



NordREG
Nordic Energy Regulators

NordREG Activities 2007



NordREG Activities 2007

NordREG
c/o Energy Market Authority
Lintulahdenkatu 10
FI-00500 Helsinki
Telephone: + 358 10 60 5000
Telefax: + 358 9 622 1911
E-mail: virasto@energiamarkkinavirasto.fi
Internet: www.nordicenergyregulators.org

12 March 2008

Preface

Since 1 July 2007 all electricity customers of the EU have enjoyed the right of free choice of supplier. In September the European Commission launched its “3rd energy liberalization package”. Both events are major milestones in the process of establishing one integrated European electricity market based on genuine competition in generation and supply.

The Nordic countries still are in the forefront of this liberalization and integration process. The NordREG cooperation between energy regulatory authorities of the Nordic countries has a specific responsibility to actively contribute to improve even more the Nordic electricity market integration. 2007 has been an active year in this respect. Through analysis, publications and dialogues with stakeholders additional steps were taken towards the fulfilment of NordREG’s strategic priorities. A number of analytical tasks dealt with were initiated by Nordic Council of Ministers. The NordREG responses to these requests constitute an important element in these achievements.

NordREG through 2007 in addition to inter Nordic relations and issues increasingly has focussed on the interaction and integration with the electricity markets of continental Europe. The members of NordREG have actively engaged in the CEER and ERGEG work acknowledging that development and integration of continental markets will be of major importance both for security of supply and for price and quality of service in the Nordic countries.

This annual report outlines the strategic priorities of NordREG and what was achieved during 2007 in relation to these priorities. It also describes some aspects of NordREG members’ contributions on a European level.

Finn Dehlbæk
Danish Energy Regulator
Chairman of NordREG 2007

NordREG strategic priorities and achievements

In autumn 2004 NordREG formulated the following strategic priorities:

- A truly common Nordic retail market with free choice of supplier
- A well-functioning Nordic wholesale market with competitive prices
- Reliable supply
- Efficient regulation of TSOs

These priorities coupled with more specific objectives have been the framework for NordREG cooperation since then. The 2007 Work Programme (NordREG Report 1/2007) and work were structured according to these priorities. In NordREG's opinion the work contributed in a reasonable manner to the progress towards the goals. Not all tasks planned were accomplished within 2007, but they are all on track and will be finalized during the first months of 2008.

The Nordic electricity market is quite well developed compared to other European markets of a regional character. There is, however, no ground for complacency. While the wholesale market is well integrated there are still unnecessary barriers to trade. The trading interface with continental Europe is still subject to a number of constraints, though improvements are under way e.g. within the framework of the ERGEG Regional Initiative. The Nordic retail markets are still to a high degree separate markets.

NordREG work through 2007 repeatedly revealed that some of the imperfections are due to lack of harmonized framework conditions. Harmonization has a number of levels. Regulatory authorities might mutually decide on regulatory harmonization within the frameworks of national legislations. If change in legislation itself is needed, national governments and parliaments normally will have the responsibility. Therefore NordREG pays the utmost attention to the cooperation with Nordic Council of Ministers. A number of 2007 NordREG tasks were actually initiated by the Nordic ministers of energy meeting in Bodø in September 2006. The ministers' meeting in Helsinki in September 2007 welcomed the contributions of NordREG and asked for additional contributions before spring 2008 on a couple of issues within NordREG's strategic priorities.

Cooperation is also essential for NordREG in relation to other stakeholders. The Nordic TSOs represented in Nordel as well as Nord Pool Spot are the operational "doers" on several crucial issues as congestion management, balancing and security of supply. And the participants in the market are the users of the services offered, the generators, traders and suppliers being represented especially by the Nordic energy associations represented in Nordenergi.

A truly common Nordic retail market with free choice of supplier

This strategic priority during 2007 was addressed by the interrelated working issues of "A common Nordic platform for balancing services" and "market design of the Nordic retail market". Harmonized balancing rules are an important precondition for integrating retail markets. NordREG evaluated the February 2007 Nordel agreement on balancing, which was found to constitute an appropriate basis for a comprehensive Nordic balancing system. However the final view will be

reserved until more operational details are drafted. NordREG especially focuses on the costs of the system, on the incentives to make more market participants become balance responsible and in general on the ability of the system to promote competition.

A qualitative cost benefit analysis of introducing an integrated Nordic retail market indicates that benefits will most likely outweigh costs with a clear margin. The additional work on drafting a harmonized supplier switching model and addressing the functional separation of monopoly network activities as major elements in outlining a proposal for a harmonized market design progressed well during 2007 and will be finalized in the beginning of 2008.

A well-functioning Nordic wholesale market with competitive prices

The basic status of the functioning of the Nordic wholesale market is given in the 2007 version of “Nordic market Report”, which was published in June 2007. The review relates to the year 2006. The year witnessed an efficient response in the market to the shift from a dry and warm summer to an autumn with high levels of precipitation. More than 60 per cent of electricity consumption was traded on Nord Pool Spot compared to around 45 per cent in 2005 and around 10 per cent back in 1997.

Nord Pool Spot, thus, is the most important vehicle for a well-functioning Nordic wholesale market. In order to reflect the Nordic aspect of a power exchange formally governed by the Norwegian legislation, the Norwegian regulatory authority in 2002 made guidelines for the cooperation of Nordic national regulatory authorities in relation to the regulation of Nord Pool Spot. During 2007 NordREG carried out reflections on how this cooperative monitoring and regulation can be further developed.

The Nordic cooperation in the regulation power market is another important aspect of both a well functioning wholesale market and an appropriate level of security of supply. NordREG reviewed the functioning of this cooperation with a joint “bidding ladder” – all contacts to suppliers of regulation power (manually activated reserves) remaining with the national TSOs. The system obviously reaping a large share of potential benefits of Nordic cooperation on this issue, however, might benefit from increased harmonisation. NordREG calls for increased transparency of the system and will address more in detail the need for cooperation on monitoring.

Reliable supply

The roles of the national regulatory authorities of the Nordic countries in relation to security of supply issues are very different. Other public authorities, too, have important responsibilities and in certain cases the responsibilities assigned to regulatory authorities are minor. During 2007 NordREG has been carrying out a review of the roles and responsibilities as well as of the legislation relevant to the issue. Based on this a NordREG report on cooperation between Nordic regulatory authorities and other competent authorities will be finalized at the beginning of 2008.

Efficient regulation of TSOs

TSOs play a crucial role in the efficient operation of the market, especially the wholesale market. Therefore the strategic priorities of “efficient regulation of TSOs” and of “a well-functioning Nordic wholesale market with competitive prices” are closely linked.

A 2007 NordREG work described the regulation of TSOs in each Nordic country and concluded that the regulators’ roles and powers as well vis-à-vis the TSOs as in general are significantly different. Harmonisation may lead to more efficient functioning of the Nordic market. A review among stakeholders on their view on the TSOs’ handling of tasks revealed a number of issues which, however, are already addressed by NordREG or Nordel.

A NordREG analysis initiated in 2006 and finalized in beginning of 2007 reviews the use of market splitting, counter trade and reduction of interconnector capacity as congestion management tools in the Nordic countries. It calls for explicitly taking competition issues into account in the regulation of TSO activities together with harmonization of roles of Nordic regulatory authorities in accordance with the above mentioned study. The analysis stresses the importance of appropriate implementation of the new EU Congestion Management Guidelines. In accordance with the efforts of the ERGEG Regional Initiative of North Europe it stresses the need to take into account the interface with continental Europe.

The implementation of the EU Congestion Management Guidelines was more specifically addressed in a follow-up study during 2007. This is intended to become the first of regular compliance monitoring exercise with the Congestion Management Guidelines. While the implicit auctions of the Nordic countries fully comply with the Guidelines more transparency in the use of reduction of interconnector capacity as a congestion management tool is called for. The TSOs in addition are encouraged to increase mutual co-ordination and information exchange as well as publication of relevant information to market participants in a fully non discriminatory way. In addition to such efforts to optimize the use of the present transmission system necessary new transmission investments should be promoted through increasingly coordinated planning and by monitoring of the use of congestion income by the regulatory authorities.

The NordREG work in 2007 was based on a number of working groups for the tasks outlined in the Work Programme. The work included important dialogues with Nordel, Nord Pool Spot, the Electricity Market Group of Nordic Council of Ministers, Nordenergi and other institutions, in some cases in the form of topical workshops. Draft reports were subject to public consultations prior to finalization and publication.

NordREG in addition pursued its strategic priorities by participation in external working fora e.g. on Nordic AMR (Automated Meter Reading) Forum and a congestion management study financed by the Electricity Market Group.

NordREG international cooperation

NordREG members are actively participating in the work of the EU regulators' institutions of the CEER and ERGEG, realizing the increased importance of the progress of market functioning and market integration on a European scale.

For NordREG the coordination between the work on intra-Nordic market issues and the work on a more pan-European scale in the CEER and ERGEG is of utmost importance. The European work allows a close cooperation with other regulatory colleagues as well as with the European Commission. Seeing the Nordic market in a European perspective much better reveals advantages and shortcomings of the Nordic market model. In addition it allows promoting the integration between the Nordic and the Continental Europe markets.

In 2007 dealing with the European Commission "3rd energy liberalization package" has been one major task, the regulatory authorities drawing on their vast practical experiences in the electricity market. Reviewing national implementations of EU legislation as for instance the Guidelines on Congestion management was another important set of issues. Nordic work could draw on these CEER/ERGEG experiences.

The ERGEG Regional Initiative was launched in February 2006 and the work gained momentum through 2007. The regional focus is not an end in itself but merely a transitional approach on the road to one single EU electricity market. The Nordic regulatory authorities cooperate with the regulatory authorities of Germany and Poland within the North Europe Region. The work focuses on developing the market interface between the Nordic countries and continental Europe. In 2007 especially the work on a harmonized set-up for transparency in the whole sale market of the region proved successful. Regulators, TSOs, power exchanges and main organizations of market participants agreed on a model to become introduced in two steps during 2008.

TSOs operating the interconnectors between Germany and Denmark as well as the power exchanges EEX and Nord Pool Spot in October 2006 signed a memorandum of understanding to introduce day-ahead market coupling on German-Danish interconnectors. The work from the start became integrated with the Regional Initiative of the region. It is planned to start market coupling 3 June 2008.

The interconnectors Baltic Cable between Sweden and Germany and SwePol Link between Sweden and Germany are both in practice exclusively used by their owners ("merchant lines"). Owners of these interconnectors and representatives from regulatory authorities through 2007 analyzed the legal framework and the prospects for making these interconnectors available to the market. A report will be published at the beginning of 2008.

During 2007 preconditions for an increased integration of Nordic and continental electricity markets improved also physically. The commissioning of the Estlink interconnector between Finland and Estonia has recently been followed by an agreement to establish connection between Lithuania (Baltic Region) and Poland. To the west the NorNed Cable linking Norway and Netherlands was layed out, but unfortunately is not yet in operation due to technical problems. In a transitory period the NorNed cable will be operated by explicit auctions until harmonization of gate closure times will allow the market coupling which was the licensing precondition.

The interconnectors between the Nordic countries and continental Europe involve 3 regions of the Regional Initiative. This fact stresses the need for mutual compatibility not only within regions but also between regions. ERGEG explicitly addresses this problem and has published its first report on “coherence and convergence” of the regional initiatives.

Annex

NordREG Reports – brief summaries

Congestion management in the Nordic region

A common regulatory opinion on congestion management

NordREG Report 2/2007

The report reviews use of market splitting, counter trade and reduction of interconnector capacity as congestion management tools in the Nordic countries. It outlines the joint Nordic challenges regarding

- Requirements of new EU Congestion management Guidelines and the practical implementation taking into account the interface with continental Europe
- Taking competition issues into account
- Necessary harmonization of roles of Nordic regulatory authorities
- Development of methods for monitoring and competences of regulatory authorities
- Progress towards a more detailed representation of the physical network in the market splitting model

Congestion Management Guidelines

Compliance report

NordREG Report 8/2007

Congestion management guidelines under Regulation 1228/2003 were amended at the beginning of December 2006. This first Nordic compliance report evaluates the current status of compliance and sets out the further work to TSOs and regulators for ensuring full compliance with the CM guidelines. Furthermore, compliance across the Northern Europe region should be addressed in further work.

The report includes the following observations:

- Implicit auctions used comply with the CM guidelines
- Reduction of interconnector capacity as a congestion management tool should become subject to increasing transparency
- Increased focus needed on joint Nordic network planning in order to deliver timely expansions
- More advanced co-ordination and information exchange between TSOs should be considered to ensure the security of the Nordic power system and enhance the efficient functioning of the Nordic market
- Nordic regulatory authorities should consider a common process for regular evaluation of the CM guidelines
- Information release by Nord Pool Spot and TSOs is well developed, but should be further coordinated and developed in compliance with CM guidelines and the agreed harmonized elements on transparency within the ERGEG Northern Europe Regional Initiative
- The process on regulators' monitoring of use of congestion income should be harmonized

A common Nordic platform for balancing services

NordREG Report 4/2007

The report evaluates Nordel's proposal on balancing contained in the report "Balance Management - Common principles for cost allocation and settlement" (April 2006) and the Nordel agreement on balancing of 7 February 2007. In sum, NordREG finds that the principles agreed on by Nordel create a sound base for a harmonised Nordic balance management that has a potential to enhance the functioning of the Nordic market and also to strengthen the Nordic market in the Regional and European context. NordREG also has the following observations

- The proposal of a common cost base is in line with the EU electricity market directive
- The proposed model on imbalance pricing does not cover the total cost for balancing services. Also these costs should be covered in an non-discriminatory way
- Harmonising the balance management will lead to changes in payments among market participants. In total, the new common system should not be more costly than the old systems. The regulatory authorities need more economic information to be able to assess whether the final fee structure is fair and does not create undue barriers to certain categories of players.

The report also addresses the coordination of national approval procedures of the harmonized balancing model as well as necessary changes in national laws and regulations.

Costs and Benefits of Nordic Retail Market Integration

NordREG Report 5/2007

The report identifies and evaluates qualitatively some of the costs and benefits of Nordic retail market integration. NordREG considers that the benefits will most likely outweigh the costs by a clear margin.

If retail market integration can have an influence on the general retail market development leading to best practise solutions in all Nordic countries, the benefits could be substantial. There is a clear potential for efficiency improvement, reduction of operational costs and innovation in all Nordic retail markets. The costs are primarily on the technical and organizational side. Although potentially large, these costs should not be exaggerated.

Monitoring of the Nordic Regulation Power Market

NordREG Report 6/2007

The report briefly describes the existing Nordic regulation power market and looks at further needs for monitoring of this market. The suggestions for improvement of the present monitoring and the suggestions for further work are based on interviews with the TSOs and market actors and discussions within NordREG. The report contains among others the following observations:

- There is a need for increased transparency of the regulation power market. A detailed description of the existing rules and operations of the market should be published by the TSOs.
- Monitoring of the regulation power market might need to be more harmonised in order to secure equal treatment of the market participants and to get a better overview between the different electricity markets. Not desirable arbitrage between the markets might exist and the abuse of market power must be avoided.

- An increased level of harmonization of the national elements of the regulation power market might be a necessity both to improve the functioning of the market and in order to allow better monitoring

Regulation of the Nordic TSOs with focus on Market Efficiency and Harmonisation *NordREG Report 7/2007*

The report describes the regulation of TSOs in each Nordic country, including the economic regulation, and with a view to the latest EC requirements. Furthermore, a questionnaire has been conducted among the stakeholders in order to gain more knowledge on stakeholders' views on the TSOs and handling of their tasks.

The examination shows that not only acts, but also further regulation seem very alike. Concerning the regulator's role and power, as well vis-à-vis the TSOs as in general, there is, however, a significant difference between the Nordic countries. Harmonisation may lead to more efficient functioning of the Nordic market.

The results of the questionnaires show a need for addressing issues concerning network planning, investment decisions and the financing thereof, construction authorisation and permission process, transparency of TSO actions and a wish to accelerate the ongoing work may be called for. These issues are already addressed within either NordREG or Nordel.

Nordic Market Report 2007 Development in the Nordic Electricity Market *NordREG Report 7/2007*

The Nordic Market Report, the second in a row, describes the status and development of the Nordic electricity market, covering Norway, Sweden, Finland and Denmark. Among other things the report offers statistical information on the Nordic market, description and data of the market structure, main players and information on the retail market.

c/o Energiamarkkinavirasto
Lintulahdenkatu 10
FI-00500 Helsinki
Finland

Telephone: +358 10 60 5000
Telefax: +358 9 622 1911
E-mail: virasto@energiamarkkinavirasto.fi
Internet: www.nordicenergyregulators.org