy are minimised. This objective would best be met with a flexible enough, power based tariff structure.
- Power based tariff approach meets the targets set for the DSO tariff:
    - Tariff is cost reflective and guarantees a predictable revenue stream for DSOs also in the changing operational framework.
    - Power based tariffs, together with the energy based supply pricing, provide customers with incentives to optimize their consumption and their own production while contributing to the efficiency of the whole energy system.
    - It encourages customers to participate in demand response activities.
    - Power based pricing is a cause-fair tariff system for customers.
    - It meets the demands of the Energy Efficiency Directive (2012/27/EU).

**Summary of possible regulatory actions**

ACER: *We will undertake further analysis to develop and improve the common European balancing target model defined in the Network Code.*

We support network codes as a means to develop European energy markets. We however like to emphasize the importance of giving DSOs a clear role in the drafting process. We also emphasize that sufficient Cost-Benefit Analysis is performed before new legislation is introduced. These analysis need to take into account the whole electricity market chain (incl. retail market level) and all market actors. Finally we emphasise that regulation must respect the liberalisation of energy markets and competition in the

electricity market. Different actors are offering different product structures that suite different customers' groups. Regulation must not hinder this product development, but shall ensure level playing field and the sufficient basis for companies serving customers. Among other things these include smart metering, freedom to change supplier and the end of price regulation.

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