



3rd Legislative Package Input
**Paper 5: Powers and Independence of
National Regulators**

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1 Background

In the Communication “an Energy Policy for Europe”, the European Commission wrote that “the levels of powers and independence of energy regulators need to be harmonised on the basis of the highest, not the lowest common denominator in the European Community”. In the Communication “Prospects for the Internal Gas and Electricity Markets”, they also come to the conclusions that energy regulators need to be strengthened at national level and have the required level of discretion to take decisions on all relevant issues.

Heads of State or Government at the Spring 2007 European Council called for “further harmonisation of the powers and strengthening of the independence of national energy regulators”.

MEPs were more specific in a report prepared by the ITRE Committee at the end of last year. They have proposed “significant increases in the powers of Member State regulators, who should be fully independent of government and industry, and to harmonise their powers which could be achieved via the establishment of common rules on transparency, disclosure and accountability, which should be monitored by the Commission and annually by the European Parliament, and to set minimum binding guidelines on the procedure for the appointment of regulators; believes that national energy regulators should be given a role of advising competition authorities in the Member States and of ensuring that energy companies have a statutory obligation to give energy saving advice to customers.”

In order to achieve a high level of competition within a single European electricity and gas market it is important that the rules for the operation of the market and the monopoly networks provide a sound basis. They must be non-discriminatory and facilitate the operation of the market. It is essential that the market and network rules are subject to adequate regulatory oversight to ensure that market participants can be confident of a level playing field. In order to undertake this task national regulatory authorities (NRAs) must have a common and high level of powers, and must be able to fulfil their task in an independent and fair way. This paper sets out the requirements for EU legislation in order to achieve this.

2 Powers of regulators under the current EU framework

At an EU level, the powers and competences of national regulatory authorities (NRAs) are given in the electricity and gas Directives (2003/54/EC and 2003/55/EC) and in the Regulations 1228/2003 on electricity and 1775/2005 on gas. The Commission Decision of 11 November 2003 on establishing the European Regulators Group for Electricity and Gas (EREG) is also relevant. It is essential that the existing framework is fully and effectively implemented, in the spirit and the letter, which is not yet the case in all Member States.

The Electricity Directive – as well as the Gas Directive – requires Member States to give responsibility for a number of decisions to designated “regulatory” or “competent” authorities. Article 23 of the Electricity Directive and Article 25 of the Gas Directive provides for a set of minimum competences for NRAs. These provisions are supplemented by other requirements at national level.

There is some legal basis for cross-border issues in the Electricity and Gas Directives and Regulations.

Under the Directives, Regulators are required to contribute to the development of the internal energy market and of a level playing field by cooperating with each other and with the Commission in a transparent manner. Also, in the event of cross-border disputes, the deciding NRA shall be the authority which has jurisdiction in respect of the system operator which refuses use of, or access to, the system.

Under Regulation 1228/2003/EC (electricity), the NRA must:

- Approve of general schemes for the calculation of the total transfer capacity;
- Decide (or at least provide an opinion) on exemption to normal access rules for new investments (article 7). Any exemption decision shall be taken after consultation with other Member States or regulatory authorities concerned;
- Ensure compliance with the Regulation and all binding guidelines adopted under the Regulation. According to Article 9, “where appropriate to fulfil the aims of this Regulation, [regulatory authorities] shall cooperate with each other and with the Commission”;
- Cooperate in order to meet the requirements of the Regulation.

Under Article 22 of Directive 2003/55/EC (gas), NRAs decide (or at least provide an opinion) on exemptions from normal access rules for new investments. Any exemption decision shall be taken after consultation with other Member States or NRAs concerned. Under Regulation 1775/2005 (gas), the regulatory authority must ensure compliance with the Regulation and all binding guidelines adopted under the Regulation. According to Article 10, “where appropriate to fulfil the aims of this Regulation, [regulatory authorities] shall cooperate with each other and with the Commission”.

These provisions are complemented by the Commission Decision 2003/796/EC establishing the ERGEG. According to Article 1.2, “the Group shall facilitate consultation, coordination and cooperation of national regulatory authorities, contributing to the consistent application in all Member States of the provisions set out in Directive 2003/54/EC, Directive 2003/55/EC and Regulation 1228/2003 as well as possible future Community legislation in the field of electricity and gas.”

3 Proposals for additional EU legislative requirements

This section presents the additional requirements that would be needed in new EU legislation to ensure that NRAs’ powers are enhanced and harmonised as necessary to oversee the secure and efficient operation of the EU grid and the creation of a single European energy market. For this reason, the scope of this paper is limited to transmission and to the operation of wholesale markets. Given the current difficulties with the application of the existing Directives, the Commission should, in line with better regulation principles, consider a more prescriptive approach to ensure a future regime is fully implemented.

3.1 Governance of NRAs

a) Duties

Existing EU legislation provides that “NRAs shall contribute to the development of the internal market and of a level playing field by cooperating with each other and with the Commission in a transparent manner” (Article 23.12 of Directive 2003/54/EC; Article 25.12 of Directive 2003/55/EC).

New EU legislative requirements should be placed on NRAs to promote the development of a competitive single European electricity and gas market. NRAs will in addition have a new EU duty assigning to them responsibility for applying at national level, within their jurisdictions, the duty to oversee the secure and efficient operation of the EU grid. The duty to co-operate should be extended to other regulating institutions, including for example financial regulators to cover the implications of trading in energy related financial instruments.

b) Independence

Existing EU legislation:

- According to Article 23 of Directive 2003/54/EC and to Article 25 of Directive 2003/55/EC, national regulatory authorities “shall be wholly independent from the interests of the [electricity] gas industry”;¹
- The Directives also provide for certain regulatory decisions which relate to the NRAs’ core duties to be submitted for formal approval to the Member State (e.g. Article 23 of Directive 2003/54/EC states that “Member States may provide that the regulatory authorities shall submit, for formal decision, to the relevant body in the Member State the tariffs or at least their methodologies”). NRAs should not be subject to ex ante control by Ministries.

New EU requirements:

- Member States shall ensure that their national legislation, including the statutes of their national regulatory authorities, is compatible with the statute of the new “European System of Energy Regulation”;
- The President/Chair and the members of the Board of each national regulatory authority shall have a standard duration for the term of office. The President and the members of the Board of a NRA may be relieved from office only if they no longer fulfil the conditions required for the performance of their duties or if they have been guilty of serious misconduct.

¹ For details on the European System of Energy Regulation (ESER) proposed by ERGEG and of the new European Regulatory Function, see ERGEG’s advice on 3rd legislative package input: “Paper 2; Legal and regulatory framework for a European system of energy regulation” (C07-SER-13-06-02-PD).

Motivation: both NRAs and the “European Regulatory Function” should be independent both of commercial interests and direct political influence. Regulatory independence should be properly audited. Regulatory decisions should be based on recognised and predictable criteria in order to ensure a sound climate for investment.

c) Resources

Existing EU legislation: no explicit requirement in EU legislation, even though according to Article 25.7 (Article 23.7) “Member States shall take measures to ensure that regulatory authorities are able to carry out their duties in an efficient and expeditious manner”.

New EU requirement: it should be written explicitly in EU legislation that Member States have a duty to ensure that the regulatory authority is given adequate human and financial resources to carry out its duties, specifically taking into account the particular characteristics of the energy sector. To this end NRAs should preferably be funded by levies.

d) Accountability

Existing EU legislation provides that NRAs “shall publish an annual report on the outcome of their monitoring activities” (Article 23 of Directive 2003/54/EC; Article 25 of Directive 2003/55/EC).

New EU requirement: generic requirement on Member States to ensure that national regulatory authorities are properly accountable.

Motivation: the form of accountability of NRAs is a matter for subsidiarity.

e) Sharing of data

Existing EU legislation: no explicit requirement

New EU requirements:

- Subject to confidentiality rules, Member States shall ensure that the information submitted to one NRA can be made available to another such authority in the same or different Member State, after a substantiated request, where necessary to allow either authority to fulfil its responsibility under Community law;
- NRAs and national competition authorities (NCAs) shall provide each other with the information necessary for the application of the provisions of Community law. In respect of the information exchanged, the receiving authority shall ensure the same level of confidentiality as the originating authority.

3.2 Requirements for network regulation

NRAs must have the powers to ensure conditions for the use of the networks are non-discriminatory and that markets are not subject to abuse. This section describes the overall package of powers that NRAs require to undertake their functions:

a) Network Access

Existing EU legislation:

- Article 23 of Directive 2003/54/EC as well as Article 25 of Directive 2003/55/EC provide that “the regulatory authorities shall be responsible for fixing or approving prior to their entry into force, at least the methodologies used to calculate or establish the terms and conditions for: a) connection and access to national networks, including transmission and distribution tariffs. These tariffs, or methodologies, shall allow the necessary investments in the networks to be carried out in a manner allowing these investments to ensure the viability of the networks; b) the provisions of balancing services”. In accordance with Article 23.4 and 25.4, “regulatory authorities shall have the authority to require transmission and distribution system operators, if necessary, to modify the terms and conditions, tariffs, rules and methodologies referred to in paragraphs 1, 2 and 3 (of Articles 23 and 25) to ensure that they are proportionate and applied in a non-discriminatory manner;
- With regard to conditions for access to the network, the provisions of Regulations 1228/2003/EC (cross-border exchanges in electricity) and 1775/2005/EC (natural gas transmission) are already quite detailed. They provide in particular that NRAs approve (and monitor) contractual terms and conditions (either using harmonised transportation contracts or a common network code).

New EU requirement: NRAs should be explicitly required to decide and enforce these provisions (including effective, proportionate and dissuasive sanctions) without an obligation to submit, for formal decision, the regulatory decisions on these provisions to any administrative body in the Member State.

Motivation: NRAs must have the powers to ensure conditions for the use of the networks are non-discriminatory and that markets are not subject to abuse. This should include the approval, monitoring and enforcement of rules for access to the networks, including access rights, connection offers and agreements, and conditions for network access; and the approval of the transmission and distribution tariffs for access to the network, without an obligation to submit the regulatory decisions for formal decision to any administrative body in the Member States.

The detailed requirements for new or amended guidelines are attached, in draft form, to ERGEG's 3rd legislative package input -Paper 3 on the overall framework for Network Regulation (C07-SER-13-06-3-PD). The rules for access to other infrastructure are also related to network access, in particular gas storage facilities, LNG facilities and interconnectors. Such access rules must also be subject to regulatory approval, monitoring and enforcement. These issues will be covered further in this detailed input on the requirements for new or amended guidelines for electricity and gas in the third package of legislation.

b) Network operation and development

Existing EU legislation:

- According to Article 23 of Directive 2003/54/EC as well as Article 25 of Directive 2003/55/EC, NRAs are required to monitor “a) the rules on the management and allocation of interconnection capacity, in conjunction with the regulatory authority or authorities of those Member States with which interconnection exists; b) any mechanisms to deal with congested capacity within the national gas system; c) the time taken by transmission and distribution system operators to make connections and repairs”;
- As mentioned above, Article 23.2 of Directive 2003/54/EC, as well as Article 25.2 of Directive 2003/55/EC provide that “tariffs, or methodologies, shall allow the necessary investments in the networks to be carried out in a manner allowing these investments to ensure the viability of the networks”;
- With regard to network operation and development, the provisions of Regulations 1228/2003/EC (cross-border exchanges in electricity) and 1775/2005/EC (natural gas transmission) are already quite detailed. They contain important provisions concerning capacity allocation mechanisms and congestion management procedures as well as balancing rules and imbalance charges. NRAs are required to monitor compliance with these requirements;
- Under Articles 7 of Regulation 1228/2003/EC and 22 of Directive 2003/55/EC, NRAs decide (or at least provide an opinion) on exemption to normal access rules for new investments (including interconnectors between Member States, LNG and storage facilities). Any exemption decision shall be taken after consultation with other Member States or NRAs concerned.

New EU requirements

- NRAs should be explicitly required to enforce these provisions (including effective, proportionate and dissuasive sanctions);
- The approval by NRAs of rules for the development of the networks should include the publication and accuracy of forward network development plans such as 7/10 year statements; rules relating to new investment in the network; network planning and its execution and rules for the development of related infrastructure including LNG facilities, gas storage facilities and generation plants.

- As networks become more integrated and the development of European electricity and gas grids becomes a reality, NRAs must be able to monitor, and enforce compliance of TSOs in their jurisdiction with European standards, and where appropriate must take account of methodologies for allocating the cost of the European grids in setting domestic tariffs.

Motivation: Regulators should oversee the approval, monitoring and enforcement of rules relating to the live operation and development of the networks, including congestion management, balancing, imbalance charging, maintenance (including outage planning); as well as the publication and accuracy of forward networks plans. NRAs must be able to approve network planning and its implementation, regardless of the organisational or legal form of the company which owns, operates and develops the networks.

c) Customer protection and quality of supply

Existing EU legislation:

- Article 3 (3) of Directive 2003/54/EC stipulates “Member state shall ensure that all household customers ... enjoy universal service, that is the right to be supplied with electricity of a specified quality within their territory...”
- Article 3 (5) of Directive 2003/54/EC: “Member states shall take appropriate measures to protect final customers...”
- Article 5 of Directive 2003/54/EC and 2003/55/EC : “Member states shall ensure the security of supply issues... they may delegate this task to the regulatory authorities... This monitoring shall, in particular, cover... envisaged additional capacity being planned or under construction, and, the quality and level of maintenance of networks...”
- Article 3 (3) of Directive 2003/55/EC: “Member states shall take appropriate measures to protect final customers and to ensure high level of consumer protection...”
- Article 3 (4) of Directive 2003/55/EC: “Such measures may include, in particular, national and Community tools, for the maintenance and construction of the necessary network infrastructure...”
- Article 23 (1) c) of Directive 2003/54/EC and Article 25 (1) c) of 2003/55/EC: (regulatory authorities shall monitor) ...”the time taken by the transmission and distribution system operators (undertakings) to make connections and repairs;” (This is the matter of actual continuity of supply. As long works are being carried out on the network, the consumers are interrupted)

New EU requirements:

- In order to enhance customer protection NRAs should have power to regulate quality of supply in all its aspects (commercial quality, continuity of supply, voltage quality).

Motivation:

Quality of supply is an important component of customer protection. For all aspects related to network (e.g. connection times, interruptions, voltage disturbances and so on) monitoring is not sufficient to prevent the risk that network companies increase their profits at expenses of the quality of supply (for instance by reducing maintenance and development of the network). Therefore, regulators should have power for an active regulation (setting standards and compensations, linking tariff or revenues with the quality levels, setting voltage quality limits, etc.) on all aspects of quality of supply related to networks. Considering the implemented regulation model, NRAs are the only entities in conditions to assure a correct balance between quality of supply offered and tariffs paid by costumers.

3.3 Requirements for market regulation

a) Market rules

Existing EU legislation:

- Article 25 (h) of Directive 2003/55/EC (23(h) of Directive 2003/54/EC) require NRAs to “monitor the level of transparency and competition”.

New EU requirements:

- Market rules in respect of the compulsory market should be subject to regulatory approval. This market is the one that participants cannot avoid – in some market models it could be the rules of a compulsory (gross) pool, and in bilateral markets it could be the imbalance market. Voluntary markets will normally be subject to financial services and competition rules.
- As markets integrate then increasingly problems in one jurisdiction may manifest themselves as price distortions in another market and jurisdiction. NRAs must therefore be able to co-operate in undertaking investigation and enforcement activities in such cases. Each NRA must be allowed to undertake inquiries on the reasonable request of another NRA, to collect and share data, and to undertake enforcement action where the effect is in another market.

b) Transparency

Existing EU legislation:

- Directives 2003/54/EC and 2003/55/EC require NRAs to monitor “the publication of appropriate information by transmission and distribution system operators concerning interconnectors, grid usage and capacity allocation to interested parties, taking into account the need to treat non-aggregated information as commercially confidential” (Article 23.1(d) and 25.1(d));
- These provisions are complemented by the requirements of Regulations 1228/2003/EC and 1775/2005/EC e.g. in particular Article 6 which regard the role of the NRA in implementing the “three-minus rule”.

New EU requirements:

- NRAs should be able to enforce these requirements, including effective, proportionate and dissuasive sanctions ;
- National regulators should be required to ensure that the information is published in a consistent manner and shall cooperate with each other to ensure that it is the case (e.g. available capacity at entry/exit points, electricity interconnections) and with sufficient frequency and timeliness.

Motivation:

NRAs are the best placed to identify transparency requirements, following appropriate consultation of market players, and monitor that these requirements are implemented –and enforce these requirements if necessary. They should also be the ones deciding on exemptions, on a case by case basis.

See also ERGEG's 3rd legislative package input - Paper 6 on transparency (C07-SER-13-06-6-PD).

c) UnbundlingExisting EU legislation:

- Article 25.1(f) of Directive 2003/55 requires that the NRA monitors “the effective unbundling of accounts (...) to ensure that there are no cross-subsidies between transmission, distribution, storage, LNG and supply activities”. Article 23.1(e) is the equivalent in Directive 2003/54/EC;
- Articles 9 of Directive 2003/55/EC (10 of Directive 2003/54/EC) require TSOs to submit an annual report setting out the measures taken to ensure that discriminatory conduct is excluded (compliance programme) to the NRA.

New EU requirements:

If ownership unbundling is the option retained by the third regulatory package, few incremental requirements will be needed in EU legislation. If an ISO model is preferred, the complexity of the regulatory arrangements needed to ensure that there is a firewall between competitive activities and network activities will vary depending on the ISO depth (shallow versus deep). At the very least, incremental legislative requirements will be needed so that NRAs are empowered:

- To approve the operational relationship between the ISO and the TO which should take the form of a transparent and binding document, to monitor compliance, and if necessary, to require that the terms and conditions are modified;
- To ensure that information held by the ISO and the TO are held entirely separately and that adequate internal compliance arrangements are in place. This involves investigation powers for the NRA;
- To ensure that there is adequate legal and management separation between the ISO and the TO which will require the NRA to have powers to enforce changes where the separation arrangements are inadequate.

Motivation: national regulators must ensure that unbundling is effective and properly enforced.

See also ERGEG's 3rd legislative package input - Paper 1 on Unbundling (C07-SER-13-06-1-PD).

d) Emergency arrangements

Existing EU legislation: according to Article 24 of Directive 2003/54/EC (Article 26 of Directive 2003/55/EC), "in the event of a sudden crisis in the energy market, and where the physical safety or security of persons, apparatus or installations or system integrity is threatened, a Member State may temporarily take the necessary safeguard measures".

New EU requirement: any arrangements for dealing with an emergency situation and how these affect the operation of the market and/or the rights of market participants to access the networks must be subject to regulatory approval.

e) Enforcement

Existing EU legislation:

- The NRA is the dispute settlement authority for complaints against a transmission, LNG or distribution system operators (Article 25.5 of Directive 2003/55/EC; Article 23.5 of Directive 2003/54/EC). Also, in the event of cross-border disputes, the deciding NRA shall be the authority which has jurisdiction in respect of the system operator which refuses use of, or access to, the system;
- Article 18 of Directive 2003/54/EC and Article 16 of Directive 2003/55/EC provide for a right of access to the accounts of electricity and natural gas undertakings.

New EU requirements:

- Member States shall ensure that [gas undertakings and electricity producers/wholesale customers/suppliers/ TSOs/SSOs/LNG system operators/DSOs] provide all the information, including financial and technical information, necessary for NRAs to carry out their duties according to Community law;
- These undertakings shall provide such information promptly on request and to the timescales and level of details required by the national regulatory authority. The information requested by the NRA shall be proportionate to the performance of the task. The NRA shall give the reasons justifying its request for information; Subject to confidentiality rules, Member States shall ensure that the information submitted to one NRA can be made available to another such authority in the same or different Member State, after a substantiated request, where necessary to allow either authority to fulfil its responsibility under Community law;
- NRAs shall be empowered to apply effective, proportionate and dissuasive sanctions at least in certain areas (access to network, operation and development of networks);
- NRAs should be empowered to conduct joint-investigations.