

VII GEODE Spring Seminar

The third energy package: challenges of implementation

The view of the European Parliament

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Good morning ladies and gentlemen,

It was with great pleasure that I accepted to take part in the annual seminar of the European independent distributors of electricity and gas to share with you the view of the European Parliament on the implementation of the third energy package. This legislative initiative was one of the priority dossiers of our Chamber during the last term and one of which we are more satisfied. As you are aware, the discussions were tough within the Parliament and then with the Council but I firmly believe that we managed to strike a deal in the end that represents a true step forward in the liberalisation and integration of the internal market in electricity and gas.

The liberalisation of the energy markets came at a much later date than other sectors since the founding treaties. It was only during the 1990s, and thanks largely to the impulse of our dear Commissioner Loyola de Palacio, that it really got under way with the second package. It was then when industry was seen as mature to handle a deep programme of reform of the vertically integrated model that existed throughout the Union at the time. Since these first efforts, our goals haven't changed. We are still pursuing the full introduction of competition in the wholesale and retail markets, fair and non-discriminatory access to the networks for all producers and suppliers, a sound regulatory framework across the EU and well interconnected networks.

The report of DG competition of 2005 on the state of implementation of the second energy package gave us an excellent overview of the situation listing the divergences on the ground with respect of the reference model. We could identify the remaining

obstacles to the achievement of market integration and liberalisation: market dominance of the incumbents, vertical lock-up of the market through long-term contracts – both, upstream and downstream -, barriers to entry, insufficient dissociation between competitive activities (generation and supply) and monopolistic ones (networks) giving way in some instances to discriminatory access to essential infrastructures, existence of generalised end-user regulated tariffs and an overall lack of market integration at EU level.

This report that highlighted the shortcomings of implementation of the legislation opened the way to the launching of the third energy package in 2007. As you know, and that's why I am here today, I was rapporteur of one of the five legislative proposals and part of the negotiating team of the Parliament. I can tell you that this negotiation has been in my two-term experience as an MEP one of the toughest dossiers, if not the toughest, because of the obvious divergence of national interests and the resistance of certain Member States to let partially go of their stronghold in these sectors. As an example, 15 out of 27 Member States still have in place mechanisms of price control which results in practice in the staggering figure of 80% of final consumers buying energy at an artificially low regulated tariff. In my home country, Spain, this tariff is 30% below market price. This illustrates the mistrust of Governments in markets and while the process towards full liberalisation is fully on its way, it still has some convincing to do.

Energy has traditionally been regarded as a matter of national interest and security and it is psychologically challenging to accept the new paradigm that tells us that, like in many other areas, energy policy can no longer be seen strictly under a purely national perspective. But all is well that ends well and we did manage to strike a balance between the two Institutions in an agreement that will require a lot of effort from all stakeholders, public and private.

The third energy package establishes a regulatory framework that aims to remove the

remaining obstacles to full market integration. That is, ensuring a level playing field between European companies – incumbents and new entrants –, the now famous unbundling issue, a high level of consumer protection, strong and independent regulators, the promotion of interconnection capacity between Member States and the development of European network plans and the upgrading of the networks to be able to adapt to the integration of renewable energy sources. These are only part of the objectives of this ambitious legislative package.

What do we, as legislators, expect from governments and private stakeholders? In short, what we hope to see is full and rapid implementation. If the question is: what is Parliament's vision of the outcome of such implementation? Then the answer is a bit longer. Like I said earlier, the present EU market situation is far from ideal and companies and consumers alike are suffering the consequences.

Under the provisions of the package, the Member States will have the opportunity to choose between three different approaches on more effective unbundling:

- Full ownership unbundling (OU) – The transmission system operator (TSO) owns the electricity/gas network and is not controlled, directly or indirectly, by a vertically integrated undertaking (VIU) that is also active in supply and generation.
- Independent System Operator (ISO) – VIUs retain ownership of their transmission networks but must hand over the operation, maintenance and development of the transmission system to a separate entity, the ISO.
- An Independent Transmission Operator (ITO) model (the so-called "third way approach") – The TSO remains within the VIU but additional regulatory conditions are introduced in order to guarantee the independence of the ITO from the VIU.

As you know the European Parliament's preferred option, particularly for the electricity sector, is full ownership unbundling in line with the Commission's original

proposal. However, there was enough opposition in the Council to force a negotiation to include these three options. Can I just say that the negotiating team of the Parliament is very proud of what it has achieved with regard to the so-called third option. Indeed, we insisted and succeeded in making it as controlled as possible, subject to very tough sanctions in the case of intervention of the integrated company in the investment decisions of the TSOs. I think we have managed to make it so tight that it makes ownership unbundling quite an appetizing option!

This of course, is a crucial point of the package and we will be watching carefully how it is implemented and we will study closely the Commission's report on it in a few years.

Obviously, this third option could not be accepted without a much stronger role and independence of the national regulatory authorities, who under the ITO model get a whole new set of powers that included the possibility of issuing a penalty of 10% turnover should a vertically integrated company interfere with its TSOs investments.

An element of the package is the obligation of each Member State to ensure that its national regulator:

- is independent from the interests of the government and industry (public and private entities);
- has sufficient financial and technical capacity to perform its functions; and
- is impartial and transparent in its activities.

The regulators must obtain greater powers and responsibilities with regard to the separation of activities (transmission and distribution), mandatory investment and abuse of dominant position. Furthermore, the regulator will be entitled to impose "effective, proportionate and dissuasive penalties" against electricity and gas undertakings not complying with their obligations or not performing legally binding decision issued by the Commission. This requires further amendments to national legislation.

And while these new powers are particularly relevant to the countries where the ITO model will be in place, there are also many new responsibilities and improvements for the regulators in unbundled countries. Indeed, like I have often said, unbundling is not the solution to all internal market problems. Again, I will use the example of my country to illustrate this. Spain is an unbundled country yet we have two big obstacles to the proper functioning of the market. On the one hand we have a generalised regulated tariff like I mentioned earlier and, on the other hand, we have a regulator that lacks independence from government and that has very little powers. In other countries you have them too dependent from Government and with too many powers considering they depend directly from the political authorities. In sum, what we need to level these criteria across the Union. This will also ensure that the newly created Agency for the Cooperation of Energy Regulators will be able to take sound decisions.

This brings me to my next point, and one of the biggest achievements of this package, the creation of ACER. I will not dwell too much on this because they will explain it themselves in a bit but I would like to stress the importance that Parliament gives to this new Agency. As you know, we fought very hard to get as many powers as possible for this new body and, while the reluctance of both Commission and Council to empower it with further responsibilities made us fall short of our expectations, we see this as a very first step and look forward in the future to revise the regulation to make further improvements.

The package will also improve cross-border cooperation between Transmission System Operators through the establishment of ENTSO and ENTSO-G. These new bodies have been entrusted with the difficult tasks of harmonising the network codes that will allow, among other things, the introduction of renewable energy in the system, developing the ten-year network development plans as well as to promote R&D in the field of energy.

This brings me to the issue of consumer protection. Customer protection and the

consumer rights are among the main issues of the third energy package. The new Electricity and Gas Directives provide some improved measures on consumer protection. Customers will have the right to:

- change their electricity or gas supplier, while respecting contractual conditions. The change will be performed by the operator(s) concerned within three weeks. In addition the customers will not be charged for changing suppliers;
- receive a final closure account following any change of gas or electricity supplier no later than six weeks after the respective change;
- receive all essential data related with the electricity or gas consumption;
- be properly informed of actual electricity or gas consumption and costs frequently enough to enable them to regulate their electricity consumption;
- compensation and refund arrangements, which apply if contracted service quality levels are not met, including in case of inaccurate or delayed billing.

The expected implementation in the national legislation of the provisions related to customer rights and their protection will be one of the main and most important changes in the near future. The regulator will be entitled to impose 'effective, proportionate and dissuasive penalties' against electricity and gas undertakings not complying with their obligations.

This is a great achievement for Parliament and probably one of the biggest challenges for undertakings. All these new provisions have also a cost and we should not forget that and we understand that. And one of the challenges for Governments and companies alike is to explain this very well to consumers. However, this will be impossible to do where the regulated tariffs persist. These distort price signals to consumers and the Parliament is not of the view that these additional costs should be hidden away in taxes and subsidies.

I insist so much on the issue of regulated tariffs because I truly believe they are an grave anomaly in the energy market that puts all our goals at risk, whether it is

liberalisation, energy efficiency or the integration of renewable energy. Allow me to elaborate. One of the biggest misconceptions about liberalisation is that energy will automatically be cheaper. In some places it will be, but in others it won't. It is not a direct consequence as many have been saying in the past. Energy is not necessarily cheap and things like, for example, the energy mix or volatility of oil prices are a main factor of the price of the kWh. We want renewable energies, then there is a price to pay for it. By artificially lower the energy bills yet increasing their taxes to subsidise renewables, we are not giving complete and transparent information to consumers. There is also no point in telling people that consuming less energy will reduce their costs if then we tax them to compensate companies for being forced to sell at a loss because the tariff is below market price. And there is no point in taking about how unbundled we are if the tariffs do not allow new entrants in the market to make a profit.

We cannot use the argument of lower prices any longer. The prices are what they are and we cannot continue pretending otherwise. The framework has changed considerably in the last decade. We have ambitious environmental targets set in the energy climate package and we have new concerns about security of supply. The measures needed to address these concerns have a significant cost and we have to accept it.

In this regard, the third package plays also an important role in terms of security of supply. The regulations for the development of cross-border interconnections are an essential part of the package that aims to ensure that electricity and gas can freely flow within the Union. We are now in the middle of the legislative process of the regulation on security of gas supply and it is obvious that the EU really needs to step up its game in terms of infrastructures within our borders. During the last gas crisis between Russia and Ukraine we realised that we had enough gas but not enough cross-border infrastructure to let it flow where it was needed. So these regulations, along with ACER and the ten year network development plan will play an essential role in improving our energy security.

As you see, the third package also serves as a link between the three pillars of the European Energy Policy: competitiveness, sustainability and security of supply. And for this reason, it is imperative that it be fully and rapidly implemented.

I have had the chance to be a small part of the immense transformation that have taken place in the energy policy of the EU during the two full terms I have served as Member of the European Parliament always in the ITRE committee. It is undeniable that the mentality of Member States and the European Institutions overall has shifted toward a common approach. It has been a slow but steady progress and I am a firm believer that we are on the right path. At EU level, it is a team effort, a bit like in football: Loyola de Palacio gave the first push, Andris Piebalgs kept the ball rolling and Gunther Oettinger will need to kick the ball in the net ensuring proper implementation of all the energy legislation. And, of course, as much as Parliament and Commission can do can do, most of the work will have to be done by you, regulators, distributors, generators and consumers, among many. And we must not forget that we are all on the same boat and we sail towards the same objectives. Quoting the celebrated address of Lord Nelson to the British sailors before the battle of Trafalgar, the European Union expects each one of us to do our duty. Simple to say, difficult to accomplish. So we have no other option than to be up for the challenge. And that brings me to the two words that will be the end of my speech: Good luck.