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Workshop on perspectives, concerns and overall planning for the setup of an independent energy regulator in Azerbaijan(CWP.01.AZ)



Experience of EU/EnC member states on the establishment of independent energy regulatory authorities

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Agenda



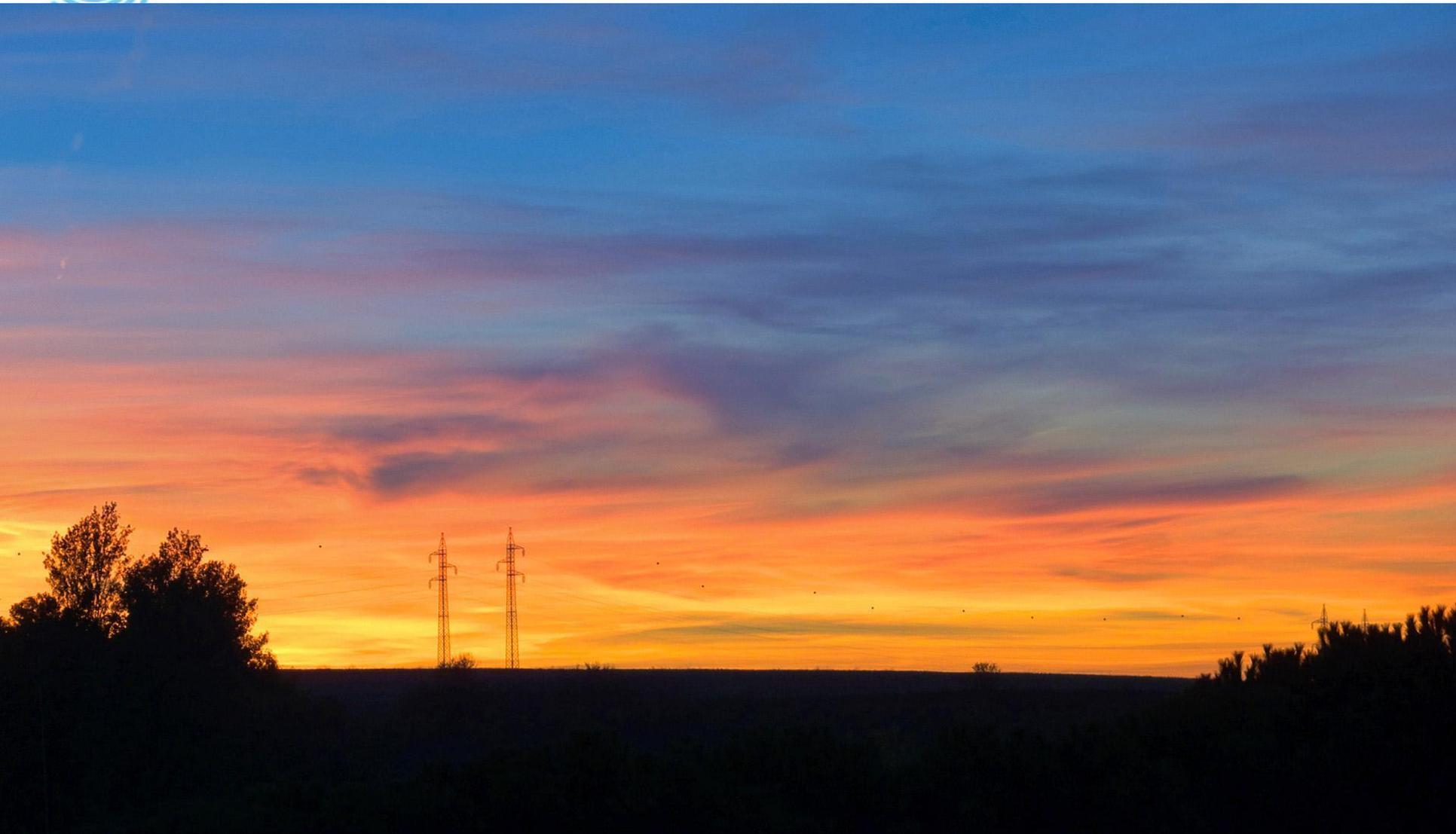
- Why and how do we need to regulate energy companies
- Different regulatory models
- Establishment of regulators in the EU and EnC member states
- Main regulatory functions

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Why and how do we need to regulate energy companies



Energy sector regulation



- Why do we need to regulate it?
- How to regulate it?
- Why do we need an independent regulator?

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Objectives of regulation (why?)



- protection of consumers
- ensuring the financial viability of the companies
- promotion of competition
- collection and dissemination of information

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How to regulate?



- no regulation
- self-regulation
- command and control
- independent regulation

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Old style regulation



- energy, water, telecommunication companies
- state owned monopolies
- Government approves minor operating decisions
- sectorial ministry is an owner and a regulator
- state owned enterprise is protected from competition but may be not allowed to cover all its costs
- subsidies and cross-subsidies are allowed and politically supported

Need for a new type regulation



- emerges with an introduction of a private capital
- investors want to secure themselves from the Government intervention
- increases with the liberalization of the sector (unbundling, introduction of competition)
- regulation of the liberalized, privatized sector require new tools and approaches

Need for an independent regulator



- to protect investors from unacceptable risks
- to protect consumers from the monopoly power abuse
- to give to all the market players clear, transparent stable rules of the game

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Different regulatory models



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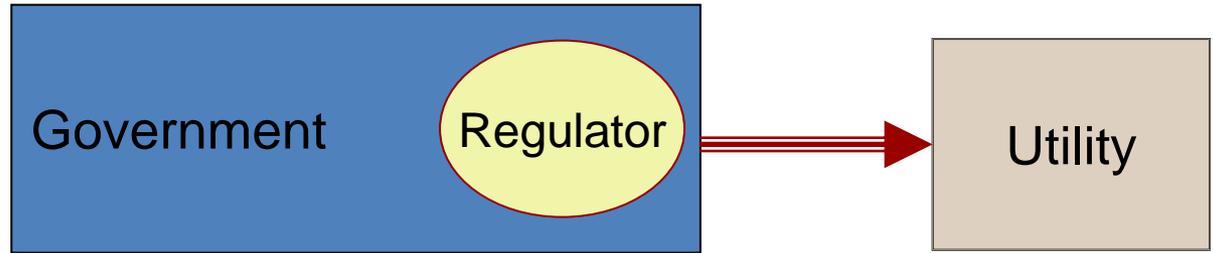


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Different regulatory models



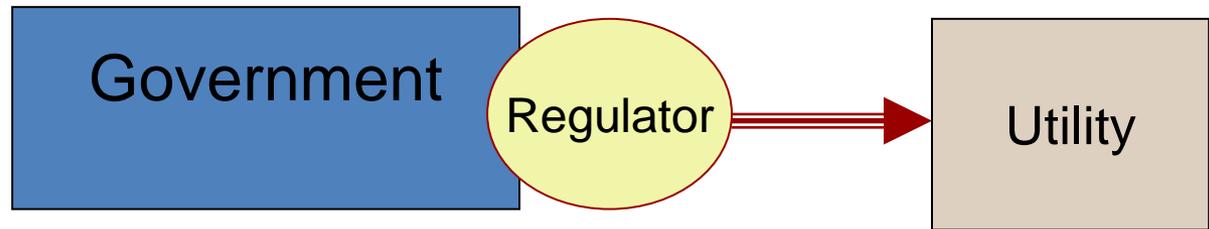
Ministry's model



Advisory model



Ministerial Agency model



Independent model



Independent advisory agencies



- Independent from the ministries and operate autonomously
- Plays an advisory role in a wide variety of regulatory issues, but has no decision making powers on regulatory matters
- Usually have monitoring responsibilities and authority in the resolution of disputes of such issues as network access

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Ministerial agency's model



- Agency is an autonomous body linked to the sectorial ministry
- Operates on a separated budget and under the autonomous management
- May operate with a substantial degree of independence
- Ultimately a ministerial agency is subordinated to the ministry

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Independent regulatory agencies



- Outside ministerial structure
- Does not require approval for
 - changing tariffs
 - granting licenses
 - settling disputes
- Clear separation of roles
- Decisions of the agency may be appealed in courts
- It does not act in a vacuum, it should implement the general Government's policy

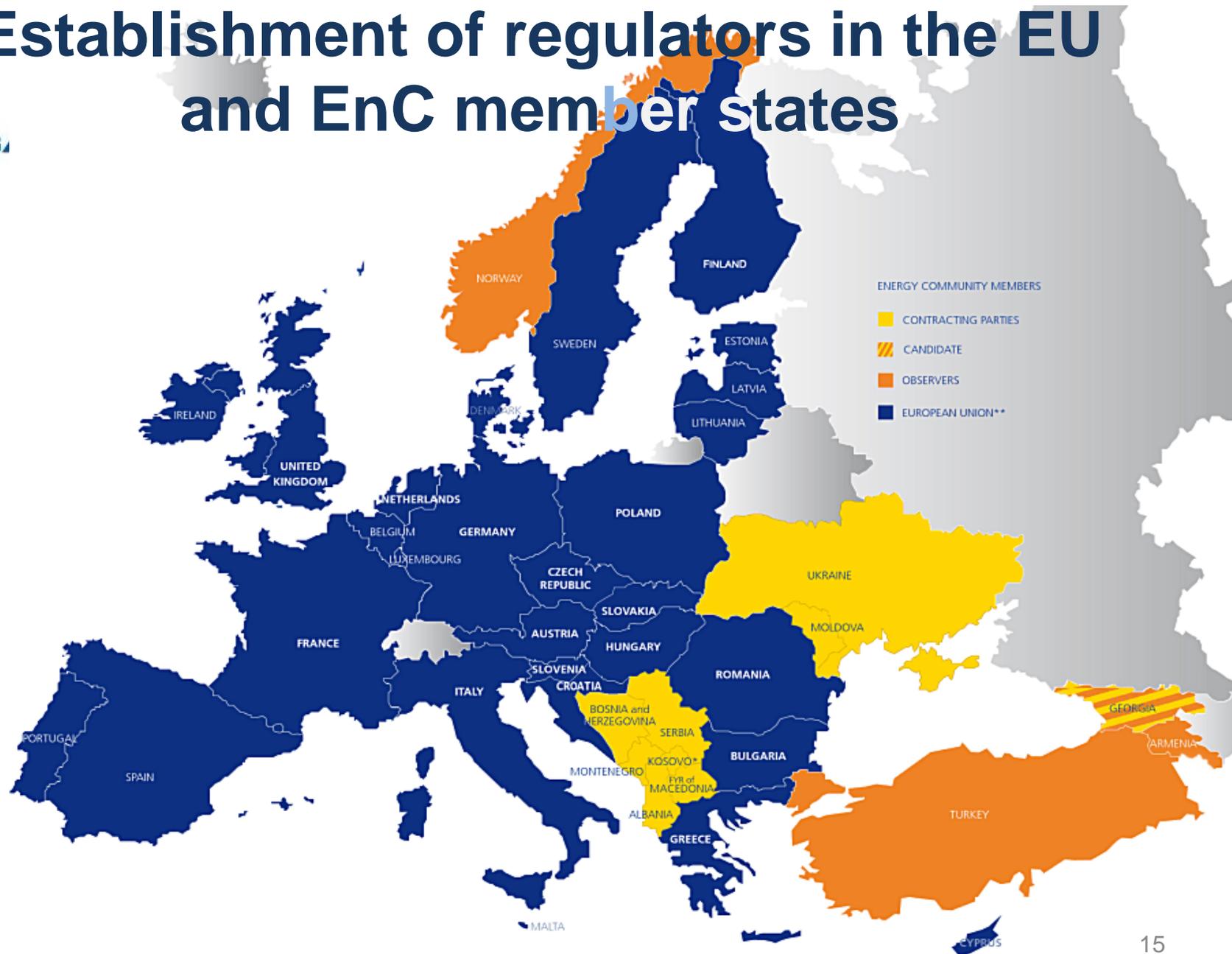
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Establishment of regulators in the EU and EnC member states



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Energy regulators are rather new in the EU



Established in	Countries
1986	UK (gas)
1989	UK (electricity)
1994	Hungary
1995	Italy, Finland
1997	Lithuania, Poland, Portugal, Spain
1998	Estonia, Sweden
1999	Ireland, Netherlands
2000	Belgium, Denmark, France, Greece, Latvia, Slovenia
2001	Austria, Czech Republic, Slovakia
2005	Germany

Different regulatory bodies



- In the EU there are 2 main structures of the regulatory authorities: agencies and commissions
- Northern countries in general prefer agencies (U.K., the Netherlands, Denmark, Sweden, Finland, Poland, Czech R., Hungary, Estonia, also Romania)
- Commissions are preferred in the South (Italy, Greece, Bulgaria, Spain, Portugal, France, Belgium, but also Slovakia, Latvia and Lithuania)

Different historic background



- a number of countries (Ireland, UK, France, Italy, Greece, new MS) have a long history of state-owned monopolies
- to make liberalization credible in these countries calls for a regulator with a broad mandate
- Nordic countries, Germany, the Netherlands have a different background with a much more decentralized industry structure, less state ownership and tradition of self-regulation
- approach to market regulation in these countries is less ambitious, building on existing institutions that gradually are modified to cope with the changing situation

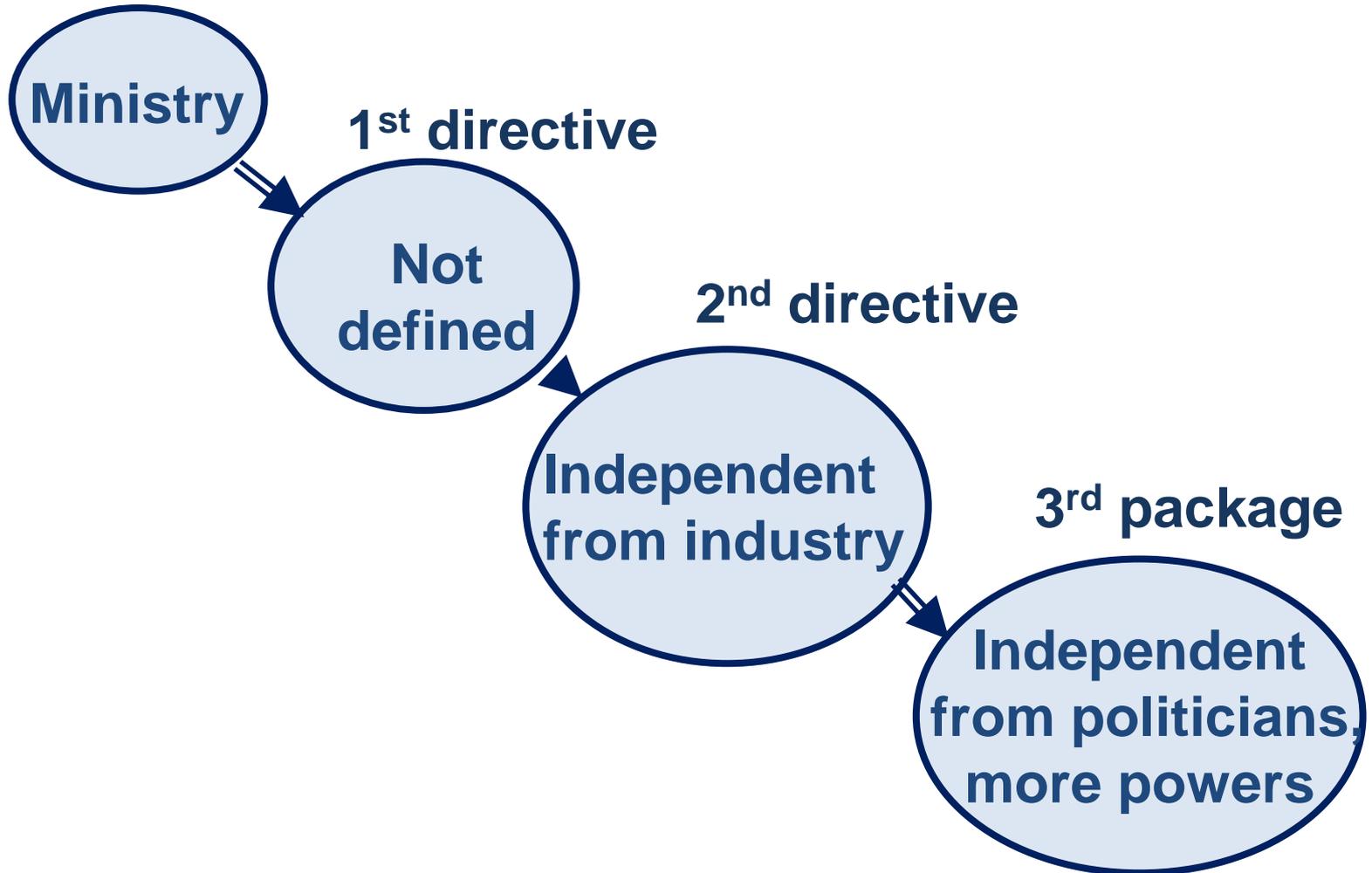
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EU Electricity Directives on a regulator



before 1996



Energy regulator in Hungary (1)



- Hungarian Energy Office (HEO) was established in 1994 – the second regulator in Europe
- Was responsible for issuing and amending licences
- The licenses are the key document in the monitoring and enforcement of regulation
- This was a new approach in Europe and especially in the CEE region
- HEO was responsible to establish pricing criteria and rules, but it was the Minister of Industry who actually decided on the final prices

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Energy regulator in Hungary (2)



- HEO in fact was a ministerial agency with a certain independence
- But the management of HEO was appointed by the minister and there was no fixed term or appointment criteria
- With implementation of the 2nd and 3rd EU Energy Packages HEO was converted into an independent regulatory agency - Hungarian Energy and Public Utility Regulatory Authority (HEA)

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Development of regulation in the Czech Republic



- Law on Energy was enacted in 1994 under which the Ministry of Economy was responsible for all aspects of regulation except price regulation
- Price regulation was the responsibility of the Ministry of Finance
- In 1998 with a separate Regulatory Department within the Ministry of Industry and Trade was established
- Finally, the Energy Regulatory Office was set up on 1 January 2001
- It is an independent administrative authority responsible for regulation in the energy sector

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Energy regulator in Moldova



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- Independent energy regulator - National Agency for Energy Regulation (ANRE) was established in 1998 when Parliament passed laws on electricity and on gas
- According to these laws ANRE is responsible for issuing licenses, setting tariffs, market monitoring, consumer protection – all usual functions of an independent regulator
- ANRE is managed by the Administrative council consisting of five directors, all decisions are taken by the majority votes and each director has one vote only
- Director General and directors are appointed by the Parliament for a 6 year time period with a possible renewal

Georgian National Energy Regulatory Commission



- The Georgian National Energy Regulatory Commission (GHERC) was established in 1997
- It is based on the Law on Electricity and Gas and the Law on Independent Energy Regulatory Authorities
- Both laws give high level of independence to GNERC
- So, it issues licenses and controls the licensees, sets pricing methodologies and approves all tariffs, resolves disputes of the market players and protects consumers' rights

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Main regulatory functions



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Traditional regulatory functions



- setting **pricing methodologies** only or fixing **tariffs** based on the methodologies (set by the Regulator or by another institution)
- approving **investments** ex-ante or ex-post
- issuing **licenses**, setting and changing (or not) license conditions, monitoring implementation, imposing sanctions
- settling **disputes** between market players

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New regulatory functions



- Monitor market behavior and enforce rules
- Detect market power and promote competition
- Promote trans-national market integration and regulatory cooperation
- Provide dispute resolution and settlement processes
- Ensure public service obligations and consumer rights
- Maintain security policies, etc.

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Cost analysis for the tariff setting



- Regulator collects data from the regulated companies
- data is checked, compared, analyzed
- for the comparison international (regional) data may be also used
- historical costs are analyzed but efficiency of the company's operation should be evaluated
- many meetings of the staff with the regulated company – checking data
- Regulator revises the structure of the assets too
- assets not related with the regulated activity should be excluded from the rate base
- Regulator may set different depreciation rates for the pricing purposes

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Setting final tariffs



- in vertically integrated monopolies Regulator should set all the final tariffs
- more liberalised approach is also possible
 - regulated company prepares the final tariff design as it better knows structure of the consumers and may encourage or distract consumption (load curve regulation)
 - Regulator checks if the final tariffs calculated by the regulated company are not discriminatory and do not exceed the price cap set by the Regulator
- with the liberalisation of electricity markets in Europe there will be no more final tariffs set by the Regulator (except of for the supplier of last resort supplying temporarily to the vulnerable consumers)

Licenses



- Licenses are tools to regulate the market players
- They are usually used as a tool to protect the weak participants, especially consumers
- Licenses are very different and used for different purposes:
 - in all states where licenses exists, they are used for network activities (transmission, distribution)
 - in some countries licenses are used in combination with authorisation for electricity generation,
 - in some countries licenses are used for supply and trade business

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Quality of supply



Customer service issues



Commercial quality



Continuity of supply



Voltage quality



Non-payment handling
Disconnection for debts
Complaints
Billing
Security deposits
Reconnections
Connections to network
Meter's investigations
Planned supply interruptions
Unplanned interruptions
Voltage limits
Voltage dips
Flickers
Harmonics

Ensure compliance



- one of the main functions of the Regulator is to ensure compliance with the prevailing rules and regulations
- non-compliance may be detected, but could not be ensured by monitoring
- compliance can be achieved by
 - ✓ voluntary agreements between the regulator and the regulated firms
 - ✓ enforcement

Some conclusions relevant to Azerbaijan



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Need for a regulatory agency



- In Azerbaijan energy regulation is split among several institutions:
 - licensing is responsibility of the Ministry of Energy
 - pricing is responsibility of the Ministry of Economic Development and of the subordinated Tariff Council
 - determination of general rules and standards in generation, transmission and distribution – responsible a special State Committee
- With the planned liberalisation of the energy sector it is necessary to merge the main regulatory functions in one agency
- The agency could be a separate independent institution at the Ministry of Energy

Energy regulatory agency



- The newly created Energy Regulatory Agency at the Ministry of Energy would be responsible for:
 - issuing licenses and control behaviour of the licensees
 - develop pricing methodologies for different activities in the electricity and natural gas sectors
 - calculate tariffs for all regulated companies and present them for approval to the Minister of Energy
 - monitor activities of all companies in electricity and gas sectors
 - resolve disputes between market participants and answer consumer complaints
- The final decisions on licensing and pricing could be left to the Minister of Energy

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