Infrastructure projects and effects of prolonged price regulation in SEE

Gas and Electricity projects' treatment

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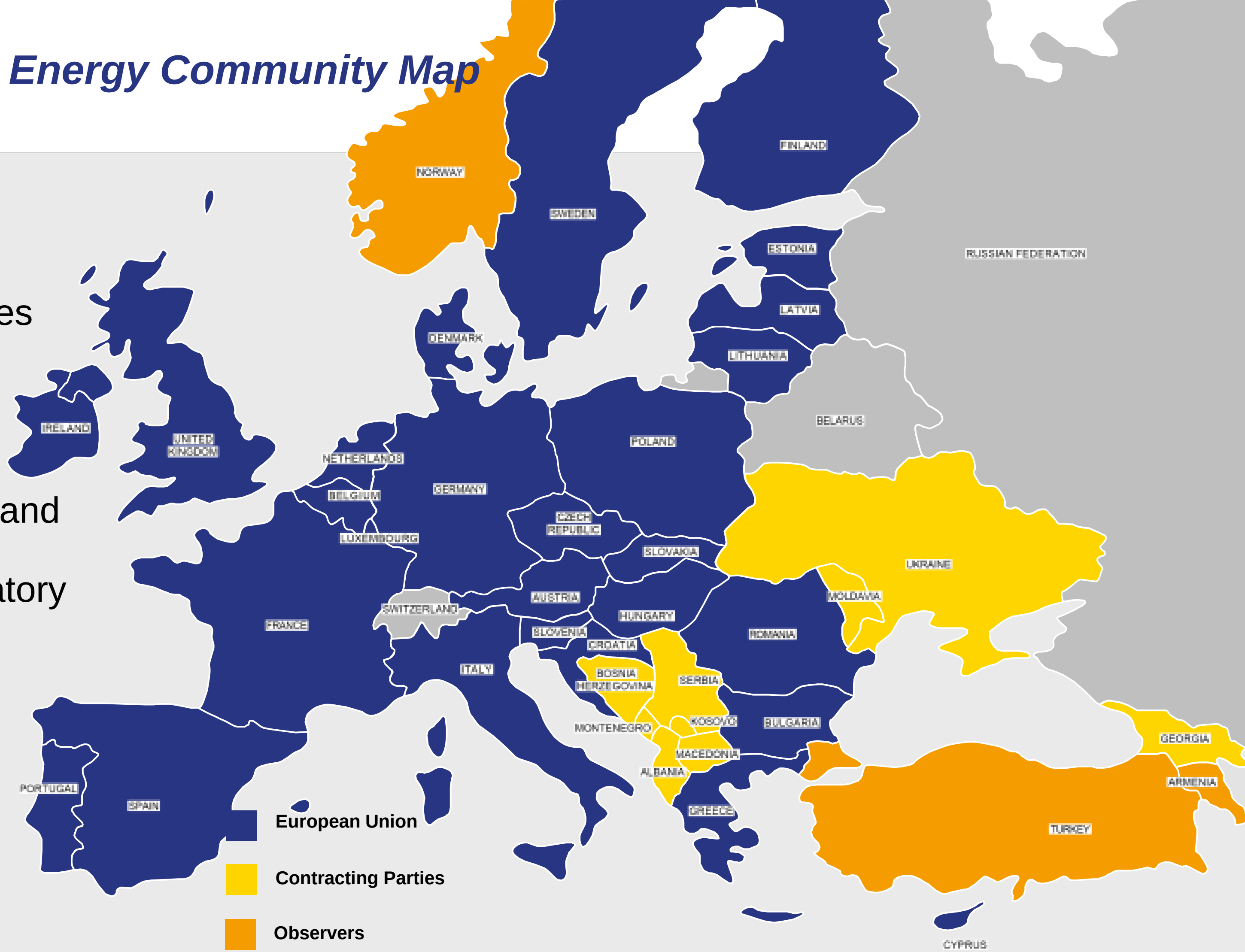
Energy Community Map

Parties to the Treaty
- European Union
- 9 Contracting Parties
- Observers

Goal
- Extend the internal Energy market to SEE and Black See Region
- Create single regulatory and market framework

By
- Rule of Law



The Energy Community acquis and areas of work

Gas

Electricity

Infrastructure

Renewable energy

Environment

Competition

Oil

Social

Statistics

Energy Efficiency

Aspects of ECS work...
Prerequisites of a functioning energy market...

Energy Community

The colourful world of a functional energy market requires...

Transparent Legal Framework

- 3rd Energy Package
- Network Codes
- Tariff Regimes
- Etc.

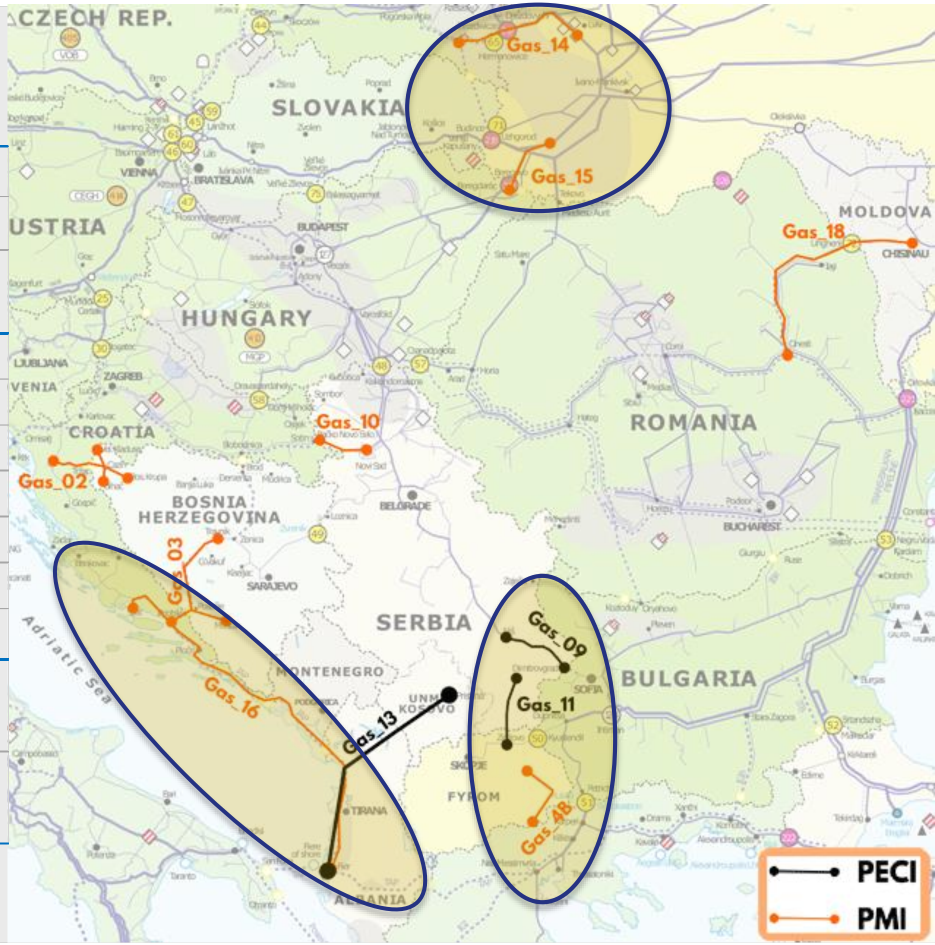
Functional Infrastructure Background

- Physical Connectivity
- Security of Supply
- N-1
- Source and Route Competition

Gas Infrastructure Projects in the Energy Community

Project identification excercise in EnC - PECI/PMI selection ~ PCI selection in EU

General Criteria	Potential Benefits outweigh costs	Involves at least 2 CPs or a CP and a MS
		Located in one CP and has a Cross-border impact
	Fits in the defined project categories	
Specific Criteria	Electricity	Market Integration
		SoS
		Sustainability
	Gas	Same + Competition
	Smart Grid	
	Oil	SoS
		Mitigation of Environmental Risk
PECI	If involves a CP and a MS has to be PCI first in EU	
PMI	If involves a CP and a MS and is not PCI in the EU	



What is the key for market players...?
I. Third Party Access - examples

1) In RS rules provide for TPA but not happening in practice

- TPA at Kiskundorozsma RS – Entry would enable access to EU Market: CEGH – HU VTP
- RS-BG Interconnector would provide source and route diversification – differently priced gas from the Southern Gas Corridor (SDII, Greek LNG...) – TPA will be key

2) In UA TPA in practice on IPs with MSs and the VTP

- VTP launched in January 2016
- But majority of capacity granted to Naftogaz (Budince) justified by PSO and SoS
- NC of UTG enables LT and ST capacity allocations; but in 2016 all capacity on IPs and national market was booked on monthly basis
- Auction on IPs only if *available capacity* < *required capacity*

3) In FYROM Makpetrol is buying on the BG border from Gazprom; several industries also procure on the border

4) In BiH only incumbents can access the network

Implementing rules on paper is an important step one, but implementation in practice and avoiding administrative barriers to enter the market is key!

What is the key for market players...?

II/a Price Regulation - examples

1) In UA there are 3 levels of price regulation

- The price at which Ukrgazvydobuvannya (UGV) sells its gaz to Naftogaz for protected categories (households, religious org; district heating companies)
- The price at which Naftogaz sells to end-user suppliers
- The price at which end-user suppliers sell to protected customers

2) General practice of price regulation – for protected customers

- Main wholesale supplier procures gas at unregulated prices - can't be regulated if the source is import
- The NC sells to retail suppliers at regulated price
- Retail suppliers sell to protected customers at regulated price

Price regulation on the basis of Directive 2009/73/EC would be in order.
EnC can challenge the Public Service Obligation Act of the countries.

What is the key for market players...?
II/b Regulated Prices within the supply chain

But problems do exist with the implementation of price regulation

- Does not always apply to all households; but it is easier to regulate them all → inefficiently targeted
- Measurement problems –
  - Who is household?
  - Who is small enterpreneurship? - Not all DSOs differentiate them
- Problems transferred from other sectors e.g.:
  - District heating, protecting not competitive industry, protecting national supplier from competition, ...

What is the key for market players...?
III. National Champions:

*"There can be good reasons for governments to make energy more affordable, [...] for the [...] vulnerable groups without access to modern energy. [...] Many subsidies **are poorly targeted**, [...] benefiting wealthier segments of the population. [...] the effect of most subsidies is to encourage consumers to waste [...] energy, **putting** [...] **pressure on energy systems** [...] and often **straining government budgets**. [...] subsidised electricity prices in some economies are a major underlying reason for the **poor financial state of utilities**, **undermining their ability to invest** in new energy infrastructure... ."* Toshiyuki Shirai - Senior Energy Analyst, WEO, IEA - https://www.iea.org/newsroom/news/2017/april/commentary-putting-the-right-price-on-energy.html

National Champions: the winners and loosers of price regulation

- Discre0pancy between higher import price and lower regulated sale price questions the financial sustainability in the long run
- Investments might lack, and might not be efficiently choosen → service niveau might falter
- If subsidised from state budget, it does not help corporate development and preparation for competition which shall come sooner or later
- If state budget supplements revenues, in the end it is still the population who pays the for the actual cost of the import gas - partially the same who are protected from the higher price
- Risk of pervert incentives – as economic theory nicely puts it...

What is the key for market players...?
IV. Adopting Network Codes - overview

Energy Community

Working Group on Network Codes within EnC

- Contracting Parties (NRA + TSO)
- Neighbouring Member States (NRA + TSO)
- COM, ENTSOG, ACER

Interoperability and CMP NCs

- COM to propose text to Permanent High Level Group of EnC in October 2017

CAM and Balancing Network Codes have been touched upone

Tariff Network Code is for the future

**Crucial is to apply common rules for all. Network Codes shall be applied on EU – EnC border.
EnC has found partner in neighbouring Member States: HU; PL; RO; BG; HE.
So far they have signed declaration to implement NCs on their borders with CPs IF EnC confirms that the CPs have implemented the NCs themselves as well.**

Thank you for your attention!

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