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AK Position Paper

# Communication of the EU-Commission on the New Electricity Market Design

## About us

**The Austrian Federal Chamber of Labour is by law representing the interests of about 3.4 million employees and consumers in Austria. It acts for the interests of its members in fields of social-, educational-, economical-, and consumer issues both on the national and on the EU-level in Brussels. Furthermore the Austrian Federal Chamber of Labour is a part of the Austrian social partnership.**

**The AK EUROPA office in Brussels was established in 1991 to bring forward the interests of all its members directly vis-à-vis the European Institutions.**

### **Organisation and Tasks of the Austrian Federal Chamber of Labour**

The Austrian Federal Chamber of Labour is the umbrella organisation of the nine regional Chambers of Labour in Austria, which have together the statutory mandate to represent the interests of their members.

The Chambers of Labour provide their members a broad range of services, including for instance advice on matters of labour law, consumer rights, social insurance and educational matters.

More than three quarters of the 2 million member-consultations carried out each year concern labour-, social insurance- and insolvency law. Furthermore the Austrian Federal Chamber of Labour makes use of its vested right to state its opinion in the legislation process of the European Union and in Austria in order to shape the interests of the employees and consumers towards the legislator.

All Austrian employees are subject to compulsory membership. The member fee is determined by law and is amounting to 0.5% of the members' gross wages or salaries (up to the social security payroll tax cap maximum). 560.000 - amongst others unemployed, persons on maternity (paternity) leave, community and military service - of the 3.4 million members are exempt from subscription payment, but are entitled to all services provided by the Austrian Federal Chambers of Labour.

Rudi Kaske  
President

Werner Muhm  
Director

## The AK position in detail

Within the context of the recast of the EU electricity-system, BAK endorses the development of the current electricity-only-market and strongly opposes the introduction of capacity markets. BAK also refuses steadfastly the proposed “new deal” foreseeing the metamorphosis of the electricity consumer to an electricity speculator as far as households are concerned. The **financialisation** of commodity markets **results in high volatility** and in the enhancement of divergence of demand and offer, this having the contrary effect than envisaged by the EU-Commission. This is especially the case for commodities which represent a special good of general economic interest as electricity is.

Having said this, BAK proposes to underpin the development of the electricity market design by a transparent framework based on public order law, allowing for a steered, systemic-holistic progression of the energy market. We hold the opinion that only this way a cost-efficient, affordable and sustainable electricity provision for households and real economy can be achieved. The corner stone for this energy policy will be the increase of energy efficiency.

### Fundamental considerations

In the present Communication the EU-Commission neglects the fact that (electric) energy is not an ordinary commodity. The reliable and affordable provision with energy represents an existential fundament of human beings in modern society. Hence, energy provision is a

service of general public interest. Moreover, the Communication totally ignores that the **political room for manoeuvre is determined by the law of physics**. Fundamental factors of the energy market as transport capacities in the transmission and distribution grid and the relevant costs or the fact that electricity storage possibilities are very limited are blinded out on the one hand.

Whereas on the other hand financial instruments are strongly endorsed: Already today electricity is traded up to seven times before it is provided to the final consumers. Each level of trade equals an additional mark-up. This fact is aggravated by the **complexity** of the **electricity market** which **prohibits** de-facto ex-post **control of market abuse**. It is practically impossible to forward evidence if high electricity prices derive from competition or collusion of market participants. Our market observations show that market risks and high electricity prices are passed mainly on private households. Based on the experience with other commodity market places, BAK assumes that with increasing financialisation of these markets price volatility will accelerate.

This fact brings about the risk of **market foreclosure mainly of small and medium sized energy producers**. Due to these uncertainties price signals do not suffice in order to create meaningful incentives for cost-efficient investment into necessary energy infrastructure and to minimise the systemic cost as a whole. With regard to the macroeco-

conomic importance of investment into energy supply BAK dreads that increasing financialisation will have direct negative implications on employment and growth.

It is striking that the Commission's Communication omits to deal with the **question of affordability of energy**, energy services and new technologies. The possibility of participation of private households in the conversion of the energy system is directly linked to their financial resources. This is true for the execution of cost intensive energy efficiency measures as well as the possibilities of production of renewables and the installation of intelligent technologies (e.g. smart home applications). The lack of considerations as to these distributional perspectives will bring about the creation of a two-class society of energy consumers.

### **Unrealistic expectations as to demand flexibility of households**

Up to now, the high expectations as to demand flexibility of consumers have not been fulfilled in real life. As an introductory remark BAK retains that the market design concept of the EU-Commission omits the distinction between three totally different types of consumers:

1. industrial consumers,
2. small and medium-sized enterprises
3. and private households.

Whereas electricity producers and big energy consumers like industrial clients dispose of all necessary technical and administrative pre-conditions to actively participate in the energy market, this is true for only a very small percentage of

private households. The representative **private household is not in the position to adjust its load behaviour to short-term price volatility.**

The EU-Commission's imagination of a rational optimisation of consumption by private households does not correspond to real life of human beings and therefore is not actionable. Electricity demand is steered by daily routine (with demand peaks in the morning and late afternoon). Hence, the possibility to change the consumption point of time over the day is very limited for standard household applications. Relevant research work confirms that the demand flexibility of households is limited mainly to automatically adjustable electro-thermic devices (as for example refrigerators, heating, warm water processing).<sup>1</sup> Only households in Scandinavian countries, which often use electricity for heating, dispose of a bigger flexibility as to electricity demand. However, electric heating is an exception within the EU Member States and can not serve as a valid sample or model.

Furthermore, from BAK's point of view it is unrealistic to assume that flexible electricity demand by households can balance the fluctuations in the production and thus avoid the actual enormous price volatilities of the energy market. By its financialisation the market risks are simply shifted onto the private households. They will be divided into two types: On the one hand the financially well equipped, technic-affine and well informed "smart household" which participates actively in the energy market – so to speak a speculator – profiting from price volatility. On the other hand the majority of households that cannot actively manage their energy consump-

tion, neither from a financial nor from a time perspective. The most negative effect has to be expected for households with low income.

**The affordable and reliable provision with electricity is the precondition for all citizens to participate in modern life.** The EU-Commission’s proposals favour a small group of “smart households” which dispose of all requirements to profit from favourable prices. The majority of households, however, will be confronted with considerably higher costs. Due to the inflexibility of their demand they cannot avoid high electricity prices. Moreover, they will not be able to profit from an “insurance against price volatility” as considered by the EU-Commission. The reason for this is simple: Energy dealers will include the additional costs into the energy price. By consequence, BAK strongly rejects this option from a consumer and distributive perspective.

And finally: Time dependent price and tariff structures lead to unacceptable interventions into private and family life of households BAK is totally opposed to such interference into the private sphere.

BAK strongly urges the EU-Commission to take into consideration the different participation possibilities of energy consumers and to implement concrete measures for vulnerable consumers.

**Better use of supply side flexibilisation potential**

Supply must be oriented along the necessities of consumers and not the other way round. This, however, is less and less the case. In order to reduce the

enormous systemic cost – especially re-dispatching cost, cost for balancing energy and for the grid expansion – it is high time to come toward a balance of electricity demand and supply.

Therefore, BAK is positive about the flexibilisation of the electricity supply side. It is an important lever for the reduction of systemic costs. To achieve this target a reform of renewables’ subsidies will be indispensable. State aid as it stands provides no de-facto incentive for producers of renewables (wind, photovoltaic) to adjust their production to actual demand. This is true even in the case of negative prices at the electricity exchange. The main reason for this unreasonable behaviour is to be found mainly in subsidy frameworks based on quantity: Renewables producers receive a fixed fee per kilowatt hour of electricity independently of the market price. It is the households who have to bear the main share of these systemic costs. In order to achieve market integration of renewables in a cost efficient way, subsidy frameworks should be altered and simplified as fast as possible mainly based on incentive oriented investment aid. This way, demand oriented production can be stimulated and volatility as well as power peaks will decrease and grid expansion can be carried out without the need of capacity mechanisms.

**Reinforcement of cross-border trade**

BAK is positive about the increased coupling of electricity markets, that is to say the cross-border cooperation of transmission system operators and electricity exchanges. By creating bigger trade spaces cross-border transmission capacities may be better used, systemic costs (shortage management,

re-dispatch services) will decrease and thus systemic stability and the general security of supply will increase.

A positive example for cross-border electricity exchange represents the shortage-free border between Austria and Germany.

Essential pre-requisite for cross-border cooperation is the transparent price setting, which is only achievable by effective regulation of electricity exchange places. Experience, however, shows that due to the complexity of the electricity market regulators are put in the position to regulate with the wisdom of hindsight instead of proactive management. Hence, BAK proposes to permit access to electricity exchange only to those legal persons or entities which either produce or consume electricity. Financial institutes and market makers shall be excluded from electricity exchanges.

Within this context it is adamant to allow electricity trade only on the basis of standardized contracts in order to exclude ex-ante highly complex contractual agreements, especially non trivial derivatives.

Finally, all electricity exchange places should be subject to harmonised regulation in order to avoid regulatory arbitrage which exists for example between the Leipzig and Paris electricity exchange. To cite as an example, on the Paris spot market – a cooperation partner of the Leipzig electricity exchange – public control is limited: The French regulator is only competent for the trade in France and for cross-border trade. The spot trade carried out in Paris for the German and Austrian spot market is left to self-regulation.

The consequence of the lack of regulation is estimated to be significant, as the spot exchange determines the prices for the future and OTC trade. Futures depend on the trends of spot prices (spot markets). Estimates show that if the prices on the spot exchange places were manipulated by insider trading or market manipulation, thus leading to an increase only 1% of future prices for the next year, this fact would bring about increased cost of € 250 million per year <sup>2</sup>

#### **Re-enforcement of regional cooperation – no decision-making structure under private law**

BAK agrees with the EU-Commission that regional cooperation between transmission operators and the expansion of power grids are a central pre-requisite to secure reliable electricity supply. New possibilities of intelligent grids have to be used, promoted and adapted to the necessities of the energy market. This way, regional disparities - electricity surplus or deficit – can be balanced in an easier way without having to resort to additional production capacities. The expansion of grids – especially connected grids (Verbundnetze) require efficient concession procedures to reduce on the one hand time consuming proceedings, on the other hand to consider well-founded interests of third parties in an adequate way.

Efficient cooperation needs detailed and harmonised rules. However, they have to be stipulated by the competent authorities and not by the addressees of the law themselves, the transmission operators (ENTSO-E and ENTS-G). BAK rejects the transfer of sovereign power to transmission operators as

well as the expansion of their competences – as proposed in the Communication: Although the regulation of cooperation between grid operators (grid codes) might be highly complex, administrative authorities have still the obligation to secure their own sufficient knowledge and expertise to exercise control over the addressees of regulatory rules. Within this context BAK is also strongly opposed to the proposed empowerment of the European Agency for the Cooperation of Energy Regulators (ACER). Important decisions of ACER are taken behind closed doors and in a non-transparent way: To cite as an example the actual decision of ACER to separate the German-Austrian electricity price-zone.

#### **Capacity mechanisms only in the form of reserves for network stability**

BAK rejects the introduction of capacity markets, as the electricity market as it stands is characterised by over-capacities. In order to use the existing capacities for the maintenance of security of supply, the requisite transmission grids have to be established. Moreover, legal provisions have to be implemented in order to keep the necessary power plants operable. For the actual and substantiated costs of operability the plant operators shall be compensated in an adequate way.

#### **Inclusion of system operators and municipalities**

BAK takes the view that the Communication does not give sufficient attention to system operators. Distribution grids represent the essential infrastructure for the integration of decentralised renewable power plants. When establishing demand-response flexibilities within the electricity system, the introduction of an intelligent governance of distribution grids is of central importance. As already mentioned, BAK does not share the opinion that demand-side flexibility can be realized at household level. The balancing between supply and demand can only be achieved by local and regional coordination steered by the grid and by inclusion of an adequately high number of decentralized producers and consumers. Especially municipal establishments and infrastructure represent central elements of load management from the production and consumer perspective. The coordination and balancing function should be assigned to the system operator.

## Footnotes

<sup>1</sup> Vgl. Gawlik, Wolfgang et. al.: "aDSM - Aktives Demand-Side-Management durch Einspeiseprognose"; Endbericht; April 2014; Internet: [http://www.ea.tuwien.ac.at/fileadmin/t/ea/projekte/aDSM/aDSM\\_834612\\_vorlaeufiger\\_Endbericht.pdf](http://www.ea.tuwien.ac.at/fileadmin/t/ea/projekte/aDSM/aDSM_834612_vorlaeufiger_Endbericht.pdf) (21.9.15)

<sup>2</sup> UNCTAD –Studie, Juni 2011 „Price formation in financialized commodity markets“



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