

## 2. What and when to auction?

### 2.1 What to auction and how early?

**Question 1** As a general rule throughout the trading period, in your opinion, are early auctions necessary?

**Yes, absolutely. The priority for the electricity sector is to secure early release of phase 3 allowances to deliver sufficient market liquidity to allow generators to hedge their forward electricity sales and the management of their portfolio of plants.**

Generators typically hedge 10-20% of their output 3 years in advance, 30-50% 2 years in advance and 60-80% 1 year in advance. At this point the prices of electricity, fuel and carbon are locked in and backed by contracts for physical supply, e.g. EUAs in the case of carbon, thereby managing both commodity and commercial risk.

Assuming that 50% of EU electricity production is covered by such hedging policies would lead to a requirement for approaching 1 billion allowances to be available ahead of 2013.

It is highly unlikely that sufficient 'surplus' phase 2 EUAs or JI/CDM credits will be available to satisfy these requirements and physical access to phase 3 allowances will be required to avoid undesirable price volatility in the secondary market with knock on impacts on power prices.

While the secondary market could offer forward contracts for phase 3 allowances, these would not be backed by physical supply without early auctioning and volumes could also be expected to be limited. Given that generators will be very short of allowances in phase 3 and the penalties for non-compliance are very high, the requirement to physically back sales of EUAs becomes increasingly important.

Consequently, **early EUA auctioning is a priority for the electricity sector to maintain liquidity in both the power and carbon markets.** This leaves the issue of whether allowances should be auctioned as spot or futures.

**If so, what should the profile of EUA auctions be?**

- 5-10% in year n-2, 10-20% in year n-1, remainder in year n
- 10-20% in year n-2, 20-30% in year n-1, remainder in year n
- 20-30% in year n-2, 30-35% in year n-1, remainder in year n
- Other? Please specify.

In terms of choosing among the options presented, option 3 (20-30% in year n-2, 30-35% in year n-1) is closest to our position. Indeed, as a general rule-of-thumb, the more EUAs auctioned ahead, the better. For the pre-2013 period, auctioning ahead of 50% or more is best. We assume that the figures refer to EUAs issued in any given year. Finally, the Commission may want to raise the option of EUA auctions for year n-3.

**Question 2** Do you think there is a need to auction futures? If so, why so?

Yes, absolutely.

**Our (real) experience tells us that auctions need to be in place early** (by-mid 2011 for 2013/14 allowances) as electricity companies need to hedge their positions several years in advance. **Otherwise risk exposure will lead to unnecessary, higher costs and loss of liquidity in connected markets.**

By the far the biggest advantage of Futures is that they enable emitters to hedge their risks. As it is essential for electricity companies that they can hedge risk, EUAs need to be hedgable. That is why EUA futures are a necessity.

Another very important reason why we favour futures auctions is because they require a much less initial outlay of cash than spot auctions. This is important since it will increase the number of entities participating in the auction (since the up-front financial effort is lower).

On the negative side, auctioning of futures will be a less effective choice if an improper design increases transaction costs to participating parties. Likewise a rejection of a common approach to auctioning may render the development of derivative products more difficult. However, from EDP's point of view, the two arguments presented here against 'futures' auctions are administrative and political and should be pre-empted in the Regulation with requirements for a single set of rules with simple participation criteria.

Therefore, **EDP is strongly in favour of futures auctions.** Any decision 'not to auction early' would have serious ramifications for the electricity market.

If futures auctions are not in place the consequences are as follows:

- Producers and suppliers cannot manage commodity risk thereby resulting in higher risk premiums and higher costs
- Less liquidity in market due to lower risk-taking on part of participants, thereby leading to inefficiency and higher costs.

**Question 3** What share of allowances should be auctioned spot and what share should be auctioned as futures for each year?

See answer to question 1 (above) for amounts auctioned in 2011 and 2012. Going forward, following-on from our position from December 2008, we believe that **as many EUAs as possible should be sold as futures**, provided that Member States are able to properly arrange and solve the requirements for providing futures. This would be facilitated by a streamlined and fully harmonised approach in auctioning aiming at centralised or interoperable bidding platform(s) and avoiding the use of multiple auctioning places within the EU (in particular avoiding 27 separate auctioning places).

In the initial period, and in the lead-up to the upgrade of the CITL, then auctioning ahead of 50% or more is best. Also noted above, the Commission may want to raise the option of EUA auctions for year n-3.

**Question 4** Should the common maturity date used in futures auctions be in December (so the maturity date would be December in year n, both when auctioning in year n-2 as when auctioning in year n-1)? If not, please suggest alternative maturity dates and provide evidence to support your view.

Yes. Having one common maturity date per year is important for the liquidity of the secondary market. It also makes the administrative process much easier (hence reducing associated costs). In any case, this is already the standard in the market for other future products. Finally, it is important to emphasise here that deliveries from auctions must be done before deliveries from the market to enable settlement of physical market transactions. Put another way, in order to manage commodity risk you first need to have physical allowances available.

## 2.2 Auction calendar

**Question 5** For spot auctions:  
What should be the **optimum** frequency of auctions?

Reaching an optimum solution requires balancing the twin goals of predictability and liquidity. Frequent auctions would increase predictability (i.e. steady stream of EUAs issued) and a common platform would allow for simplicity. A common platform would also be liquid, something which probably cannot be said of holding monthly auctions in smaller Member States.

Where there are a number of platforms operating under the same rules - then less-frequent auctions would be more practical from a simplicity point of view. Likewise, less-frequent would also be more liquid than monthly auctions. However, this solution would still have the negative impact of increasing 'lumpiness' which would decrease predictability.

A second-best solution which could be used where a common platform is not in place, is for the various platforms to use some form of auction rotation - i.e. the platforms could take it in turns to auction EUAs, providing that it could grow into a centralised approach as soon as possible.

What should be the **minimum** frequency of auctions?

Quarterly. Lower frequency will result in less flexibility to incorporate market information.

What should be the **maximum** frequency of auctions?

Monthly  
Higher frequency will result in administrative burden for the companies.

Please provide arguments to support your case.

**EDP strongly favours more frequent auctions wherein participation costs are low.**

Our reason for not recommending weekly auctions (as opposed to monthly) is that the operation cost for participants, especially small players, may be too high.

**Question 6** For spot auctions, what should be auction size?

When a centralised (or hybrid) approach for auctioning is adopted, auction size is less important (compared with smaller national auctions). Therefore, EDP believes that a simple division of the number of auctions to be held per year and allowances available for that year would suffice. In the vast majority of cases, all auctions should have the same volumes give-or-take 2 or 3 percent. Under such an approach, each member state could be required to bring a preset certain percentage of its annual volume to auction. This would provide assurance to all MSs that revenues from auctions are equalised. For instance if 500 million EUAs are to be auctioned on a common platform in one year, this should equate to approximately 10 million per week.

**Question 7** For futures auctions what should be the frequency?

Same as answer to question 5. The optimum arrangement is for the auctions to be held on a monthly basis on a common platform.

**Question 8** For futures auctions, what should be the auction size?

Same as answer to question 6. In the vast majority of cases, all auctions should have the same volumes. For instance if 500 million EUAs are to be auctioned on a common platform in one year, this should equate to approximately 10 million per week.

**Question 9** Should volumes of spot allowances be auctioned evenly throughout the year?

Yes, evenly - see answer to question 6.

**Question 10** In case futures are auctioned, should the volumes for spot and futures auctions be spread over the year in the same manner?

Yes. The proportion sold as futures should be as large as possible so as to allow generators to hedge their needs – therefore, the amount sold in futures auctions should be greater. That said, both spot and future amounts should be spread over the same manner.

**Question 11** Does the Regulation need to have provisions to avoid holding auctions during a short period of time before the surrendering date?

No (to both spot and futures) - just that the amounts auctioned are frequent and equal throughout the year. However, there may need to be some special provisions to deal with public holidays. To avoid MS-specific differences, the ECB holiday calendar should be used ([http://www.ecb.int/press/pr/date/2000/html/pr001214\\_4.en.html](http://www.ecb.int/press/pr/date/2000/html/pr001214_4.en.html)).

**Question 12** Which dates should be avoided?

Major holidays (as per ECB holiday schedule).

**Question 13** Is a harmonised 10-12 hrs CET auction slot desirable?

Yes

**Question 14** How long in advance should each element of the calendar be determined?

The key issue here is to get frequency and amounts pre-determined and set. This will provide sufficient certainty so that setting a calendar one year ahead is ok. Everything other than dates should ideally be set more than four years in advance (amounts, etc). Finally, there is no need to have to wait for a final confirmed emissions amount before auctioning can take place (e.g. 20% or 30% etc). The calendar should be binding to avoid political events.

In order to maximise predictability and allow agents to plan their activity, all relevant information (i.e. the calendar, the distribution of spot and futures, the dates of individual auctions, volume and product type for individual auctions and the auctioneers carrying out the auction process) should be known as much as possible in advance. This basic principle must apply to all the above mentioned elements and, in particular – to the type of auctions to be hold, the nature of products to be sold, the auctioneers that will exist – to minimise possible interferences with the process by Member States.

**Question 15** What should be the volume of allowances to be auctioned in 2011 and 2012?

See answers to question 1, 2 and 3 for our views on this. Over Phase 1 of the EU ETS, the combustion sector, which largely consists of electricity generators, emitted in the order of 1,400Mt of CO<sub>2</sub> p.a.

Assuming only half of EU generators follow a hedging strategy where they typically sell forward up to 80% of their electricity production one year in advance, up to 50% two years in advance and up to 10% three years in advance, then this leads to the following auctioning volume requirements ahead of 2013.

	2011	2012	Total
Allowances to hedge 2013 forward electricity sales, Mt	350	210	560
Allowances to hedge 2014 forward electricity sales, Mt	70	280	350
Allowances to hedge 2015 forward electricity sales, Mt	-	70	70
Total volume requirement	420	560	980

Consequently, around 1 billion allowances need to be auctioned ahead of 2013 to satisfy electricity generator hedging strategies and maintain liquidity in European power markets.

**Question 16** What should be the rule with respect to allowances not auctioned due to force majeure?

Firstly, any *force majeure* regime should be clearly-defined and codified in advance. Secondly – and regarding what happens if force majeure is called, any affected allowances should automatically be added to the next auction on the calendar, irrespective of the auction process (or the next three auctions in the case where auctions are held monthly and there is little time until the following auction post-*force majeure*). The impact which this will have will depend on the frequency of auctions i.e. the greater the volumes and time between auctions, the greater the disruptive effect.

### 2.3 Lot size

**Question 17** Is 1,000 allowances the most appropriate lot size? If not, why not?

Yes, as this is the standard lot size in the secondary market.

## 3. Auction design

### 3.1 Auction type

**Question 18** Is a single-round sealed-bid auction the most appropriate auction format for auctioning EU allowances?

Yes. As price discovery is not an issue (due to the secondary market), EDP fully favours the single-round sealed-bid approach. As opposed to a multi-period dynamic auction, this type of auction lowers transactions costs, preserves bidder anonymity, increases understanding of the price-formation process and helps avoid any possible collusion.

While in some industries the use of this auction-type could lead to what is known as the 'winner's curse' (i.e. where the winner bids too high), the existence of a functioning secondary market will provide bidders and sellers with a good reference price. In addition, as there will be many auctions in the ETS and an effective secondary market also exists, bidders do not face a one-shot game where there is only one chance to have a successful bid.

### 3.2 Clearing price

**Question 19** What is the most appropriate pricing rule for the auctioning of EU allowances? Please provide arguments to support your case.

Uniform-pricing is the most appropriate rule. This gives a clear price signal for the value of an EUA, thereby increasing predictability. It also ensures that every successful participant pays the same price, meaning that the auction price will be fair and minimises the risk of distorting the secondary market.

**Question 20** Should the rules for solving ties in the Regulation be:

- random selection; or
- pro-rata re-scaling of bids?

Please comment on your choice.

Pro-ration would seem fairer.

### 3.3 Reserve price

**Question 21** Should a reserve price apply?

No.

Firstly, auctioning serves as an alternative to distribute (allocate) allowances in the ETS market instead of grandfathering or benchmarking. That is the main goal of auctioning. Setting reserve prices may introduce the risk of ensuring government income or other

policy goals. As any *ad hoc* intervention would reduce predictability and distort investment signals, **there should be no intervention in the EUA market.** The greater the likelihood that intervention will occur, the greater the negative effect there will be on participants, and the higher the costs caused by subsequent risks created. Therefore, to preserve predictability, Member States and other relevant authorities should refrain from unduly intervening in the auction process *ex post* if the result is politically undesirable e.g. that prices rise or volatility increases. As such, no price floor or cap should be put in place.

Secondly, if market design is good, then there would be no need for a reserve price. Prices seen at auction would reflect fair market value as observed in the secondary market.

**Question 22** In case a reserve price would apply, should the methodology/formula for calculating it be kept secret? Please comment on your choice.

No. See answer to question 21 above.

However, any reserve price – **if imposed** – must be dynamically-linked to the secondary market price. To incentivise governments to use a good design, then the reserve price should be at a discount to secondary price. If such a reserve price was established, then it's formulation and application should be fully available to the public i.e. all methodologies/formulae must be published. Transparency is required to avoid gaming.

### 3.4 Maximum size of bids allowed from a single entity

**Question 23** Is a maximum bid-size per single entity desirable in a Uniform-price auction?

No. Since there is a liquid, open secondary market in place, there is no need to set restrictions on participants in the primary market. If there are adequate market abuse rules in place, then there is no need for a maximum bid size.

**Question 24** if yes to q23, what should be Bid size limit?

Does not apply; see answer 23.

**Question 25** In case only one of the two following options would be chosen, to limit the risk of market manipulation or collusion, which one would be preferable?

- A discriminatory-price auction format?
- A maximum bid-size per single entity?

Please comment on your choice.

Neither. Intervention is not necessary if secondary EUA markets function properly, as is currently the case. Only if there is market failure should a maximum bid-size be

imposed. Otherwise, the monitoring provisions contained in the regulation should be the main means used to ensure that manipulation does not take place.

## 4. How will the auction(s) be implemented?

### 4.1 Pre-registration of auction participants

#### **Question 26** Are the following pre-registration requirements appropriate and adequate?

Yes, most of the requirements listed are appropriate. However, we have some comments on the following item:

- *Intended auctioning activity*: we do not believe this is relevant if a participant has passed pre-qualification;

In addition, the requirement for '5-year declarations' timetables may need to be harmonised at Member State level before application. The nature of the 'Declarations' is probably too wide and vague. In order to be effective, 'Declarations' should relate to aspects that are relevant for the process in question and should have an objective and straightforward wording. Finally, the Regulation should provide for the possibility of applications being submitted in English only, regardless of the mother language of the Member State.

#### **Question 27** Do you agree that the pre-registration requirements for admittance to EU auctions should be harmonised throughout the EU?

Yes; harmonised requirements would ensure a level-playing field as well as access to any auction for any participant.

#### **Question 28** Should the amount of information to be supplied in order to satisfy the pre-registration requirements for admittance to EU auctions depend on the:

- means of establishing the trading relationship;
- identity of bidder;
- whether auctioning spot or futures;
- size of bid;
- means of payment and delivery;
- anything else? Please specify.

If so, what should the differences be?

We consider that the main difference on the amount of information to be supplied should consider whether it relates to auctioning spot or auctioning futures.

To auction futures the auctioneer will need to have more guarantees to minimise counterparty risk, thus implying that the amount of information should be more complete, exhaustive and complex than in spot auctions.

In case the requirements of information are different, the information to be supplied should probably also depend on its creditworthiness (rating).

**Question 29** Should the bidder pre-registration requirements under the Regulation apply in the same manner irrespective of whether or not the auctioneer is covered by the MiFID or AML rules?

Yes.

**Question 30** Do you agree that the auctioneer(s) should be allowed to rely on pre-registration checks carried out by reliable third parties?

Yes, given that these third parties comply with requirements as strict as those for auctioneers in order to guarantee harmonisation and coherence and equal treatment among different countries.

**Question 31** In order to facilitate bidder pre-registration in their home country, should the auctioneer(s) be allowed to provide for pre-registration by potential bidders in other (or all) Member States than the auctioneer's home country e.g. by outsourcing this to a reliable third party?

Yes, because the rules need to be harmonised. Ultimately, except for those restrictions highlighted in question 26, there should be no barriers to entry at Member State level. Ideally, there needs to be mutual recognition of pre-qualification agents. Where Member States do not trust or recognise one another's pre-qualification processes, the Commission should step-in to offer an EU-wide level prequalification option, thereby transcending any inter-member state trust issues.

If so, should such entities be:

- Covered by the AML rules?
- Covered by MiFID?
- Covered by both?
- Other? Please specify

Please comment on your choice.

The regulation should not deal with these matters since they are already covered in existing legislation.

**Question 32** Should the Regulation prohibit the multiplicity of pre-registration checks in the case of Member States auctioning jointly? Please comment on your choice.

Yes. See answer to question 31 above for reasoning.

## 4.2 Guarantees and financial assurances – so-called collateral

### 4.2.1 The need for harmonisation of collateral measures

**Question 33** Do you agree that the level of collateral accepted in EUA auctions should be harmonised for all EU ETS auctions? If so, how should they be harmonised?

Yes – in line with rules which apply in the secondary market. This is required to avoid distorting the electricity market.

**Question 34** Do you agree that the type of collateral accepted in EUA auctions should be harmonised for all EU ETS auctions? If so, how should they be harmonised?

Yes if proportionate. Collateral needs to be easily-tradable, liquid etc.

#### 4.2.2 Collateral in spot auctions

**Question 35** Do you agree that 100% collateral in electronic money transfer ought to be deposited up-front at a central counterparty or credit institution designated by the auctioneer to access spot auctions?

This is not necessary for spot auctions. Therefore, there should be no obligation to provide collateral for spot transactions. If one defaults, then there should be some form of participation deterrent, but no collateral obligation. Quantities unsold can be transferred to next auction. In a word, spot is less risky.

If not, why not? What alternative(s) would you suggest? Please provide arguments to support your case.

Not applicable.

#### 4.2.3 Collateral in futures auctions

**Question 36** In case futures are auctioned, should a clearing house be involved to mitigate credit and market risks?

Yes – clearing houses are an essential part of futures regime.

The use of clearing houses is an absolute must. Besides the fact that it mitigates credit and market risks it also simplifies the whole administrative process and reduces costs (risk/reward opportunity cost). The applicable rules should not be much different from the ones used in other similar exchanges which have already proven their resiliency and are very well known by the bidders.

If so, should specific rules – other than those currently used in exchange clearing houses – apply to:

- the level of the initial margin;
- the level of variation margin calls;
- the daily frequency of variation margin call payments?

If you have answered yes, please justify and elaborate on the rules that should apply and the mechanisms to implement them.

All the above are standard requirements so there is no need for further elaboration.

### 4.3 Payment and delivery

**Question 37** What are the most preferable payment and delivery procedures that should be implemented for auctioning EUAs?

- Payment before delivery.
- Delivery versus payment.
- Both.

Please comment on your choice.

As per the prevailing 'norms' in the secondary market – i.e. payment after delivery.

**Question 38** Irrespective of the payment procedure, should the Regulation fix a maximum delay of time for payment and delivery to take place? If yes; what should it be?

- 4 working days [ ]
- 5 working days [ ]
- 6 working days [ ]
- 7 working days [ ]
- Other, please specify.

Yes, 4 working days as a maximum.

#### 4.3.2 Handling of payment and delivery failures

**Question 39** Should the Regulation provide any specific provisions for the handling of payment and delivery incidents or failures? If yes, what should they be?

As per norms in secondary market.

### 4.4 Transaction rules under the Regulation

**Question 40** Should the Regulation provide for all matters that are central to the very creation, existence and termination or frustration of the transaction arising from the EUA auctions? If not, why not?

Yes

If so, are the matters enumerated below complete?

- The designation of the parties' to the trade.
- The characteristics of the auctioned product:

- Nature: EUAs or EUAAs, trading period concerned.
- Date of delivery: date at which winning bidders will receive the allowances on their registry account.
- Date of payment: date at which payment will be required from winning bidders.
- Lot size: number of allowances associated with one unit of the auctioned good.
- Events of 'force majeure' and resulting consequences.
- Events of default by the auctioneer and/or the bidder and their consequences.
- Applicable remedies or penalties.
- The regime governing the judicial review of claims across the EU.

If not, what additional matters should be foreseen in the Regulation and why?

Yes. The secondary markets already have similar rules in place. EDP's view is that these secondary rules should apply. This is the most effective way to assure the required harmonisation across all Member States and the future existence of a common EU 'level playing field'.

**Question 41** Should the Regulation provide for rules on jurisdiction and the mutual recognition and enforcement of judgments?

Yes.

If so, should these be:

- specific to the Regulation;
- by reference to the Brussels I Regulation;
- by citing exceptions from the Brussels I Regulation;
- by citing additions to the Brussels I Regulation?

'By reference to the Brussels I Regulation'.

#### 4.5 Facilitating cost effective participation in EU auctions

**Question 42** Which auction model is preferable?

- Direct bidding?
- Indirect bidding?
- Both?

Both

EDP strongly believes that, subject only to a requirement to demonstrate creditworthiness and provide financial assurance any party should be allowed to participate in an auction. This may be done and demanded to agents acting in the name of others, assuming the former the obligation to demonstrate the creditworthiness and financial assurance. Any further restrictions on participation should be clearly objective, and must not be based on nationality and/or on firm type or size. Therefore, **there should be no requirement to use intermediaries, but these should be allowed as the costs associated to direct auction participation (including**

**organisational costs) might be an obstacle to smaller agents..** Therefore we are firmly against any model which limits access solely to primary participants.

Concerning prequalification, in order to assure credit worthiness of bidders, any bid received above the credit or financial allowance of the bidding party could be disqualified. If doubts remain, the Commission should introduce a system where there is a requirement on bidders to make declarations of 'Beneficial Ownership'. A declaration of 'Beneficial Ownership' could mean that every participant would have to disclose the party sponsoring or benefiting from the agent's activities in the allowance market if it was other than themselves or their immediate employer. Disclosure would be to the relevant authority and not the market – this information should be kept confidential.

Moreover, we believe that any bid made should be considered a binding contract. Therefore, successful bidders need to meet certain payment timelines – proportionate penalties for non-compliance would assist in this. Proportionate deposits are another option. On the seller side, timelines need to be established for the auction administrator/Member State to transfer EUAs to the purchasers registry account.

**Question 43** If an indirect model is used, what share of the total volume of EU allowances could be auctioned through indirect bidding? Please provide arguments to support your case.

No. As EDP does not support the obligatory use of intermediaries, then there should be no *ex ante* split or reservation of volumes between direct and indirect bidding pools. Use of intermediaries should be for market participants/emitters to decide. See answers to question 42 and 44.

**Question 44** If the primary participants model is used, what provisions would be desirable for mitigating disadvantages of restricting direct access (more than one answer is possible):

EDP strongly opposes the 'primary participants' model (See answer to question 42). For electricity generators, there is no need for a 'middle-man' where an emitter has the means and expertise required to participate directly in auctions. Conversely, the imposition of a primary participants model risks compromising the aim of making EUA auctions accessible to as many participants as possible at least cost. This is completely unnecessary.

The only conceivable 'benefit' of a primary participants model is that it could possibly make oversight easier. However such a 'benefit' is removed where a robust prequalification system is in place. Such a system could cover credit-worthiness of bidders, beneficial use of EUAs and the enforceability of contract terms and conditions:

- In order to assure **credit worthiness of bidders**, any bid received above the credit or financial allowance of the bidding party could be disqualified.
- If doubts remain, the Commission should introduce a system where there is a requirement on bidders to make declarations of '**beneficial ownership**'. A declaration of 'Beneficial Ownership' could mean that every participant would have to disclose the party sponsoring or benefiting from the agent's activities in the allowance market if it was other than themselves or their immediate employer.

Disclosure would be to the relevant authority and not the market – this information should be kept confidential.

- Moreover, we believe that any bid made should be considered a **binding contract**. Therefore, successful bidders need to meet certain payment timelines – proportionate penalties for non-compliance would assist in this. Proportionate deposits are another option. On the seller's side, timelines need to be established for the auction administrator/Member State to transfer EUAs to the purchasers registry account.

**Question 45** If the primary participants' model is used, what conflict of interest requirements should be imposed? (more than one answer possible)

See answer to question 44.

**Question 46** What obligations should apply to primary participants acting in EU-wide auctions as:

- Intermediaries?
- Market makers?

See answer to question 44.

**Question 47** Under what conditions should auctioning through exchanges be allowed (more than one answer possible):

- Only for futures auctions open to established members of the exchange?
- Also for spot auctions open to established members of the exchange?
- Only when the exchange-based auction is open to non-established members on a non-discriminatory cost-effective basis?
- Other? Please specify.

Please provide arguments to support your case.

Exchanges should at least be members of a clearing house. That said; market participants should be able to choose exchange.

What is crucial is that bidders have a contractual relationship with the exchange.

**Question 48** Should direct auctions through:

- third party service providers; or
- public authorities

be allowed?

Yes, preferably through third party service providers (i.e. exchanges) subject to the condition that rules are common, that access is open to all participants and that competency is demonstrable. This would reduce costs and would facilitate early auctioning.

## 4.6 Ensuring full, fair and equitable access to SMEs and small emitters

**Question 49** Do the general rules for auctioning EUAs suffice for ensuring full, fair and equitable access to allowances to SMEs covered by the EU ETS and small emitters? If not, why not?

Fair and impartial rules applying equally to all emitters should be put in place. Smaller emitters will have easy access where access to the market is non-discriminatory, where lot sizes are small (i.e. 1,000) and where there is a liquid secondary market in place. This means that SMEs have access to the auctions via an appropriate mechanism.

**Question 50** Is allowing non-competitive bids necessary for ensuring access to allowances to SMEs covered by the EU ETS and small emitters in case of:

- discriminatory-price auctions?
- uniform-price auctions?

A simple (uniform) sealed-bid format will allow simple access for SMEs, using intermediaries where optimal. Therefore, there is no need for non-competitive bidding.

**Question 51** If non-competitive bids are provided for in spot auctions, what maximum share of allowances could be allocated through this route?

We do not believe that non-competitive bidding is necessary where lot-sizes are small, functioning secondary markets are in place, participation is not restricted and EUAs are transparently auctioned in a simple, regular, co-ordinated manner. In any case, experience with existing regimes which allow for non-competitive bidding indicates that such bidding means may not be used (e.g. current Austrian system).

**Question 52** What rule should apply for accessing non-competitive bids (more than one answer possible):

We do not believe that non-competitive bidding is necessary where lot-sizes are small, functioning secondary markets are in place, participation is not restricted and EUAs are transparently auctioned in a simple, regular, co-ordinated manner. In any case, experience with existing regimes which allow for non-competitive bidding indicates that such bidding means may not be used (e.g. current Austrian system).

**Question 53** What should be the maximum bid-size allowed for SMEs covered by the EU ETS and small emitters submitting non-competitive bids?

We do not believe that non-competitive bidding is necessary where lot-sizes are small, functioning secondary markets are in place, participation is not restricted and EUAs are transparently auctioned in a simple, regular, co-ordinated manner. In any case, experience with existing regimes which allow for non-competitive bidding indicates that such bidding means may not be used (e.g. current Austrian system).

**Question 54** Are there any other specific measures not mentioned in this consultation that may be necessary for ensuring full, fair and equitable access to allowances for SMEs covered by the EU ETS and small emitters? If so, please specify.

In addition to the need for a simple auction design, we believe that transparency is very important.

## 4.7 Auction information disclosure

### 4.7.1 Pre-auction information disclosure

**Question 55** What should be the minimum period of time before the auction date for the release of the notice to auction? 2 weeks  1 month  2 months  Other  Please specify. Please comment on your proposal.

2 months or more - preferably in line with the auction calendar. Full transparency means that participants should have as much preparation time as possible. Any unplanned changes should be published immediately.

**Question 56** What should be the minimum period of time before the auction date for the submission of the intention to bid?  
1 week  2 weeks  1 month  Other  Please specify.  
Please comment on your proposal.

In our opinion the announcement of an intention to bid should not be needed. If the registration process is completed and the company is authorized to participate in the auctions, it will have to be free to decide if they want to participate or not in the auction, and no communication should be required before the auction day.

However, if this is seen as needed **it should not involve any costs, should not be binding, and might be done** 1 week before the auction bid date

**Question 57** Are there any specific provisions that need to be highlighted in:

- The notice to auction?
- The intention to bid?
- Both?

Please specify what they are.

The auction rules applying would need to be clearly presented (including any restrictions). The notice should also say when results will be released. Of course, all the processes should be public and accessible through webs, phone, information documents etc.

## 4.7.2 Post-auction information disclosure

### Question 58 What information should be disclosed after the auction?

- Clearing price (if allowances are awarded on a uniform-price basis or in the case of non-competitive bids being allowed)
- Any relevant information to solve tied bids
- Total volume of EUAs auctioned
- Total volume of bids submitted distinguishing between competitive and non-competitive bids (if applicable)
- Total volume of allowances allocated?

Anything else? Please specify.

- Number of successful participants; Total amount unsold and carried over to next auction; Number of participants (total); The aggregated supply and demand curve

### Question 59 What should be the maximum delay for the announcement of auction results?

5 minutes  15 minutes  30 minutes  1 hour

Other  Please specify. Please comment on your proposal.

Five minutes. The closer to the event the better, as this will affect the secondary market.

### Question 60 Do you feel that any specific additional provisions should be adopted in the Regulation for the granting of fair and equal access to auction information?

If so, what may they be?

Provided that information is not commercially-sensitive, all information should be provided at the same time, according to a standardised format. There should be a prohibition on any unauthorised discriminatory release of information. Furthermore, all information should be put on one single website.

## 4.8 Auction monitoring and reporting

### Question 61 Should an auction monitor be appointed centrally to monitor all EU auctions?

Yes.

Given the large number of participants, the holding of relatively frequent, fully open auctions should preclude the ability of any purchasing party to influence EUA auctions. In addition, a well-functioning secondary market will strongly reduce the influence the

impact any one party would have on the market. Therefore, an EU-wide monitoring body is not strictly necessary where the secondary market works well.

Nevertheless, given the financial consequences of improper conduct, the introduction of adequate supervision and transparency measures are needed. As such, provisions should be made (with appropriate penalties) to govern the release of such information by authorities and the Commission.

As such, EDP considers it appropriate to have in place a mechanism to monitor the effectiveness of auctions and the performance of the market with a view to identifying opportunities to improve its efficiency. In terms of who does this, EDP believes that the relevant body responsible for monitoring – EU or national - needs to be independent of the beneficiary (i.e. MS Treasuries), of buyers (e.g. energy market participants and financial institutions) and of authorities who are tasked with the achievement of other potentially conflicting objectives (e.g. energy regulators).

**Question 62** Do you agree that the Regulation should contain general principles on:

- the designation and mandate of the auction monitor; and
- cooperation between the auctioneer(s) and the auction monitor?

Should these be supplemented by operational guidance, possibly through Commission guidelines?

Yes to all the above suggestions. We believe that the auctioneer and monitor roles must be separated.

#### 4.9 Preventing anti-competitive behaviour and/or market abuse

**Question 63** Is there a need for harmonised market abuse provisions in the Regulation to prevent insider dealing and market manipulation? If not, why not?

Please comment on your choice outlining the provisions you deem necessary and stating the reasons why.

Internal and external discussions are currently ongoing within the Commission regarding the desirability of having an energy-specific market-abuse regime. Such a regime will also cover CO<sub>2</sub>.

As EDP supports the development of such a regime, we do not believe that issues to be dealt with under this regime should also be dealt with in the EUA regulation. We do not want an overlap of these rules.

#### 4.10 Enforcement of the provisions of the Regulation

**Question 64** Should the Regulation provide for harmonised enforcement measures to sanction?

- Non-compliance with its provisions?

- Market abuse?

Please provide arguments to support your case.

Regarding enforcement, there are two groups which rules need to apply to:- Member States (and possibly the auctioneers acting on their behalf) on the one hand, and bidders in the auction on the other.

Non-compliance with its provisions will most likely be due to Member States actions. Looking at the history of compliance by Member States with the provisions in the ETS directive over the past years, one can easily remark that only a very few of them have met, for instance, required deadlines on time. In addition, they have sought to use creativity in designing Allocation Plans and applying rules. The Commission has few measures (except going to the Court in Luxemburg) at its disposal to correct this behaviour.

For a timely and harmonised organisation of auctions, enforcement at EU level seems inevitable looking at the track record of Member States. Oversight should also ensure that volumes are always brought to the market by Member States according to schedule and not withheld in order to drive prices up or wait for "better" moments.

Any rules which apply should be enforced with equal weight. Only then will a level-playing field exist.

**Question 65** Should the enforcement measures include?

- The suspension of the auctioneer(s) and/or bidders from the EU-wide auctions? If so, for how long should such suspension last?
- Financial penalties? If so, at what level should such penalties be fixed?
- The power to address binding interim decisions to the auctioneer(s) and/or bidders to avert any urgent, imminent threat of breach of the Regulation with likely irreversible adverse consequences?
- Anything else? Please specify. Please provide arguments to support your case.

We do not support the first bullet point proposal. We would propose that if no auctioning takes place, then allowances should be transferred to other auctioneers.

**Question 66** Should such enforcement measures apply at:

- EU level?
- National level?
- Both?

Please comment on your choice.

EU-level. See answer to question 64.

**Question 67** Who should enforce compliance with the Regulation (more than one answer is possible):

- The auction monitor?
- The auctioneer?
- A competent authority at EU level?
- A competent authority at national level?

- Other? Please specify  
Please provide evidence to support your case.

A competent authority, either at EU level, with the auctioneer (exchanges/brokers if different from authority) being the front-line compliance monitor.

## 5. Who auctions? Auction processes and auctioneer(s)

### 5.1 Overall model for EU ETS auctioning system

**Question 68** Which of the three approaches for an overall EU auction model do you prefer? Please rate the options below (1 being the most preferable, 3 being the least preferable)

- Limited number of coordinated auction processes. [ ]
- Full centralisation based on a single EU-wide auction process. [ ]
- The hybrid approach where different auction processes are cleared through a centralised system. [ ]

Please give arguments to support your case.

Ideally, EDP is strongly in favour of a centralised system.

However, recognising political reality in the EU, we are leaning towards some form of hybrid system with bids cleared centrally. The hybrid approach combines the benefits of a central bid book giving a single EU-wide auctioning price (which fits seamlessly with ETS and the secondary market) and easier harmonisation with the possibility given to Member States in the ETS directive to set up auctions. The use of a central bidbook resulting in a single price not only benefits the market, but has also benefits for Member States, since they all receive the same price for their allowances. This clearly avoids tensions or competition between Member States and thereby adds to the regulatory stability of the approach.

That said, the hybrid approach would only really be a good first approach provided that it could grow into a centralised approach as soon as possible.

EDP strongly opposes an auctioning scheme in which all 27 Member States run auctions individually. To have effective auctions with minimal differences, extensive harmonisation of rules within the Regulation would be required and enforcement at EU level to ensure proper execution by Member States. However, some aspects would be rather difficult to achieve. If Member States all run their own auction, political difficulties may arise for smaller Member States who will not be able to run frequent auctions throughout the year because of their small volume. They have larger risks that their auctions are held in periods with "lower" prices. One can imagine that this could translate into a dispute at EU level or into ways to avoid such "losses". This would undermine the stability of the system.

**Overall our strong preference is for a "fully-centralised auction" based on a single EU-wide auction process.** The hybrid option, as proposed, would very much be a "second best". In any case a centralized clearing would be required. There is no need to reinvent to wheel here - existing "Carbon Exchanges" could act as aggregators.

**Question 69** If a limited number of coordinated auction processes develops, what should be the maximum number?

- 2
- 3
- 5
- 7

- more than 7, please specify.

Please give arguments to support your case.

If necessary, as few processes as possible!

**Question 70** Is there a need for a transitional phase in order to develop gradually the optimal auction infrastructure? If so, what kind of transitional arrangements would you recommend?

As the market evolves and as confidence develops, it may actually be possible to remove some of the initial rules. However, the overarching objective aim should be to get the rules right the first time. If the Commission is not confident that EUA auctioning processes will function properly in all instances, then the fall-back option should be for a simple issuance of EUAs into the market, as is done in Germany at present.

## 5.2 Key requirements for the auctioneer(s) and auction processes

**Question 71** Should the Regulation impose the following requirements for the auctioneer(s) and auction processes?

All the above items make for an almost fully-comprehensive list. However, in our opinion, provisions to cover the following items should also be included:

- Auctioneers should not be able to purchase in the auction – MSs should **not** be able to buy;
- Credit rating for auctioneers (if not state entities) should be high so as to cover delivery risk.

## 5.3 Administrative fees

**Question 72** What provisions on administrative fees should the Regulation include (more than one answer is possible)?

- General principles on proportionality, fairness and non-discrimination.
- Rules on fee structure.
- Rules on the amount of admissible fees.
- Other, please specify.

A rule needs to be included stating that fees have to be recovered from EUA auction proceeds.

Please provide arguments to support your case.

As the authority in charge of the auction will have a monopoly over auctioning, there needs to be some safeguard in place to ensure that participants (and hence customers) are not over-charged. The best way of doing this is for auctions running costs to be paid out of the auction proceeds.

## 5.4 How to ensure appropriate and timely preparation of auctions?

**Question 73** Should there be provisions for public disclosure of material steps when introducing new (or adapted) auction processes? Should new (or adapted) auction process be notified to and authorised by the Commission before inclusion in the auction calendar?

Yes. However this should not be necessary if rules are harmonised. Furthermore, proper consultation with market participants is also required.

**Question 74** Which one of the following options is the most appropriate in case a Member State does not hold auctions (on time)?

- Auctions by an auctioneer authorised by the Commission.
- Automatic addition of the delayed quantities to those foreseen for the next two or three auctions.

What other option would you envisage? Please specify.

EDP's view in this instance is that the allowances should be released to the market with immediate effect, perhaps by an auctioneer on behalf of Commission.

**Question 75** Should a sanction apply to a Member State that does not auction allowances in line with its commitments? If so, what form should that sanction take?

See answer to question 74 above. Such a sanction mechanism should take the form of financial penalties for Member States.