



Ministry of Petroleum and Energy

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## **Reply to public hearing – Proposal for a Regulation of the European Parliament and of the Council on Energy market integrity and transparency (“REMIT”) - (COM (2010) 726 final)**

The Norwegian Competition Authority (the “NCA”) refers to the letter from the Ministry of Petroleum and Energy asking for eventual comments about the “Proposal for a Regulation of the European Parliament and of the Council on Energy market integrity and transparency” (the “REMIT Proposal”) announced by the European Commission on 8 December 2010.

Since the reply to the public hearing could be used in an EU context, the NCA provides it in English.

### **The REMIT Proposal**

The REMIT Proposal aims at guaranteeing market integrity and transparency in the wholesale energy markets<sup>1</sup>.

The integrity and transparency of energy markets have a crucial importance for the functioning of such markets, as they can guarantee public trust and confidence, fostering investments and liquidity. Wholesale energy markets have an increasingly cross-border nature in terms of where trading takes place and where production and consumption takes place. Thus, price setting is not tied to a particular market as prices are set based on supply and demand in several countries. As a consequence, EU wide coordination is needed to effectively detect and deter market abuse.

Wholesale energy markets include both physical and financial products. The peculiarity of the wholesale energy markets leads to important regulatory challenges when it comes to ensuring market integrity.

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<sup>1</sup> The REMIT Proposal (Article 2(4)) defines wholesale energy products as:

- (a) contracts for the supply of natural gas or electricity;
- (b) derivatives relating to natural gas or electricity;
- (c) contracts relating to the transportation of natural gas or electricity;
- (d) derivatives relating to the transportation of natural gas or electricity irrespective of where and how they are traded.

On the one hand, the Markets in Financial Instruments Directive (“MiFID”, 2004/39/EC) only applies to investment companies and regulated markets for financial instruments; hence, it does not apply to physical energy markets. However, energy derivatives traded on a regulated market are covered by MiFID. On the other hand, the Market Abuse Directive (“MAD”, 2003/6/EC) – whose scope is prevention, detection, investigation and sanctioning of insider trading and market manipulation – covers only partially the wholesale energy markets (the estimate provided in the Impact Assessment accompanying the REMIT Proposal is that only 16% of the total volumes traded in 2006 was covered by MAD) as it is designed for financial markets.

The REMIT Proposal addresses the potential for unfair trading practices defining rules that are consistent at the European level and adapted to the specifics of energy markets.

In particular, the REMIT Proposal grounds on four main pillars. Firstly, it defines abusive practices in wholesale energy markets, namely insider trading and market manipulation. Secondly, the REMIT Proposal prescribes an obligation for market participants to report details (not yet defined in the proposal itself) about their transactions in the wholesale energy markets to the Agency for the Cooperation of Energy Regulators (“ACER”). Moreover, it assigns monitoring powers over the wholesale energy markets to ACER and to the National Energy Regulators. Finally, the REMIT Proposal prescribes that National Energy Regulators have investigatory powers over the wholesale energy markets.

### **Comments from the NCA on the REMIT Proposal**

The NCA welcomes the REMIT Proposal, acknowledging the importance of integrity and transparency in wholesale energy markets for the functioning of such markets. The NCA would however like to comment on some aspects of the proposal.

#### ***Definition of abusive market behavior***

The REMIT Proposal defines two categories of abusive market behavior: insider trading (art. 3) and market manipulation (defined under art. 2 (2) and prohibited under art. 4). These two categories reproduce the two forms of abusive practices described in the MAD directive for financial products (art. 1 (2)) and they address the possible abuses in the *financial markets*.

However, these two categories of abusive behavior do not cover all potential abusive market behavior in the *physical markets* as the REMIT Proposal seems intended to do. In particular, the REMIT Proposal does not include abuse of dominant position as one of the possible market misconducts; however, the Impact Assessment accompanying the REMIT Proposal explicitly states that

*“The rules need to effectively capture energy specific market misconducts, such as: trading on insider information, withholding of energy production facilities from the market and distortion of prices”<sup>2</sup>*

Thus, on the one hand, the Impact Assessment refers explicitly to an example of abusive market behavior in the physical market, namely the *“withholding of energy production facilities”* as an energy specific type of market misconduct. On the other hand, the definitions of abusive market behavior in the REMIT Proposal do not cover abusive market behavior in the physical markets. The definition of market manipulation under art. 2 (2) calls for *“entering into transactions or the issuing of orders to trade in wholesale energy products”*. However, capacity withholding may occur without any transaction being made or an order to trade being issued.

<sup>2</sup> European Commission, “Impact Assessment – Accompanying document to the Proposal for a Regulation of the European Parliament and of the Council on Energy market integrity and transparency” (SEC(2010) 1510 final), page 20.

The absence of a dominance threshold requirement in the definition of abusive market behavior would be in contrast to art. 102 TFEU (and art. 54 EEA and § 11 of the Norwegian Competition Act).

However, the NCA recognizes that art. 1 of the REMIT Proposal states that “[t]his Regulation is without prejudice to Directive 2003/6/EC and 2004/39/EC as well as to the application of the provisions of European competition law to the practices covered by this Regulation.”

### *Allocation of monitoring and investigatory powers*

As anticipated above, the REMIT Proposal provides ACER with monitoring power on the European wholesale energy markets (art. 6 (1)). At a national level, the proposal prescribes that the monitoring powers (art. 6 (2)) and the investigatory powers (art. 10) on the wholesale energy markets have to be assigned to the National Energy Regulators. This could imply a change in the current allocation of monitoring and investigatory powers at a national level.

Currently the Nordpool area is characterized by a sharp separation between the financial and the physical side of the wholesale energy markets, which are traded in two different market places: Nasdaq OMX Commodities (the former Nordpool ASA) and Nordpool Spot, respectively. This market setup allows a clear separation of the powers related to the monitoring and investigation over the two markets.

### *Jurisdiction in financial markets*

In Norway in particular, the Financial Supervisory Authority of Norway has the power to monitor and investigate in the financial markets (including the markets for the derivatives relating to energy products and for the derivatives relating to the transportation of energy products). The implementation of art. 6 (2) and art. 10 of the REMIT Proposal would then imply that monitoring and investigatory powers would be given to the Norwegian Water Resources and Energy Directorate (NVE).

### *Jurisdiction in physical markets*

The Norwegian physical wholesale electricity markets are currently jointly monitored by NVE and the NCA.

The report “Capacity for Competition” issued by the Nordic Competition Authorities, summarizes the procedure adopted for the joint market monitoring by the NVE and the NCA:

*“In 2003/2004 the Norwegian Competition Authority and the Norwegian Water Resources and Energy Directorate (the NVE) financed the development of a model for monitoring prices and strategic behaviour in the electricity market. A surveillance group with members from both authorities has been set up, and has used the model to monitor the market since the spring of 2004.*

*[...]*

*Every other month the members in the surveillance group meet to discuss the general situation in the electricity market. [...] If the group finds reason to believe that the observed price deviations indicate abuse of market power, it will recommend that the Norwegian Competition Authority opens an investigation”<sup>3,4</sup>*

An investigation would be made by the NCA under § 11 of the Norwegian Competition Act. If an abuse of dominant position is found, the NCA has the power to fine the companies in breach of § 11.

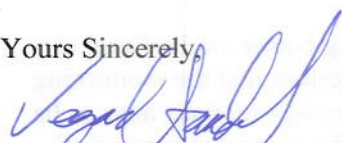
<sup>3</sup> Nordic Competition Authorities (2007), “Capacity for Competition”, Report No. 1/2007, page 25.

<sup>4</sup> The implementation of the joint monitoring solution was explicitly required by the Ministry of Government Administration, Reform and Church Affairs on 14.10.2002, in the decision on Statkraft’s acquisition of shares in Agder Energi.

As anticipated above, art. 6 (2) and art. 10 of the REMIT Proposal prescribe the allocation of both monitoring and investigatory powers in the wholesale energy markets to the NVE. The implication of this is that the current monitoring and investigatory procedures in cases of abusive practices might need to be revised.

The NCA has no further comments on the REMIT Proposal.

Yours Sincerely,



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