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Subject: "Strategische prioriteiten E&G groothandelsmarkten, zaaknummer 104195"

Dear Sir, Madam,

Vattenfall welcomes the opportunity to respond to the strategic priorities concerning wholesale power and gas markets, as proposed by the ACM. In general, Vattenfall recognises the importance of the three priorities as described on page 3 of the consultation document:

i. Completion of European market integration, primarily through implementation of European regulations and, where possible, in anticipation of the definitive adoption of these regulations;
ii. The creation of optimal conditions for efficient market operation, mainly through the implementation and enforcement of European rules for transparency and market integrity;
iii. Guaranteeing the security of supply in a future where sustainable energy has a greater share.

In this response we comment in more detail on the priorities and the consultation questions.

Priority area A – E on Market integration

Vattenfall agrees with the ACM that integrated intraday markets are necessary for an efficient use of the available interconnection capacity. More efficient use of available interconnection capacity creates trading opportunities, which enables market parties to make more efficient use of flexible production capacity (e.g. gas fired power plants) across borders. Improved functioning of cross-border intraday markets are a prerequisite to accommodate the growing share of renewables and it increases security of supply. Currently, most European balancing markets are still national and don't allow cross border capacity to participate sufficiently. Therefore Vattenfall strongly believes that all (flexible) plants should be enabled to be used in the adjacent balancing markets and asks the ACM to play an active role achieving this.

In addition to the above, we believe there is room for improvement concerning the integration between gas and power market design, which should allow for a flexible gas market that is able to react to the supply-demand situation of the power market. This could include a flexible set-up of the (exit) capacity for gas fired power plants, to reflect their (changing) role in the production of power. And in general a higher level of harmonization between allocation & day-ahead market structured of gas and power.

Furthermore, Vattenfall supports the idea that (flow-based) market coupling is essential in making use of available transmission capacity and reaching a truly integrated European electricity market. The introduction of flow based calculations should further increase the efficient allocation use of grid capacity. Vattenfall is however of the opinion that flow based capacity allocation is only effective if the TSO, power exchanges and regulators (the ACM included) inform the market in the most advanced and detailed way on (i) how the flow-based methodology works and (ii) on how the available transport capacity will be calculated. At the moment market parties lack this crucial information to be able to understand how prices will be set when flow based market coupling is introduced. Improved information, consequently leads to less market risk and hence to more efficient bidding behaviour. Therefore, Vattenfall urges TSOs, power exchanges and regulators to inform the market as soon as possible in the most detailed way. For more detailed proposals to increase the transparency of information, Vattenfall refers to the "Liquidity questionnaire wholesale electricity markets 2012".

Vattenfall agrees with the argument that optimal bidding zones ensure the price signals for investment avoiding congestion on the long term. Vattenfall considers that congestion should be managed where it physically appears. Hence, they should not be pushed to the country border. Congestions that cannot be solved by grid investments that are socio-economical justifiable, should be managed by market based solutions. Vattenfall agrees that efficient bidding zone delimitations preferable should take the physical reality into account rather than the geographical constraints. From that point of view we also welcome the message from the ACM that this may mean that the current bidding zones are rather expanded (when the grid so allows) than decreased in size. Especially for small countries with a highly meshed network like the Netherlands, the focus should be on connecting to adjacent prices zones like Belgium and Germany. To avoid congestion in The Netherlands, Vattenfall therefore believes that timely and necessary investments by TenneT and the regional grid operators are necessary.

Better functioning cross-border intraday markets (considerable shorter lead times), improved transparency on fundamental data by the TSO and even expanded prices zones may lead to increased liquidity levels on the Dutch wholesale market.

Priority area F – H on conditions for competition

Vattenfall believes that transparency is a prerequisite for a well functioning wholesale market. Therefore, Vattenfall supports the REMIT provisions, as long as the rules and conditions are sufficiently clear. Vattenfall welcomes the guidance given by ACER and understands that norms must be left open to some degree, in order to tackle new forms of market abuse.

To a certain extent case law available for market manipulation of the financial markets can be of guidance for the energy wholesale market, mainly in the area of market manipulation.

However, to the largest extent both markets are not easy to compare. On the definition of "inside information" there is only insufficient guidance or case law, especially on the kind of information falling under Article 2 (1)(d) REMIT. Vattenfall would appreciate more guidance on the definition of "inside information".

In relation to the transparency requirements for TenneT, Vattenfall agrees with the ACM that the provisions of fundamental data by TenneT to the market should be improved significantly. Considering the importance of this fundamental data on supply and demand for efficient market functioning, we support any proactive action by the ACM in this respect.

Finally, Vattenfall is pleased that the ACM supports PwC's recommendation to consider adequate investment incentives for TSOs to invest (more proactively) in required new infrastructure. A proactive approach by the grid operators will not only help to avoid congestion, but is also crucial to reach the Dutch renewable targets.

The last decade has seen a strong development of (fossil fired) generation capacity in locations designated for large scale electricity generation (SEVIII-locations). One of the reasons that necessary grid reinforcements to connect these locations to the high voltage grid has lagged, is that these developments have not been anticipated sufficiently upon. Because grid reinforcements take more time than building new generation capacity, it is very important that grid operators have the tools and regulatory framework that allows them to proactively anticipate (and invest) on developments that put a strain on the grid (e.g. starting internal studies and calculations). This will avoid delay and can optimize the connection and grid capacity in such a way that it is as efficient as possible. This would entail finding an optimal solution for the project developer and the grid operator. In the current situation a project can be made overly expensive due to grid issues. This does not mean that new grid capacity should be building ahead of FID of a new power plant, but regulation should allow for those investments that accelerate grid developments once FID of generation projects is taken. It should also enable the development of a Master plan for the grid that enables connecting the renewable energy capacity that will be build over the coming decades.

This is particularly important for connecting wind power to the grid. Similar to production locations for fossil fired capacity (that are detailed in the SEVIII) the government has designated the locations where wind power should be developed in its "structuurvisie wind op land" and "structuurvisie wind op zee". Already now grid operators should make arrangement to allow the transport of power from these locations. This is especially relevant for those locations were several market parties have advanced plans for wind power development. Similar to the connection of fossil fired capacity to the grid, TSOs should look at the investments needed to connect *all* capacity at a location and should not look at investments needed for individual project. This is highly inefficient. Regulation should also allow TSOs to more proactively invest in such projects.

Priority I – K on security of supply

Vattenfall agrees with the ACM that capacity mechanisms in The Netherlands are neither required, nor desirable. Since security of supply is an international issue, Vattenfall welcomes the strong support of the ACM a joint European approach. Considering the fact that some countries have over-capacity, whilst other countries are expecting a capacity shortage, it becomes ever important to look at capacity issues at an EU (or at least regional)

level. Vattenfall believes the ACM has a clear interest to participate actively in the European discussion concerning security of supply, in order to prevent capacity mechanisms that (unnecessarily) distort the wholesale markets.

In this context, Vattenfall likes to stress that, due to the low demand (in the Netherlands) and the import of subsidized power from Germany, there is no level playing field and, at the moment, gas fired power plants are not profitable. To establish a level playing field, market based deployment of all production facilities is necessary. More specifically, it requires a re-assessment of the current structure in the German market, where renewables do not have a clear demand-based incentive for production. Secondly, this market based deployment of production is also necessary to ensure that sufficient flexible production capacity remains available throughout the path towards a more renewable energy market in Europe. This market based structure in the future will allow the market price to reflect the combination of factors, such as a possible sudden drop in renewable supply, available demand and the higher production cost per unit of flexible, but secure fossil production.

Priority L – P on Market Integration

In general, Vattenfall supports the focus of the ACM on the development and implementation of the European Network Codes concerning gas markets and believe it is right to put this on the top of the priority list for the coming years.

Vattenfall strongly supports the focus of the CMP implementation on overselling and buy-back (OSBB), as this is the mechanism that maintains the highest level of stability in the market. This is realized by maintaining existing capacity rights, whilst offering the TSO an incentive to oversell additional firm capacity, if it believes not all sold firm capacity will be utilized. We trust the ACM will ensure substantial market involvement & consultation in the process of establishing the details of OSBB, to ensure the incentives are set correctly for the TSO, whilst offering additional capacity in a workable manner for the market. Vattenfall is naturally prepared to be closely involved in the process.

Early implementation of the CAM Network Code could indeed offer valuable information necessary for the development of capacity auctions that function. However, Vattenfall wishes to express its concerns when it comes to the early implementation of bundled capacity through PRISMA at several IPs in North West Europe. The capacity that is envisaged to be bundled in this pilot, consists of two completely different contracts on each side of the border, with different levels of firmness and different terms & conditions. The proposed bundling in the pilot does not intend to remove these differences, but will merely mask them in a ‘single click purchase’. This results in additional work on unraveling the underlying actual products and could link products that market parties do not wish to combine.

We strongly believe the ACM should prioritize the alignment of levels of firmness and other conditions of both sides of the bundled products, rather than focusing on the PRISMA platform itself, which masks the underlying problems. Solving product differences before bundling products is the only way to prevent the loss of efficiency and to maintain the previous levels of transparency that were only recently obtained in Europe, regarding capacity products. To achieve the ambitious 2014 deadline, the ACM should ensure this issue gets full attention in 2013.

Vattenfall has been closely involved in the establishment of the new balancing regime in the Netherlands. We are extremely pleased with the results and believe it provides a unique focus on market parties, when it comes to maintaining a balanced system. Naturally, we also support the European approach to energy markets and wish to see a harmonized regime that allows barrier free flow of gas between EU markets. We believe it is right for the ACM to focus its attention on the process of shifting from the Dutch balancing regime to a harmonized approach, whilst maintaining its current positive features. Monitoring the effects of the move from the bid price ladder to market based balancing for the TSO, if necessary, is important in this respect.

In the consultation text, the ACM indicates that it supports early implementation, to ensure lessons can be taken from these pilot processes, to enable a solid final implementation. Vattenfall wishes to stress the importance of analysis after a pilot period. We believe more can be done with the outcome of pilot project and we strongly propose the ACM to involve market parties in this process. As an example, we believe the results of the initial pilot project of bundled capacity auctions at Bunde – Oude Statenzijl should have been discussed, shared and consulted on, before a new and more extensive pilot was approved. We believe the new pilot does not take into account the concerns, questions and difficulties that market parties have. This prevents the TSOs from taking lessons learnt from the first into the second pilot. We ask the ACM to ensure a clear process is created for after a pilot period, to analyse the results and consult on the way forward and lessons learnt.

Priority Q – S on Optimal Conditions for Competition

Considering the recent national and international discussions about gas storage tariffs and the role storage plays in the European energy markets, we believe it is suitable for the ACM to put it high up on the agenda. We believe the measure should focus on the actual pressure it puts on (or takes off of) the grid. Rather than the implementation of an (apparently random) discount, this would provide a sustainable and stable basis for an adjusted tariff mechanism.

With regards to the last point of the ACM list, we have mixed feelings, as it encompasses such a broad topic, namely the task of the TSO and the role of the regulator in this respect. We believe it is important to keep recognizing the role of TSOs as monopolists that provide a specific service to the energy market. Due to the monopolistic nature of this task, the regulator fulfils an important role in ensuring a regulatory regime is set up that incentivises the TSO to the correct behaviour. In this respect, priority S supports this notion.

In addition to the above, we believe it is equally important to fit the tasks of the TSO into current times. In times of financial crisis and in the current difficult gas market situation in the Netherlands, investments and innovation by market parties have been replaced by the need for stabilization, recovery and consideration of the role of gas within the current and future energy market. Although we believe it is admirable of the ACM to want to push the TSO to improve and invest, we would like to ask for a cautious approach in this respect.

We believe now is the time for the ACM to focus on ensuring a stable, reliable, transparent and efficient regulatory framework for the market. To settle insecurity and reluctance to invest, we believe stability is vital. In this respect, we believe it is beneficial for the ACM to only push the TSO when it contributes to this stability. Besides this, we hope to see the ACM focus on ensuring the TSO can and does carry out its regulated services, before it explores

further (commercial) activities. We recognize the important role the ACM plays in the next years to find ensure the regulatory framework within which the commercial market can be maintained.