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Agency for the Cooperation of Energy Regulators

Publishing date: 22/09/2014

Document title:

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20 -06- 2014/358

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11 June 2014

Reply to ACER Consultation: "European Energy Regulation: A Bridge to 2025"

Dear Sir or Madam,

Rheinische NETZGesellschaft mbH is a distribution system operator for the Rhine region. It takes responsibility for more than 18.000 km length electricity grid with more than 1 million metering points and about 8.000 km length gas grid with nearly 300.000 metering points. Some 2 million residents are connected at our electricity and gas grid.

We would like to comment on ACER's public consultation paper "European Energy Regulation: A Bridge to 2025". As regards our role in the German market we would like to comment especially on DSO, Consumers, retail, and wholesale issues.

As a stakeholder, we very much appreciate the invitation to participate in the discussion on the medium and long-term framework for the advancement of the internal energy market. To our view, this advancement has to be assessed by means of competition and market as main criteria. Regulation has to provide the market with an appropriate framework. It has to promote competition and prevent restrictive business practices.

Given the fact of an increasing integration of the internal market whilst national policy instruments persist, a well-balanced set of policy instruments is and will be needed in order to achieve a continued secure, sustainable and affordable supply with electricity and gas for Europe's customers and industries. However, in short term the top priority must remain the timely and full implementation of existing legislation, in particular the 3rd energy package. With regard to the degree of unbundling, it is highly questionable if there is a remaining threat of market distortion or discrimination on the DSO level. And, secondly, it is questionable, if customer change rates are appropriate to validate competition - especially given the simple fact of a possible choice from dozens of retailers with hundreds of different tariffs everywhere in Germany.

Key messages

- We consider market-based approaches to be the first and key choice to tackle future challenges. Market based approaches are best to support any further integration of the European electricity and gas markets. Markets based instruments shall be general rule, regulation shall be restricted to substantively justified cases - e.g. overcoming market failure in fields relevant for security of supply.

- The unbundling requirements of the 3rd Energy Package are sufficient to ensure non-discriminatory network access and market functioning on wholesale and retail level - at least if they are implemented properly. Prior to setting new policy rules, the implementation of the 3rd Package's network codes for electricity and gas has to be realized.

- DSOs in Germany today facilitate market-operations and provide a level playing field in a non-discriminatory way for all market parties. Binding rules are guiding such processes as billing, switching, communication between market actors etc. DSOs will continue to assume these tasks in a "smarter world" in the future. There is no need to mix the tasks of DSOs with the ownership model.

- Demand response services are key to future market-development. DSOs can (and should) use them to do their job, e.g. tackling grid constraints. Similarly market participants will be able to carry out demand response services in order to bring benefits to the customers. The relevant system state will be indicated by so called "traffic light concept" which is promoted by BDEW, the German Energy Association.

- We see a strong need to provide clear common national market rules (data exchange processes/data formats, content and connected time frames). These rules should be mandatory for all market participants, as this will foster the market. At least for the timeframe covered by this consultation we do not see any necessity for a European wide harmonization of data processes and data formats.

- Customer data protection and privacy is key and shall be in line with the European data protection law. Additional national technical rules e.g. for minimum cryptographic standards are useful.

- Customers' satisfaction depends on price and quality of products. Dissatisfaction with prices not the least comes from political decisions (taxes, subsidies) not from a lack of regulation.

- A general shift from volumetric (kWh) towards more capacity based (kW) network tariffs could be beneficial for the electricity sector, since network costs are primarily determined by the electric capacity (kW). Yet, any change in this field has to be based on a profound impact analysis with regard to the different grid users.

- The construction of incentive mechanisms for grid operators should consider the heterogeneity of grid structures. The tasks of the relevant grid operators and their dynamics, e.g. resulting from the development of political targets, shall be reflected adequately in the regulatory system.

A. Electricity Wholesale Markets

We appreciate ACER's analysis of the ongoing transformation and the future challenges of the electricity wholesale market. The markets become pan-European whilst the generation portfolio becomes greener, smaller and more decentralized. Wholesale Markets therefore have to overarch an otherwise diffusing system. The integration of energy markets towards a pan-European market is crucial for competition and hence welfare. To achieve this integration, the implementation of network codes is of major importance. Market-based approaches should be the first choice to tackle future challenges. Our priorities are as follows:

- integration of renewable energy sources (RES) into the market;
- balance responsibility by all parties;
- further development of balancing markets;
- further development of intraday markets.

RES will assume a central if not leading role in future wholesale markets. The integration of RES, especially of intermittent production from wind and pv, into the electricity system requires not only sufficient grid capacities, but also well-functioning wholesale markets. As for intraday markets, continuous trading has to be implemented in all member states and gate closer times close to real time shall be introduced.

Regulatory interventions (only) when necessary
If the instruments mentioned above, however, are not (yet) completely implemented or more are needed, transition processes have to be carried out cautiously. Obviously, balancing energy is very important for system security and, consequently, for security of supply. This is why participants in these markets have to comply with high technical requirements.

Even if some existing regulatory interventions are legitimate and may persist, any new instrument shall be introduced only after careful examination of its necessity. ACER is right when saying that every step towards developing capacity remuneration mechanisms (CRMs) needs to be clearly justified and carefully evaluated. Providing the system with security of supply can (and should be) accomplished with market-based instruments - ideally adaptable with cross border mechanisms.

Allowing national competence for non-market issues
The electricity target model, as cited by ACER in section 3.2, can be understood as the combination of the nine network codes which are currently developed or have already been finalised. In addition to the codes on market design, technical issues concerning grid connection as well as operational questions are covered by the codes on grid connection and system operation, respectively. In these fields, there's often need for regionally specific solutions rather than a "one-size-fits-all" approach. Thus, the subsidiarity principle shall be applied where necessary. Besides, the sphere of competence of other institutions shall be respected. This applies above all to technical issues which should be treated in detail by standardisation organisations rather than in the network codes. Taking into account the long lasting network code amendment process, the codes may not be flexible enough to be reviewed if required by technological progress or organisational changes.

B. Gas Wholesale Markets

Just as for the electricity wholesale markets, we widely agree with the analysis of the current situation and the future challenges in gas wholesale markets.

Achieving a liquid pan-European gas market
ACER correctly describes that implementing the network codes will be a decisive to establish the single gas market.

We also agree with the assessment that further integration of markets can contribute to liquidity which will presumably encourage entry, leading to more competition and further improvements in liquidity. Yet, before integrating market zones the possible impacts have to be analysed, above all on the firm capacity which is available in the integrated market. This is why BDEW and Rheinische NETZGesellschaft support to consider possible changes in market zone

configurations on a case-by-case basis. The integration of market zones as well as the merger of zones should be market-driven rather than decided by authorities. The current Gas Regional Initiative (GRI) projects are the best examples for such market driven decisions. Hence we promote a market wide discussion if an integration or merger is proposed. The process (not the decision) should be attended by the NRAs.

Implicit auctions should only be considered if all other congestion management procedures proposed and fully implemented by the network codes are failing.

Uncertain gas supply and demand
As to the analysis of trends we agree that infrastructure to meet any future peak demand will still need to be in place. This might be the case for future evolvement of the role of gas fired power plants as well as gas storages. We also see that increasing grid charges as a result of declining demand or booking short term capacity are a problem and may lead towards a reduced attractiveness of gas.

Concerning the regulatory impacts resulting from uncertain gas supply and demand, ACER correctly depicts that finding the adequate level of investment in infrastructure is the key challenge for market actors, network operators and regulators. Again we would like to highlight that any market intervention should be carefully investigated. First of all the implementation of the 3rd energy package and of the FGs and NCs have to be accomplished in the whole of Europe. This should be the first and mainly goal and should also be pushed by ACER and the European Commission. After an appropriate implementation period and market settlement to these rules there should be a discussion or evaluation if any (further) market intervention is needed.

C. Infrastructure investment

We widely agree with ACER's position that investment in energy infrastructure has to be driven by market signals and needs supranational coordination, also among the regulatory authorities. We share the view that focus has to be given to economic benefit of investments regardless of their cross-border or national character.
The need of infrastructure investments however is not limited to the Transmission Systems. In fact most investments in the electricity sector are needed in distribution grids during the next decade. This is due to a fundamental change in the way grids are used given the fact that the RES are mainly entering the system via distribution grids.

Long term stability of the regulatory framework is crucial to investments in energy infrastructure. A multitude of short term and or unexpected changes can lead to uncertainty amongst investors. This will result in an increase in the cost of financing or even prevent investments from being realised.
Regulatory framework has to be designed in a way that allows investors to achieve a sufficient return on investment in order to be able to finance long term infrastructure investments.

D. Consumers, retail markets and the role of DSOs

ACER puts the consumers into the focus of its consideration. Many of the instruments proposed strive to empower consumers so that they can assume a more active role in tomorrow's energy markets. The analysis on consumer concerns ACER gives should yet be complemented by some clarification on what has already been achieved. For example, switching suppliers in Germany is easily possible for customers due to standardised market processes and data formats (see below "data exchange processes and data formats for a functioning retail market").

Concerning the access to retail markets, we support ACER's position to identify and remove barriers to the entry of suppliers in other national retail markets. Yet ACER is right when saying that an integrated European cross-border retail market is still an ambitious target. As a first step we would advise to fully implement the 3rd Energy Package's rules and to assure non-discriminatory market access for suppliers within any member state.

The empowerment of customers, a more integrated retail market as well as the implementation of demand response services may be challenging to DSOs. Yet there will be no major shift in DSO tasks. They will remain the market facilitator and guarantee neutrality and non-discrimination with regard to market participants.

Data access and data protection
Concerning consumer data, one of the challenges for regulators will be to find a sound balance between data privacy and security on the one hand and transparency and non-discriminatory data access for legitimated third parties on the other. Access to consumer data shall be granted depending on the purpose the data are used for. Concerning the access to consumer data, different approaches shall be applied depending on the addressee and the purpose of the respective data:

DSOs shall be provided with access to meter data which are necessary to fulfill regulatory duties and/or duties authorized by law without explicit consumer consent, e.g. meter data needed for balancing settlement, monitoring the state of the network and system operation, grid usage billing, historical consumption (according to the EU Energy Efficiency Directive) as well as the reading out and passing on of meter data to suppliers in case of electricity tariffs laid down in national legislation (e.g. basic tariff with annual billing on the basis of an annual metering value for household customers).

- Energy suppliers should be granted access to data which are necessary for their basic task of delivering energy.

- Meter data needed for purposes other than regulated duties or the delivery of energy should be due to consumer consent. If the customer orders specific services which go beyond the sole energy supply, he has to legitimate the relevant party, on the basis of a contract, to have access to the data needed for this service.

Removing barriers to retail markets: Data exchange processes and data formats are the key

We support ACER's view that retail markets have to be opened to a large number of competitors in order to achieve best results for consumers. Yet the instruments providing a high level of competition in retail markets already exist. The exchange of data plays an important role for the implementation of market processes (such as supplier switching). Based on the provisions of the 3rd Energy Package, data exchange processes and standardised data formats have been developed in many member states, allowing for non-discriminatory access for all competitors in the respective retail markets.

In Germany, the NRA (Bundesnetzagentur) has put national ordinances in place that are mandatory for all market participants (TSOs/DSOs, suppliers, balancing group coordinators, metering companies, ...) which lay down clear electronic data exchange processes and responsibilities, standardisation of data being concerned (basically all data for all market processes like supply, metering, supplier switching etc.), data formats (applicable to all market participants), timeframes for reading out meters (applicable for DSOs / 3rd party metering companies), timeframes for performing plausibility checks and passing on of meter data to suppliers (DSOs' responsibility). This system has proven to be successful, since the DSOs make sure that only high quality meter data is being passed on to the market parties which avoids costly settlement procedures.

As a result of the detailed provisions for data exchange processes and data formats in Germany, the German retail markets are characterised by the highest number of suppliers in Europe, showing a high level of competition intensity. In every region and every network area, consumers can choose among a large number of suppliers and products.

This example shows that the full implementation of the 3rd Energy Package's rules already guarantees strong benefits for the consumers. Therefore, before developing new provisions for the retail market level, the European authorities should focus on the full implementation of the 3rd Energy Package's rules. Currently, there is no need for regulatory measures concerning supplier switching rules which go beyond today's rules. If the development of technical facilities enables shorter switching periods in the future, regulators should leave it up to the market to develop products incorporating different switching periods.

Enabling demand response

ACER correctly states that demand response services will become more important, above all in the electricity sector due to the increasing share of NP RES. Enabling demand response requires not only the implementation of appropriate technologies but also clear-cut rules on the communication between the actors involved and their respective responsibilities. We appreciate that ACER pronounces these considerations.

ACER correctly depicts that innovative technological solutions are one base for the active participation of consumers in energy market. Smart appliances and/or smart energy management systems could help shift consumption to low price periods or to network off-peak times according to user preferences. Energy management systems can, in addition, factor in parameters like weather conditions and light intensity. Home automation systems thus can help reduce energy costs for consumers. But saving costs via these instruments is not a given as such. It always depends on the costs of the necessary technical installation, which have to be compared with the possible savings potential. The largest effect can be reached via the continuous use of energy management systems for the optimisation of processes of commercial and industrial customers.

From our point of view, the delivery of demand response services should be organised in a free market. DSOs will assume a crucial role: on the one hand, they enable demand response by managing data on system states, energy demand and energy generation of the different actors

and forwarding the data to legitimated actors. On the other hand, DSOs can make use of demand response services in order to tackle grid constraints. In the absence of grid constraints, market participants will be allowed to carry out demand response services in order to bring benefits to the customers.

The relevant system state will be indicated by the so called "traffic light concept" which was worked out be BDEW. This concept describes in an integrated way how to organise the interaction between DSOs and different types of grid users (consumers and producers), depending on the actual status of the energy system.

A smart energy system with different active market participants requires intelligent solutions for the balancing of accounts of energy quantities. Every actor has to be responsible for imbalances in balancing accounts which derive from his activities. With new players entering the market, the design of balancing accounts responsibilities has to be adapted.

Roles and responsibilities of DSOs
We are in line with ACER that, apart from grid management and distribution, the DSOs will continue to assume the role of a neutral market facilitator. The tasks allocated to the DSOs comprise

- facilitating the market by provisioning validated trustworthy data to all market participants in an neutral, efficient and non-discriminatory way,
- taking care of efficient and reliable supplier switching processes,
- allowing network access and connection in a non-discriminatory and transparent way and
- taking care of security of supply and quality of service.

Tasks which, under the consideration of system stability and security of supply, can be part of the competitive market should be allocated to the non-regulated area. Compared to today's situation, the tasks and responsibilities of DSOs will not change substantially (no "revolution") but rather evolve, following technological changes (e.g. in the field of metering). Neutrality and non-discrimination with regard to market participants will remain the basic principles for the DSOs' work.

In the context of the DSOs' tasks, ACER states that DSOs should not be able to use advance access to data to gain commercial advantage. To us, this argumentation is not comprehensible: it is the basic characteristic of the role of the DSOs that they do not act in areas where they compete with other players.

On the contrary, as market facilitators, DSOs do perform the above mentioned tasks – and these are as a basic principle **not** performed by market participants. Consequently DSOs cannot gain commercial advantage over others, be it from advance access to consumer data or from other information which they may gain when performing their particular tasks.

Unbundling of DSOs

ACER links the discussion of the roles and responsibilities of the DSOs with the question of the level of unbundling requirements and in the end with the legal form of the DSO companies. From our point of view, linking these aspects is inappropriate. The basic perception of all Energy Packages, beginning in 1996, was to prevent distortion of competition and give grid access in a non-discriminatory manner.

According to the rules established under the 3rd Energy Package, DSOs are obliged to apply informational unbundling. If fully implemented and enforced, these requirements are sufficient to guarantee that DSOs act neutrally and fulfil their tasks in a non-discriminatory manner. In Germany, the legislation has been adapted accordingly in § 6a of the German Energy Act (EnWG). Every DSO has to fulfil the requirements on informational unbundling.

ACER argues that stronger unbundling would seem necessary when DSOs assume more tasks. We do not share this view; a full implementation and enforcement of the existing unbundling rules, combined with effective data exchange processes adopted with regard to all market participants, is sufficient to ensure that DSOs assume their tasks in a non-discriminatory manner.

ACER also announces further analysis on whether the services currently provided by DSOs could be better provided within competitive markets. We agree that metering services can be offered by third parties; the German Energy Industry Act provides this option. By contrast, it is not effective or even not possible to assign data handling to entities other than the DSOs for the following reasons:

- Firstly, as described above, data protection is an important matter, especially with regard to consumer data. A well regulated DSO is the best suitable player to manage this data and ensure that access is only permitted to authorised parties.

- Secondly, data on energy demand and on production are one essential basis for the information on the system state. The DSO needs this information in order to be able to efficiently operate the network. Thus, even if a third party was responsible for data handling, the relevant information would have to be passed on to the DSO.

- Thirdly, in case of a third party being responsible for data handling, regulatory measures would be necessary to ensure data protection and non-discriminatory data access; as one feature of this construction, the third party would not be allowed to assume tasks in competitive market areas. Thus, the third party would have to be regulated just like the DSO. To our mind this would double regulation and promoting completion on the energy market.

- Fourthly, even if a larger entity responsible for data handling would be able to generate economies of scale, the network-specific data would still be needed for the single DSO to operate its network. Moreover, larger entities for data handling would be more prone to possible attacks. Thus, a decentralised approach for data handling in the responsibility of the DSOs is the preferable way.

ACER also states (3.35) that many DSOs at present are exempt from unbundling. This is not correct. According to Article 27 of Directives 2009/72/EC (Electricity) and 2009/73/EC (Gas), all DSOs - regardless of their size - have to respect the confidentiality obligations.

Since the assumption is not valid, the conclusion saying that customers connected to small distribution networks may not benefit to the same extent as those connected to larger systems is neither. Also the argument that small DSOs often have limited (or zero) interactions with TSOs is not convincing.

There is no evidence that the size of DSOs conflicts with chances to benefit from the possibilities of the energy markets and to participate as active grid users. Consequently there is no need to amend the existing de minimis rules or the threshold of 100,000 connected customers.

Network tariffs

ACER proposes to consider time-of-use pricing or locational distribution network tariffs. We would like to point out that a general shift from volumetric (kWh) towards more capacity based (kW) network tariffs could be an adequate measure in many parts of the electricity and gas networks, since most network costs are determined by the electric capacity (kW). Besides,

technological developments (e.g. micro-grids, section) and changing consumer behaviour are likely to lead to decreasing energy volumes taken from the network. Thus, on the basis of today's widely volumetric based network tariff systems, revenues for network operators would decrease which would hamper their potential to operate the network and carry out necessary investments. As a consequence, more capacity based network tariffs could be an option for tomorrow's energy networks.

When designing a future network tariff system however, it should be considered whether incentives could be set for actions of "smart consumers" which benefit from the grid. Yet, any change in the network tariff system has to be based on a sound analysis of the impacts on different grid users.

Incentive mechanisms for grid operation

Due to differences in grid structures (e.g. population density, topology), the tasks of grid operators differ both within one member state and between different countries, and so do the expenses for grid operation. Regardless of the regulatory system applied, the incentive mechanisms shall enable the DSO to gain revenues which cover the necessarily occurring costs and to carry out necessary investments.

In the case of an output-oriented incentive regulation, the "outputs" (output parameters indicating the productivity of the DSO) shall be chosen such that they reflect the tasks of the DSO with their cost drivers in a way that expected and real financial remuneration enable the DSO to cover all costs of capital including risks, and give an incentive to carry out the tasks. Since grid structures differ among DSOs, one set of "outputs" may not be applicable to all DSOs. Besides, the DSO tasks may change over time, reflecting changing political goals (e.g. connection of distributed generation units or preparation of smart grids). With these cost drivers varying over time, the "outputs" which shall reflect the costs have to be adapted as well.

Summing up, incentive mechanisms should set a frame which is flexible enough to reflect the costs resulting from existing structures and DSO tasks as well as from changes in the tasks, e.g. due to changing political goals. We doubt whether a strictly output-oriented regulatory system can reflect all cost drivers occurring within DSOs. There are situations when "outputs" alone are not able to reflect DSO costs and to set the right incentive for necessary investments. Therefore, it could be necessary to add input-oriented instruments such as budgets for specific investment projects or adders on top of interest rates that should incentivize technologies of comprehensive economic relevance.

Implications for governance
It is quite clear that regional solutions can be helpful in early stages of integrative measures such as market coupling. The dissemination of best practice examples concerning governance issues may help to avoid lengthy negotiations in similar cases.

We agree that the responsibilities of the ENTSOs should prevail over the specific interests of their specific members. However we do not see the need for regulatory oversight by ACER of these organisations. If any oversight is needed then the European Commission should assume this responsibility.

From our point of view any regulatory oversight or governance arrangements for new market entities could lead towards market hampering. The development of new market roles or market entities should be possible without any barriers. The implementation of the Target Models in electricity and gas should be subject to a regular process in which ACER and the NRAs play an important role.

But not all market facilitators should be subject to a regulatory oversight in general. Especially, power and gas trading exchanges are already subject to a regulatory oversight by a financial regulator by means of their financial character; this should be sufficient. However, if the market facilitator works for a regulated party - such as market area operators in the German gas market - it seems appropriate that the NRAs will have the regulatory oversight of the costs incurred by these bodies.

The proposed general governance arrangements for all relevant market actors which are assigned responsibilities in the Single Energy Market, such as network operators, EU bodies like ENTSO-E, ENTSOG, power and gas trading exchanges, common service providers (such as Customer Advisory Committee (CAO) and Prisma) and other future institutions remain unclear to Rheinische NETZGesellschaft. Companies related to RSCIs may need this governance arrangement but a general regulation of all relevant market actors cannot be supported.

We would prefer a market wide discussion about any further governance arrangements. Additionally, we would like to argue that market actors which do not have defined responsibility in a regulated context but have to bear the consequences of decisions taken, such as generators, DSOs, traders and retailers, should have a proper role in the governance process.

RNG Rheinische NETZGesellschaft

As to ACER's role in an expanding market we think that it is reasonable to share the knowledge among NRAs within the EU borders and beyond. However, this is a mainly political issue and should be discussed and decided upon by the relevant EU bodies (especially by the European Commission).

Yours faithfully,

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ACER

Agency for the Cooperation of Energy Regulators

Publishing date: 22/09/2014

Document title:

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