Nord Pool Comments on ‘Non-paper on Emergency Electricity Market Interventions’

As a leading European power market, Nord Pool would like to share some initial comments on the proposal to introduce a ‘price cap for inframarginal technologies for the benefit of consumers’ included in the European Commission’s Non-paper on Emergency Electricity Market Interventions.

We appreciate that the Commission is keen to retain the main principles of the current coupled markets design. It is reassuring that, in its non-paper, the Commission rules out some of the most disruptive mechanisms proposed or implemented at national level so far; such as a full market suspension, the introduction of an absolute ceiling or the EU-wide introduction of the Iberian and Greek measures. We support measures aimed at reducing consumption without adverse impacts on the market in order to ease the restricted supply situation that we are currently witnessing.

With regards to the proposal on the inframarginal cap, the Commission itself has indicated at least two potentially negative effects:

1) on ‘the trading behaviour of market participants, who may seek to avoid their trading activity being subject to a price cap by simply shifting their trading activities from the organised day-ahead market towards another market, e.g. OTC, intraday’ and

2) by encouraging generators to withhold capacity or ‘blocking potential new entry technologies’

Nord Pool is extremely concerned about these potential effects and urges the Commission to implement measures to prevent both from materialising.

If the inframarginal price cap is agreed, the Commission and Member States should also consider that not all electricity generators/producers benefit from high spot prices. Some generators/producers will only be minimally able to recover such a day-ahead price.

This is because it is normal practice for generators/producers of all kinds to forward hedge their output or enter PPAs. To the extent generators/producers have done so, they will not actually receive the day-ahead marginal price, but the fixed pre-agreed price. These are the same generators/producers already in distress due to facing enormous collateral calls to continue to participate in both the forward and spot market timeframes.

If a cap is not properly designed, there is a risk that generators/producers will incur a double penalty: the claw-back of profits in excess of the inframarginal price cap and the elevated costs of collateral.

Any inframarginal price cap, if implemented, should not be applied to any previous forward hedging / PPA / OTC contracts that the relevant generators/producers already performed and which bind them to receiving a price that is substantially lower than that of the current spot market prices. In addition, only profits above the price cap attributable to what such relevant generators/producers have not already
forward hedged, would be subject to being clawed back. The magnitude of forward hedged volumes will vary from business to business, depending on their hedging strategies.

It is critical to note that participation in day-ahead markets extends beyond generators/producers. It includes suppliers (some of whom will be in a corporate group with one or more generators/producers), traders and end-users. We assume that all day-ahead trading activity by all such participants with respect to the output that can be attributed to inframarginal plant, will be subject to the relevant price cap.

The claw-back should only be applied to the output of plants that meet both these conditions:

1. The electricity output must be attributable to an inframarginal plant;
2. The concerned output has not been hedged at prices that are substantially below SDAC prices. The definition of ‘substantially’ would need to be assessed.

We believe identifying such volumes would be a difficult and cumbersome process for any competent authority charged with performing the task. It could only be performed by an entity with access to all plant generation (i.e. metering, output) data.

The only other alternative would be for very broad and imprecise assumptions to be applied concerning how much of market participants’ traded volumes should be attributable to inframarginal plant, capping the prices of such volumes accordingly. This would clearly be an extremely blunt instrument.

On the positive side, Nord Pool believes it can be possible to implement an inframarginal cap with a well-designed portfolio bidding structure, without having to resort to unit bidding. Nord Pool would be glad to provide further input on options for portfolio design should the Commission’s proposal be adopted. For example, we could provide input on how volumes subject to the particular price caps could be efficiently identified.

If a cap is implemented, we recommend that it is calculated based on well-defined criteria founded on hard data, rather than on broad and imprecise assumptions, to ensure correct and consistent capture of appropriate inframarginal profits.

Nord Pool would also be glad to discuss potential proposals that require NEMOs to perform tasks related to the operation of the cap, such as the identification of the output volumes subject to it.

**In conclusion:**

Any measures should be limited in time, as proposed by the European Commission, with automatic triggers to disapply them when specific market conditions are met.
We firmly believe the current market design based on marginal pricing remains the most efficient means to allocate resources and provide the correct price signals to foster the green transition and economic efficiency.

By submitting these comments, Nord Pool is not in any way, endorsing proposals to implement an inframarginal price cap. Our input is intended only to share our initial thinking.