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NordREG consultation on “Measures to support the functioning of the Nordic financial electricity market”

Finnish Energy highly appreciates the opportunity to comment on the NordREG report. We find the report very informative and as such a good basis for further discussions regarding the Nordic financial markets.

At this stage it is too early for Finnish Energy to take a definitive position on which one, or if any, of the six models presented is a good fit for the Nordic financial markets. The desired characteristics of the financial market should define the most suitable model to be used.

The following fundamental issues should be taken into consideration while assessing the different models:

1. Assessing the need for TSO intervention

The report mentions that *“a clear case of market failure should be identified before the TSO is instructed to intervene”* and *“whether the TSO should be instructed to support a market maker function or auction EPAD contracts, depends on the situation in the concerned bidding zone, and should be subject to scrutiny on a case-by-case basis”*.

Finnish Energy fully agrees with the report on this. The need for TSO intervention in the financial markets should first be evaluated and understood with confidence before any changes are introduced. Any of the support measures to the market presented in the report will have a cost which will be carried by the tariff payers in the end.

In Finland, one large price area has proven to be a good way to create sufficient market liquidity. A fundamental issue that increases liquidity problems in the Nordic area as a whole is the fact that there are rather small price areas with very few potential counterparties. Results of a survey¹ conducted by Fingrid in 2015 concluded that some of the Finnish market participants were satisfied with the current EPAD market and hedging possibilities but some faced liquidity problems. One of the reasons for low liquidity was considered to be the size of bidding zones but also structural imbalance between production and consumption in Finland. Therefore it is of importance to evaluate the reasons for these possible challenges and potential ways to mitigate them before any financial measures or actual intervention of TSOs.

Testing of the different models presented in the report could possibly be done in those price areas where the price discovery process is known to be challenged, e.g. in the small price areas Northern parts of Sweden and/or Norway. The situations and challenges can be different from price area to price area and can necessitate different type of interventions. Hence, we agree with the report, that there might be a need for a Nordic tool box rather than one single measure.

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2. Market model should support EPAD availability and trading

Members of Finnish Energy find the current EPAD structure satisfactory and thus there is no need for introducing other parallel products. However, if it can be shown that there is a need to support the functioning of the financial markets, the market model used in the future should support and promote the availability of EPADs and trading and price discovery with EPADs, e.g. via the introduction of supported Market Making arrangements. Supporting an existing market model is expected to be significantly more cost-efficient for the Nordic Power market, as compared to establishing another expensive, cumbersome and unproven parallel structure i.e. FTRs.

Finnish Energy strongly agrees with Hagman Energy and Thema Consulting Group in that, "*FTR auctions are inferior to measures that support EPAD trading in the Nordic market*". The use of FTRs would most likely split financial markets and impair liquidity and thereby hedging would become even more challenging. Hence, FTR options or obligations (i.e. models 5 or 6) are not viable alternatives to EPADs.

In the light of the discussion above, model no. 1 "support market maker function" currently seems to be the preferred option. Alternative 2 i.e. TSO as a market maker should be excluded for the reasons described in the report. Models 3 and 4 i.e. auctioning of EPADs or EPAD Combos could be considered for e.g. individual specifically problematic price area borders but Finnish Energy questions exposing the TSOs to financial market risk.

Yours sincerely,

FINNISH ENERGY

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¹ Fingrid, 2015, Yhteenveto Fingridin tekemän johdannaismarkkinoita koskevan kyselyn tuloksista.

<http://www.fingrid.fi/fi/ajankohtaista/Ajankohtaista%20liitteet/Ajankohtaisten%20liitteet/2015/Kysely%20johdannaismarkkinoista%20yhteenveto.pdf>

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