

INDIVIDUAL PROFILE

ALBERTO POTOTSCHNIG

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IS THE FUTURE NOW?

This interview is based on an original recording for the Energy and Innovation podcast focusing on changes within the energy system. Each expert demonstrates both an in-depth understanding of their core area and also a broader vision of how the energy system changes. The material is useful for both teaching and research. It was created as part of a case study project of the Jean Monnet Chair in Energy and Innovation Strategy at Central European University.



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BY PROFESSOR MICHAEL LABELLE

Alberto Pototschnig is the director of the agency for the cooperation of energy regulators or ACER for short. Alberto has been the director for the past eight years. ACER is an agency reporting directly to the European Commission. It was launched in 2011 and is based in Ljubljana, Slovenia.

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What's it been like to be the founding director and serving ACER these past eight years?

Well, it has been a very exciting experience and a very rewarding one. It was very exciting to set up a new agency in a new place. Slovenia never had a European agency before, to recruit the staff to try to set up a team and to try to start working or contributing towards the integration of the internal energy market. Trying to create competition trying to deliver benefits to final consumers, because at the end of the day, the internal energy market, it is about benefit to consumers. And I have to say that after eight years, we're seeing these benefits actually being accrued to consumers and being delivered to consumers.

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When we think of the European Union and we think of ACER, these things can be quite removed from the everyday household in the EU. How did you shape the direction and the tasks of ACER to address those? To make it not so removed from the average consumer.

Well, indeed, when you are trying to integrate wholesale markets, or you're working on what I would call horizontal networks, the kind of networks that allow energy to be shipped from one country to another, you might feel that you're a bit detached to consumers. But then at the end, you see the kind of benefits, that kind of increase efficiency that you're able to achieve in the rate of billions of Euros per year. And then these savings actually delivered to consumer through better prices, greater choice and prices that reflect the fundamentals rather than being potentially manipulated or distorted by abusive behavior. So I think yes, we're not talking to consumers, for these national regulators are still in the front line, but we're still delivering benefits to them.

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One of the key messages that the agency has been putting out is really how much consumers can save on their bills through market integration. Is that one of the main messages you have trying to get out?

Well, this is where we're trying to reach out to consumers because as said most of our work has to do with wholesale markets and high tech, high voltage, and high-pressure transmission networks. When you talk to a consumer, you have to indicate what the benefits are for them. And for example, we've estimated that by introducing market coupling in the day ahead electricity market, we have already saved them around a billion Euros per year. And probably there is another quarter of a billion out for grabs. And by improving the efficiency in which the gas network is actually used, we can deliver up to 400 million euros per year to consumer. So these are fairly significant numbers. I mean, okay, if you look at them in respect to the total energy bill of European energy consumers then obviously this is 0.000 percentage. But you know, the difference between having a billion not having a billion is still a billion. And people appreciate that.

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Could you talk about joining the national markets in detail and whether there was resistance to this or not?

Indeed, some of these projects started in a pilot phase well before the agency was established. In fact, I think you can sort of date back to sort of 2003, 2006 where some of these ideas started to develop. But then it was exactly you know the experience from these pilot projects that showed the need to have a more European-wide approach to regulation. If you aim at establishing a European wide market over 28 more jurisdictions, then it's very difficult to see how you can develop the rules just by voluntary cooperation of national regulatory authority. So the agency was established with its main mission to assist national regulatory authorities to perform at European level, their regulatory functions and to coordinate their action whenever necessary. I mean, that was the main focus of the agency, at least in its initial period. And one of the activities on which this developed was the creation, the development of European wide rules, where the agency took a prominent role in developing the sort of the framework guidelines and the Network Codes. The Network Codes are the European rules for the operation of markets and systems, electricity producing gas market and systems. And these would have not been possible or would have probably taken a lot longer if the agency and the similar body on the transmission system operator side didn't exist. So I think this is, a sense, was the focus of the agency, at least in these five initial five years.

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Has ACER been able to build up and help give the National Energy regulators more competencies to oversee the whole energy sector and engage more professionally in that?

Well, I think that for sure, the agency contributed to the sharing of good practices or practices among the regulators. Companies have actually been given by the legislative packages and by the transposition of the packages into national legislation. So there, I cannot claim the agency played a role but obviously once the national regulators were established and were given competencies, we made sure that the practice that is developing in one country is available in another country. And in fact, this is one of the roles that the agency has played over these years— the sharing of best practices or good practices. So, this is one aspect. The other aspect I think, is the bringing together the European dimension and the national dimension, because obviously, you want to have European rules, European-wide rules, but on the other hand, you want rules which are applicable and suitable for the different national circumstances. And that's where I think the interaction between the agency and national regulators has been particularly helpful and valuable. National regulators are part of the decision-making process of the agency. They are members of what we have as a board of regulators. So we work together with them in trying to shape market rules and system rules, which are both suitable for integrating the market. But also applicable in each and every national member, national state and national markets. Obviously, some of these markets will have and have had to change in order to integrate better with the neighboring markets. But this was done in a way which was consistent with the starting points.



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So it's a quite a challenge to take than the EU directives at the higher level and match those and work with the national legislation and at the national level, and getting alignment there in the energy sector. And do you think moving forward then how effective can ACER be in integrating national gas markets, for example?

Well, I think now we're at a turning point, and the Commission has recognized this by launching at the end of 2016 a new legislative initiative the Clean Energy Package for all Europeans are Clean Energy for All European Package. That package is trying to move one step—the energy sector—one step further. It mainly focuses on electricity. But then the idea is that a new package would be launched by the new Commission on gas, probably in 2020. So at the moment, the Commission has a quite an ambitious program. Obviously, there is some resistance in some Member States because this will be the decisive move towards a well-functioning and fully integrated internal energy market with more responsibility to move from national level to European level. But so, yes, the integration process is progressing. And I think we can really claim that a large part of the benefits have been delivered, at least in the day ahead market for electricity. We still have the challenge of improving the way in which infrastructure is actually used that actually is, at the moment, our main focus in the electricity sector. The gas sector at the moment is working quite well. Also, partly because of the reduction in the gas flows in European networks. Congestion is actually much less than it used to be a few years ago. But there again, there is the opportunity to integrate the two, you know, the gas market more and also something that we just started to discuss also to somehow capital, the electricity and the gas sector and probably other sectors as well, in order to take advantage of the potential synergies between these two sectors in the other sectors as well. So I think we are at a critical time when the large part of the work has been done, but now we move into that sort of next stage of trying to improve the way in which the market is working.

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You mentioned a coupling of the national gas and electricity markets together. Is that based on new technology, or how could that work?

Well, this at the moment have to say it's probably a little more than a slogan here or at least you know, a title of a chapter to be filled in. For sure, there are new technologies that will allow this to happen. It will probably also involve some sort of market design changes. I just give an example which is probably the most trivial one. The going forward with an increasing share of renewables in the electricity market, the electricity system would need to have much more flexibility and one of the resources providing flexibility, at least in the medium term, could be the gas-based production. Which means that not gas, but base power production wouldn't need to itself become more flexible, and that may be promoted by a more flexible gas market. And then you can think of a gas fired power station providing flexibility in the electricity market, but also wanting to buy gas according to what its position in the electricity market it could be. And here is where, you know, you can think of somehow coupling the two markets, you can think of, for example, the operator of a gas fired power station be able to submit conditional bids in one market with respect to the outcome of the other market and vice versa. It reminds me a bit of what we faced probably 15 years ago when cross border electricity capacity was actually auctioned separately from the commodity from energy through explicit auctions. And at that time there was the problem or the potential inefficiency caused by the sub optimal coordination of the positioning of market players in the electricity market in the cross border capacity market. So, and then with implicit auctions, we try to remove this possible inefficiency and try to create you know, by construction, a combination of commodity and capacity. Here is not a combination of commodity and capacity, but it's a combination an efficient combination of the position of, for example, a gas power plant operator on the short-term gas market and in the short term electricity market. So, this is maybe the trivial one, but you know, there may be several examples like this, where, you know, technology would now allow a greater coordination The greatest synergies between these two markets and probably others, such as heating and cooling along with electromobility. I mean, there are things to be considered. And this will probably be what is necessary in the future to face and to address the challenges of a greater penetration of renewables, at least in the electricity system.

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So just as in market coupling then where the electricity and gas traders for examples wouldn't have to bid on the capacity to move the electricity or gas from one national market to another. They would actually be able to do this jointly. Together, is that right?

Indeed, exactly. And what is obvious today, in terms of the benefit of market coupling was not necessarily obvious 15 years ago. So there has been a lot of learning along the way. And, you know, it's now a pretty, you know, no one would dispute the benefits. So maybe we're going through the same process now. The next stage in trying to reap the benefits and further efficiency in the wider energy market where we bring together electricity gas. And as I mentioned, also possibly other sectors.

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So this goes to one of the core competencies then of ACER and market monitoring. And I wonder if you could talk a bit about REMIT. Since this has been in place and how this has progressed over time, and how do you see it over a long period or short period and the function that ACER plays in market monitoring?

Yeah, just before I go to REMIT, let me just clarify, this is something that we're starting to think for the future until we get there we need to deal with the you know, the immediate priorities, which is for example, try to make sure that Europe has sufficient energy supply security, that this is achieved at least cost. So there are other dimension that we know we need to tackle beforehand, but you know, from between now and 10 years from now, I think, you know, market coupling sector coupling will also become a priority.

In terms of REMIT, REMIT was a totally new chapter assigned to the agency because, you know, the agency was initially tasked mostly with what are called traditional regulatory functions and REMIT the regulation or wholesale energy market integrity and transparency is about market supervision, ensuring that trading in energy products for delivering the union does not involve market abuse in the form of market manipulation, attempted market manipulation or insider trading. So completely new task requiring in fact completely new responsibilities and new expertise. So that's what the agency was tasked in 2011. It took a bit longer than expected to put it in place also because the implementing regulation, the one defining the details of the operation of REMIT, was only issued late in 2014 and came into force in 2015. So we've been collecting data for markets surveying purposes only since late 2015.

So over the last couple of years, the idea of REMIT is to collect information on every single transaction or orders to trade entered into or executed in Europe on energy products for deliveries in Europe, for delivery in European Union, and at the moment the agency receives around 2 million records of transactions of ordered two trades per day, so at a rate of 50 to 60 million per month. Now when we receive this, we look into them, we see whether there is any anomalous pattern anomalous instances, which may indicate the presence of market abuse. And we developed an automatic screening obviously we cannot look at 2 million data point today. And our system at the moment returns around four or five, six thousand anomalous instances per month. These are then locked by my colleague in the markets, surveillance and conduct team. They prioritize because at the moment we do not have resources to look at all all the anomalous instances. So we have a further prioritization and around 1000 instances actually manually assessed to see whether they are just strange instances but perfectly legitimate, or whether there is something suspicious there. And out of this work, at the moment, we notify around 50 to 80 suspected instances at that point to national regulatory authorities for investigation and enforcement.



So we start from sort of 50 to 60 millions of transactions in order to trade reported to the agency every month. And we end up with notifying 50 to 80 suspicious instances to national regulatory authorities. And then they will investigate and if necessary, enforce.

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Is it like a huge funnel that it goes through?

It is. And well, that's the only I mean, as far as we know, is unprecedented worldwide. I mean, FERC in the US has been sort of working the markets surveillance. Only recently they turned into looking at individual trades. Until recently, they were looking at reports from market surveys at organized marketplaces or ISOs or RTOs. So now I believe that they are starting to collect also individual sort of trading information, but it is I mean, it's a massive operation. And I have to say that so far it's been quite a bumpy ride, obviously because it's always a very big IT project. And but so far also with the limited resources we've managed to take it off the ground.

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What happens to those 50 to 80 cases? Are those reported to the national authorities? Do you keep a record of those?

We do keep a record. In fact, eventually, I mean, the system only started as I said, over the last, I mean, we started to quote to receive information late in 2015. For a while we had issues with the quality of the information that we receive because also market participant were new to this. Everybody was new to this. So it took a bit before the information we got of was of the appropriate quality. Yes. National regulatory authorities have also issued fines on some of the cases number of cases are still under investigation and the latest count I have is that there are around 130-140 cases still under investigation at the moment. So, it takes some time. So, obviously by the time that you collect further evidence that you hear the parties, you try to understand what was going on, but the national regulatory authorities in Estonia, in Spain, in other jurisdictions have been actually been imposing fines. Some of these cases are still in front the administrative courts because then the roles on appeal by the market participants, but you know, it is happening.

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So, it is a concrete example for consumers that it does affect them at the end of the day.

It is and in this respect, actually, ACER has a slightly different role than with the traditional mandate because the traditional mandate as I mentioned beforehand, it was to assist national regulatory authorities. Here we have a separate role. Here we work with national regulatory authorities, but we have separate roles. So it's more a matter of coordinating our actions rather than supporting national regulatory authorities. There is an element of supporting because obviously, when we do our screening in order to come up with suspicious transactions, obviously we support them. But we have a fairly well-defined separate roles.

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According to the yearly reports, for example, it says there's a lack of funding to implement the different requirements that the agency is meant to do, and can you discuss more about the struggles to get the funding in place and ensure that market monitoring functions are supported or other tasks that you need to do at the agency and what is the story behind this?

Since the entry into force of REMIT, the agency has been struggling with resources both human and financial resources. Just a couple of indicators. In 2015, the then chair of FERC, Norman Bay, came and joined us to a presentation to the energy working party in the European Council. And then we were able to compare the resources that FERC was devoting at that time, on the same task that the agency was tasked, because actually FERC has a much wider remit today. They are also investigating in force, but we compared like with like, and at that time FERC was deploying at nine, full time equivalent at that time, we had only 26. So a third of the resources.

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So just to clarify, FERC is the regulatory agency that's in the United States...

Exactly. And as I mentioned, before they do they have a somewhat similar task to do in the US. So so we at that time, we had and we've been talking to FERC all along, and I believe we still are at a third of their resources. Then in terms of money, everybody agrees, including the, you know, the European Commission, that what we would need in order to operate remit is in the order of almost 3 million euros per year, which is peanuts. I mean, in terms of and yet, every year we're struggling. And last year, we were given 1.5 million, I'm not sure what we know, this year, we were given 1.5 million next year, we probably won't even get that. So again, they are here we're sort of around a half of what the funding that we need. Now, in four different ways. We were sort of able in the past because we had other, you know, developments, we were able to save money elsewhere and to turn them into REMIT now, but this is not a sustainable situation. And I'm not sure that this will be the case next year with this possible next year. So there is a real risk if things break not improved that we will have to discontinue our market survey and Sundaram it, which would be a pity, in terms of the return that this can bring. And also in terms of all the sunk costs that us and also market participants and national regulatory authorities have invested in in this business.

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Is there a way to fund ACER, for example, in some countries, energy regulators receive money from a fee That's charged energy companies? Is there a way to do this at a similar level at European Union level? So companies are paying for the activities of ACER, for example, market monitoring?



Well, indeed, this has been an ongoing debate in Europe. There are we believe that there are two obvious sources of funding through fees. One would be the parties reporting transactions in order to trade on behalf of market participants under remit. We call them registered reporting mechanisms. At the moment, we've registered around 120 of these mechanisms, who could easily pay a fee. In fact, most of them were surprised when in who are not charging them anything because he because in the financial services market, they are actually charged for reporting. So this would be an obvious and any very reasonable fee for them once you multiply by 120 or more becomes serious money for us. And then the other constituency that could help with through fees would be the transmission system operators because actually most of what we do is linked to the activities of transmission system operators.

We have around 100, transmission system operators, electricity and gas in Europe. And again, a very modest fee on each of them would mean sort of serious money for us. Now, there are two caveats here. First, we need legislation and maybe the Clean Energy package which is being now discussed by the college's later is an opportunity even though there are different views, including by Member States. The other aspect is that it has to be seen whether any revenues from fee will be compensated one by one by through a reduction in the subsidy from the union. Because this is what something sometimes has happened with two other agencies that you know, once you start collecting fees, then the budget from our subsidy from the union is actually reduced. And that obviously would not solve the problem. So, it is it is a fight. It is a struggle, and it is a challenge has been a challenge for the agency will still be a challenge for the agency, I guess in the years to come.

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What is the future of energy regulation? As technology changes, the example we had of gas and electricity being coupled, or smart grids or energy storage, How do you see over time the role of ACER in the role of regulation adjusting to these new technologies become deployed in the energy sector?

Well, with smart technology, I think regulation will also become smarter than it is at the moment. I don't think that regulators should be in the business of guessing what will be the technology of the future. And in any case, regulation will adapt, always in a much slower way, then then the way in which technology progresses so and, you know, the future will become much smarter than we think. And we become smarter much sooner than we think. So I think we have to somehow develop a future proof regulation, oh, it's this is easier to say than to do it. But one way that I'm personally thinking because this is still you know, discussion to mean to be had is to try to develop a toolkit, a regulatory toolkit, where you have different approaches to different structures or different characteristics of various activities because the problem well the problem the the challenge with regulation with them, With technological progress is that regulation, different types of regulation may needed be needed, depending on what the competition landscape that technology would support. So there are activities at the moment for example, which are delivered on the monopolistic market structure, technology may allow to be delivered through a more competitive market structure.

I mean, if you think in Telecom, you know, what used to be a very monopolistic part of a segment, you know, the last mile. Now, we're not talking about last mile anymore, because there are so many ways of reaching the homes of people that, you know, the monopolistic element of the large sort of copper wire in the last mile is not relevant anymore, and maybe there are issues similar issues also in energy. So, I think maybe in the future, we should think of regulatory tools. Where you have different ways of regulating different activities and then as technologic as technology progresses, then you move activities from one sort of one box to another box. But then stakeholders market participant would know what to expect, when you know the activity moves from one box to the next, because they know what how regulation will be, you know, how the next box is regulated, how regulation would be implemented into next box. Now, again, this is easier to say than to do it, but maybe we should start you know, sort of realizing that we cannot have a technological regulation cannot no longer be technologically technology based, and even technology neutral doesn't mean much could not meet marchment anymore in the future. So what we need to be is future proof and technology proof.

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So, there then would be attempt to instill some regulatory certainty at the different stages of technological development.

Yes, exactly, I mean, we cannot because no one can predict the future technological development. So, there is no point in predicting regulation, what we can predict or what we can provide certainty about is the tools which regulation will use in the future. And then depending on the technological development in the different activities, different tools will be different tools will be used.

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What do you think is one of the biggest achievements or one or two biggest achievements you have had since joining ACER then?

Well, I think is setting up an agency from scratch. Recruiting that an excellent team and delivering that's obviously the first achievement which was my, you know, my job in a sense in my what I was asked to do, and the second one which was I didn't expect it to be so effective. But it turned out to be quite important is to establish a constructive relationship with national regulatory authorities and other stakeholders and other institutional stakeholders, the European Commission, the parliament, etc. Now, we have very open discussions with national regulatory authorities, sometimes we disagree about the pace of market integration, but still the discussion and the interaction is always very constructive. And that is something that I think, you know, is of great value for the for the work of the agency. So, I would say that this is and then the obviously the third achievement is getting REMIT off the ground. It was not obvious. A lot of people did not believe that it could be done in 2011, when the when the REMIT was were entered into force, and we proved them wrong.





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