

CHALLENGES AND TASKS OF THE LEGAL REGULATION OF ELECTRIC POWER AND CAPACITY TRADING IN THE WHOLESALE MARKET

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The legal regulation of trading in the wholesale electric power and capacity market is based on the Law on the Electric Power Industry and the Wholesale Electric Power and Capacity Market Regulations. The peculiarities of legal regulation established by the Federal Law “On Insolvency (Bankruptcy)” should also be considered. As of March 17, 2020, the List of Wholesale Market Actors Undergoing Bankruptcy Proceedings included 40 companies. Poor payment behavior in the wholesale electric power and capacity market is one of the main issues. Failure to pay does not only affect the settlement status in the market, but also leads directly to an unscrupulous market player being declared insolvent. In this case, the existing legal regulation does not guarantee protection against wholesale electric power and capacity market transactions being disputed unreasonably. It seems that the best way to prevent transactions from being disputed in bad faith is to amend the current revision of Article 61.4 of the Bankruptcy Law by adding provisions stating in which cases transactions required by the wholesale electric power and capacity market rules cannot be disputed.

Keywords: energy law, legal regulation of energy markets, wholesale electric power and capacity market.

Legal studies have been conducted on various aspects of the legal regulation of energy markets [1]. As correctly stated by V.V. Romanova, “the regulations governing public relations in energy markets are predominantly established by energy sector-specific laws” [2]. The organization of trading in the wholesale market involving the consummation and settlement of transactions for trading electric power, capacity, and other tradable commodities in the wholesale market is performed by the

wholesale market infrastructure organization, the wholesale market commercial operator (ATS, JSC) under the Law on the Electric Power Industry and the Wholesale Market Regulations without a special permit (license) (Article 33 Clause 7 of the Law on the Electric Power Industry). In the study on the legal regulation of energy markets, V.V. Romanova noted that “a material aspect of the legal regulation of the wholesale electric power and capacity market is the establishment of the peculiarities of the legal status and powers

of commercial infrastructure organizations, such as the Market Council, the commercial operator, other commercial infrastructure organizations, by the legislator” [3].

The volume, prices and cost of electric power purchased daily by wholesale market participants, including the Debtor, are determined by the trading authorities, ATS, JSC and System Operator of the Unified Energy System, JSC, upon the completion of the bidding procedures based on the public bids submitted by wholesale market traders.

Exchange trading takes place on both dedicated energy exchanges and global exchanges. In the UK, wholesale electric power trading is mainly conducted via bilateral contracts often linked to the wholesale market price, as well as via the power exchanges operating in the UK, EPEX and Nordpool. In the EU, there are 9 main electric power exchanges: Nord Pool, EEX, IPEX, Powernext, APX NL, APX UK, Belpex, Endex, GME, and Omel. Wholesale electric power trading in France is performed via power exchanges (EPEX Spot SE and Nord Pool (spot markets), EEX (electric power futures contracts trading)) and under bilateral contracts [4].

In Russia’s energy market, the current laws stipulate that electric power can be traded both under contracts made in the wholesale electric power and capacity market (WEPCM) and on exchanges, however, while the regulatory framework exists, exchange trading currently fails to attract market players as an efficient electric power trading mechanism. Thus, contracts made in the WEPCM remain the only mechanism for electric power and capacity trading.

The peculiarities of legal regulation established by the Federal Law “On Insolvency (Bankruptcy)” should also be considered. The constantly updated List of Wholesale Market Actors (including those disqualified as wholesale market subjects) Undergoing Bankruptcy Proceedings included 40 companies as of March 17, 2020 [5]. Poor payment behavior in the wholesale electric power and capacity market is one of the main issues. Failure to pay does not only affect the settlement status in the market, but also leads directly to an unscrupulous market player being declared insolvent. As per the Bankruptcy Law, the purpose of bankruptcy proceedings is proportional satisfaction of creditors’ claims. It is the duty of the receiver exercising the powers

of the debtor’s manager and other management bodies to the extent, in the manner, and on the terms established by this law to achieve this purpose [6].

The main task of the trustee in bankruptcy is to maximize the debtor’s bankruptcy assets. Disputing transactions is one of the effective mechanisms. The debtor’s transactions disputable under the Bankruptcy Law are divided into suspicious transactions and transactions with preference (preferential transactions). Any transactions consummated within one month before filing for bankruptcy, including those in the WEPCM, meet the criteria of transactions made during the suspect period. This allows the trustee in bankruptcy to seek the voidance of such transactions for the purpose of restitution in court. This law does not contain any limitations for disputing transactions made in the WEPCM. Thus, the trustee is provided with a mechanism that requires the creditors operating in the market to justify why such transactions cannot be disputed on general grounds.

In these circumstances, preventing transactions consummated with the bankrupt in the WEPCM from being unreasonably disputed is of particular importance. Current laws do not contain provisions protecting WEPCM transactions from being disputed unreasonably. Article 61.4 of the Federal Law on Bankruptcy establishes the peculiarities of disputing certain transactions of the debtor. Under Articles 61.2 and 61.3 of the law, transactions consummated on the exchange based on at least one public bid (including financial contracts), as well as actions aimed at performance of obligations and duties arising from such transactions, transactions involving transfer of property and incurrence of obligations or duties consummated in the ordinary course of business of the debtor cannot be disputed, while the debtor’s transactions aimed at performance of obligations for which the debtor has received equivalent reciprocal performance of obligations immediately upon execution of a contract can only be disputed under Article 61.2 Clause 2 of the Bankruptcy Law. The other grounds listed in said article cannot be deemed universally applicable as they apply only to financial contracts.

Therefore, in order to protect a transaction from being disputed unreasonably, one shall prove that the transaction was consummated on the

exchange or in the ordinary course of business of the subject, and that the debtor has received equivalent consideration.

The case law on the qualification of transactions made by wholesale market participants in the wholesale market as transactions consummated on the exchange is limited and cannot be deemed well-established, since the arbitration case file analysis revealed just two relevant judicial disputes with issued final court orders: the Ruling of the Ninth Arbitration Court of Appeal on Case No. A40-78182/2011 Б dated June 9, 2014, upheld by the ruling of the Moscow Region Federal Arbitration Court, Order of the Penza Region Arbitration Court on Case No. A49-3135/2013 Б dated February 25, 2015. [7] Petitions of receivers seeking to dispute WEPCM transactions are currently being considered by courts of arbitration within isolated disputes in bankruptcy cases.

In view of the aforesaid, the question of legal qualification of the procedure under which electric power and capacity are traded in the WEPCM has a major practical bearing.

The Bankruptcy Law uses the concept on-exchange trading. According to Federal Law No. 325-ФЗ “On On-Exchange Trading” dated November 21, 2011, on-exchange trading means trading conducted regularly under specific rules with a certain procedure for authorizing traders to enter into sales contracts for commodities, securities, foreign currencies, repurchase agreements, and derivative financial instruments. At the same time, this law states that relations arising in the wholesale electric power (capacity) market are beyond its scope and are governed by Federal Law No. 35-ФЗ “On the Electric Power Industry” dated March 26, 2003. However, this wording does not negate the fact that WEPCM transactions are consummated during on-exchange trading, but under an industry-specific law.

As defined by Article 3 of Federal Law No. 35-ФЗ “On the Electric Power Industry” dated March 26, 2003 (hereinafter referred to as the “Law on the Electric Power Industry”), a wholesale market is an area of the distribution of particular commodities, electric power and capacity, in the Russian Unified Energy System within Russia’s Single Economic Space with the participation of major electric power and capacity producers and buyers, as well as other parties awarded the status of wholesale market subjects and operating according to the wholesale market

rules approved by the Government of the Russian Federation.

In the Law on On-Exchange Trading, the legislator specified the following features of on-exchange trade:

a) Exchange trading is conducted regularly:

The wholesale market has an organized system of contracts between wholesale market subjects defining the basic terms of operation of the corresponding wholesale market subjects, electric power and capacity sale, service terms. The list, system, and procedure of the execution of contracts mandatory for wholesale market participants are established by the Wholesale Market Regulations (Article 32 of the Law on the Electric Power Industry).

The commercial operator (ATS, JSC) and the system operator (System Operator of the Unified Energy System, JSC; SO UES, JSC) perform necessary procedures to organize wholesale trading, including day-ahead and system balancing auctions.

b) Exchange trading is conducted according to specific rules:

— A procedure for admission to trading is predefined for exchange trading,

In order to participate in transactions for sale and purchase of electric power and capacity in the wholesale market, one shall be granted the status of a wholesale market subject, a wholesale market electric power distribution participant, and access to the wholesale market trading system as prescribed by the Law on the Electric Power Industry (Article 35), the Wholesale Market Regulations (Section II), and the Accession Agreement.

— Bidding and commitment accounting procedures have been established.

According to Article 30 Clause 2 of the Law on the Electric Power Industry, wholesale market subjects are free to choose to buy and sell electric power by creating market prices and selecting bids to buy and offers to sell based on the lowest electric power prices in specific pricing zones of the wholesale market, in accordance with the wholesale market regulations, or by entering into bilateral electric power sales contracts,

Clause 8 of the Wholesale Market Regulations states that the commercial infrastructure organization conducts a day-ahead auction in the pricing zones of the wholesale market prior to the day during which the electric power purchased on the wholesale market is to be delivered.

In order to participate in electric power trading based on the day-ahead auction and to ensure the fulfillment of obligations under the existing wholesale contracts, wholesale market participants operating in the pricing zones of the wholesale market submit bids to buy (offers to sell) electric power in each group of delivery points for each hour of the following day drawn up in accordance with the Wholesale Market Regulations and the Accession Agreement to the commercial infrastructure organization (Clause 9 of the Wholesale Market Regulations).

Wholesale market participants operating in the non-pricing zones of the wholesale market participate in electric power trading in accordance with the Wholesale Market Regulations in the pricing zones of the wholesale market based on the results of the day-ahead auction and the system balancing auction to the extent of the electric power flow along the border with the pricing zone (zones) of the wholesale market under the Wholesale Market Trading System Accession Agreement (Clause 11 of the Wholesale Market Regulations).

The day-ahead auction is conducted as defined by the Accession Agreement subject to the provisions of the Wholesale Market Regulations by means of the calculation of hourly equilibrium electric power prices and the electric power volumes included in the expected hourly production (consumption) by wholesale market participants for the pricing zones (Clause 79 of the Wholesale Market Regulations).

According to Clause 84 of the Wholesale Market Regulations, during a day-ahead auction, bids to buy (offers to sell) electric power submitted for delivery point groups of the same pricing zone are compared in each pricing zone considering the cross-zonal electric power flow volumes as described in the Accession Agreement.

Electric power volumes bought (sold) during each hour of the day using the trading method specified in Clause 4 Paragraph 3 of the Wholesale Market Regulations are determined in accordance with the Accession Agreement (Clause 90 of the Wholesale Market Regulations).

According to Clause 86 of the Wholesale Market Regulations, the procedure for calculation of equilibrium electric power prices and expected hourly production and consumption rates are established by the Accession Agreement.

The procedure for conducting a day-ahead auction and determining expected hourly

production and consumption rates of wholesale electric power market players is established by the Day-Ahead Auction Regulation (Appendix No. 7 to the Accession Agreement).

Clause 2 of Regulation 7 states that, while conducting a day-ahead auction and determining expected hourly production and consumption rates of wholesale market participants, ATS, JSC is required to determine the following according to Regulation 7:

- Expected hourly production and consumption volumes for each hour of an operating day, each prediction model node, each export/import supply cross-section, and each delivery point group (hereinafter referred to as DPG),
- Equilibrium prices for each hour and each prediction model node, as well as for each export/import supply cross-section,
- Expected hourly production and consumption (trade schedule) for each prediction model node, each export/import supply cross-section, and each DPG.

As per Clause 10 of the Wholesale Market Regulations, the system operator shall conduct a system balancing auction in the pricing zones not later than one hour before the electric power delivery after determining the expected hourly production (consumption) rate in order to create balanced electric power production and consumption conditions and manage operation modes of the power facilities

The system balancing auction is conducted by means of the calculation of electric power volumes produced by the generating equipment with an installed generation capacity of at least 5 MW and volumes consumed by the stakeholders' power receivers with controlled consumption per hour of electric power supply, as well as imbalance sale (purchase) prices at the specified hour (Clause 127 of the Wholesale Market Regulations).

Following the system balancing auction, a wholesale market player purchases electric power in the amount of the imbalance corresponding to the production decrease (consumption increase).

Following the system balancing auction, a wholesale market player sells electric power in the amount of the imbalance corresponding to the production increase (consumption decrease).

In accordance with the Accession Agreement, during the system balancing auction, the system operator includes the volumes for which the

bids participating in the system balancing auction contain the lowest price considering the costs of losses and system limitations into the dispatch electric power volumes in addition to the volumes produced using the generating capacity corresponding to the minimum values established by the system operator, provided, however, that the demand is expected to match these volumes (Clause 134 of the Wholesale Market Regulations).

The system balancing auction procedure is established by Section IX of the Wholesale Market Regulations and the Accession Agreement.

All settlements under these contracts are made via clearing (trading) accounts of the wholesale market participants open with an authorized banking institution (hereinafter referred to as the “bank”) — Article 33 Clause 9 of the Law on the Electric Power Industry, Clause 40 Paragraph 20 of the Wholesale Market Regulations, Clause 2.2. of the Financial Payment Regulation, Clauses 5.2, 5.3 of the Day-Ahead Market, Balancing Market Commission Contracts, Clauses 5.2, 5.3 of the Day-Ahead Market, Balancing Market Sales Contracts.

Based on the results of the day-ahead auction, ATS, JSC determined equilibrium electric power prices, electric power volumes bought/sold at the equilibrium prices, the cost and volume of electric power sold under each commission and sales contract, including contracts payments for which are being disputed by the Receiver.

Based on the results of the system balancing auction, SO UES, JSC determines the electric power imbalance volumes, the prices for which wholesale market participants buy/sell electric power imbalance volumes, the cost and volume of electric power bought/sold under each commission and sales contract.

In particular, ATS, JSC calculates the cost and quantity of electric power bought/sold by each wholesale market player under each contract with CFR, JSC, and submits this information to CFR, JSC in the form of liability/claim registers (provisions of the Wholesale Electric Power Market Financial Payment Regulation included in the Accession Agreement as Appendix No. 16 (hereinafter referred to as the Financial Payment Regulation)).

Based on the information on the volume and cost of electric power delivered by wholesale market participants to CFR, JSC under day-

ahead market (hereinafter referred to as “DAM”) and balancing market (hereinafter referred to as “BM”) commission contracts and purchased from CFR, JSC under DAM and BM sales contracts, CFR, JSC prepares electric power handover certificates and sends them to the wholesale market participants.

The Wholesale Market Trading System Accession Agreement contains provisions binding on the market players regulating measures ensuring trading order and discipline, resolution of disputes arising out of WEPCM transactions. The Regulation on the Imposition of Sanctions in the Wholesale Electric Power and Capacity Market (Appendix No. 21 to the Wholesale Market Trading System Accession Agreement) establishes the members and functions of a committee created specifically for extrajudicial dispute resolution, the procedure of violation case and materials review by the committee, as well as types and grounds for imposition of sanctions for violations of the Wholesale Market Regulations and the Accession Agreement. Material sanctions in the form of penalties for improper performance of WEPCM sales contracts are stipulated by the Wholesale Electric Power Market Financial Payment Regulation (Appendix No. 16 to the Wholesale Market Trading System Accession Agreement).

Therefore, wholesale electric power trading is conducted based on public bids to buy and offers to sell electric power submitted by wholesale market participants on a regular basis according to the rules established by Law on the Electric Power Industry, the Wholesale Market Regulations and the Accession Agreement stipulating specific procedures for admission to the wholesale market, trading, and rules aimed at the organization of the distribution of particular commodities, electric power and capacity, in the wholesale market.

At the same time, the existing legal regulation does not guarantee protection against unreasonable disputing of transactions made in the wholesale electric power and capacity market. It seems that the best way to prevent transactions from being disputed in bad faith is to amend the current revision of Article 61.4 of the Bankruptcy Law by adding provisions stating in which cases transactions required by the wholesale electric power and capacity market rules cannot be disputed.

Such a provision is already used in Article 61.4 of the Bankruptcy Law. The provisions of Clauses 5–7 of said article have been introduced

in order to secure close-out netting when one or more financial contracts made under a general agreement (single contract) or clearing rules are being disputed, to exclude unreasonable disputing of close-out netting, as well as financial contracts entered into to secure performance of obligations under derivative financial instruments as transactions leading to preferential treatment of certain creditors on the grounds stipulated by

Article 61.3 of the Federal Law “On Insolvency (Bankruptcy)” [8]. Thus, an exemption for a specific transaction type has been introduced in the article and applied extensively.

By implementing the proposed measures, we could eliminate additional legal risks for commerce stakeholders and make the Russian electric power and capacity market as a whole more appealing. ■

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