

EFFECTIVE AND EFFICIENT UNBUNDLING OF TRANSMISSION SYSTEM OPERATORS (TSO)

FLORIAN MARGAN *

Vysoká škola ekonomická v Praze,
Fakulta mezinárodních vztahů

Abstract

Depending on the outcome of the EU Council and EU Parliament deliberations, the new proposed legislative package presented by the European Commission on 19/09/2007 might have far reaching consequences on both the internal and the external dimensions of the energy and natural gas markets. It is necessary to give supports the Commission's aim to achieve a fully functioning internal market. This requires a lot of questions just like, effective application of the current legislation (particularly I am concerned with the topic of unbundling in v EU), non discriminatory access and system operation, stable regulatory framework conducive to support investment needs for Europe's supplies etc. I like to show shortly, where we are now in EU?

Klíčová slova:

V závislosti na výsledcích jednání Rady EU a Evropského parlamentu by nově navrhovaný legislativní balíček, který Evropská komise předložila dne 19. září 2007, mohl mít dalekosáhlé důsledky jak pro vnitřní, tak i vnější dimenzi trhů s energiemi a zemním plynem. Je zapotřebí podporovat cíl sledovaný Komisí, zaměřený na dosažení plně funkčního vnitřního trhu. To vyžaduje účinné uplatňování stávající legislativy (konkrétně se věnuji otázce unbundlingu), nediskriminační přístup a provoz soustav, stabilní regulační rámec vedoucí k podpoře investičních požadavků v souvislosti se zásobováním Evropy, atd. Chtěl bych krátce ukázat, kde jsme v EU nyní.

* Ing.Ing. Florian Margan, tato stať vznikla v rámci řešení Výzkumného záměru Fakulty Mezinárodních vztahů VŠE v Praze, č. MSM 6138439909 , e-mail: f.margan@quick.cz

EFFECTIVE AND EFFICIENT UNBUNDLING OF TRANSMISSION SYSTEM OPERATORS (TSO)

Proposal for a Directive of the Council amending Directive 2003/54/EC concerning common rules for the internal market in electricity and repealing Directive 96/92/EC ¹⁾.

The European Commission has 19.9.2007 published a third liberalization package of energy regulations. It represents a proposal for an amendment of the Regulation on common rules for the:

- Internal market in electricity,
- Directive on conditions for access to the network for cross-border electricity trade,
- and proposal of a new Directive on constitution of a European Agency for Cooperation of Energy Regulatory Offices.

I supports adoption of the package and hopes that it will be primarily the endeavour to improve the interconnection among member states that will contribute to the completion of a single European energy market without any pointless barriers.

The proposal of the third liberalization package of the EU contains mainly a proposal of a Directive which will amend Directive 2003/54/ES on common rules for the internal market in electricity ²⁻³⁾.

The proposal imposes an obligation on member states to:

- ensure implementation of ownership unbundling at the level of transmission system operators,
- or establishment of an independent system operator within one year following the transposition of the Directive into their national law.

So, the proposal of the Directive contains two alternative solutions and can be considered as a concession to member states, which expressed their disapproval to ownership unbundling.

An ownership separation of the transmission system in the Czech Republic took place already 4 or more years ago, and the operator and owner of the transmission system, CEPS, is 100% owned by the state just like in Slovenia where ELES, is owned by the state. It only confirms the fact that the Czech Republic and Slovenia is one of the leaders of the process of electricity market liberalization in the EU.

I supports the part of the liberalization package establishing an agency for cooperation of energy regulatory offices as a new community organ with legal identity.

The Agency should publish opinions for:

- transmission system operators,
- regulatory offices,
- European Commission and make individual decisions towards energy companies.

I see the coordination of the activities of national regulatory offices as the best means to integrate their decision-making practices. However, it believes that powers of the new organ need to be exactly and exhaustively determined in the final version of the new Regulation. The third amended regulation is the Resolution No 1228/2003 on Conditions for Access to the Network for Cross-border Electricity Trade. The proposal of the Regulation states that transmission system operators should cooperate within Europe through the European Transmission System Operator as an organ accountable to the European Commission.

Within the European network, a ten-year investment plan for the whole EU will be adopted and, along with that, an obligation to cooperate at regional level will be imposed on transmission system operators. HSE - Holding slovenske elektrarne considers the regional cooperation of transmission system operators essential for the improvement of interconnection capacities, which the company finds crucial for the creation of a single European energy market.

At the same time, HSE regards increasing cross-border capacities as one of the measures needed to cover the growing demand for electricity in Europe. That must, however, be accompanied by construction of new resources.

The pack of proposals will contain the draft directive amending Directive 2003/54/EC on Joint Rules of the internal Electricity Market, draft regulation on the establishment of the Agency for Cooperation of Energy Regulators and the draft regulation amending Regulation No. 1228/2003 on the conditions of access to the network for cross-border trading in electricity. The submitted proposals will also relate to the following circles of issues:

- effective cooperation between operators of transmission systems, while the enhancement of this cooperation is essential for the integration of the European electricity and gas market, and the result should be a cooperation mechanism directed at solving problems,
- the enhancement of the authority and independence of national regulators,
- the creation of an independent mechanism of the support of cooperation between national regulators, allowing the adoption of necessary decision through the establishment of the Agency for Cooperation of Energy Regulators, while the legislative proposal will bring a list of main tasks for this new community agency. The European Commission will also propose a way to manage and operate this new agency,
- the effective separation of production and electricity and gas supplies from the operation of transport networks, while this more effective "unbundling" will, of course, apply only to the operators of transmission systems, and
- improving the function of the electricity and gas market, specifying the system of exemptions, transparency and determining the framework for the gradual creation of the European retail market, as well as a framework for agreements over solidarity events to enhance the security of energy supplies in the EU.

A pragmatic approach is expected by the European Commission concerning the most discussed issues of the degree of ownership separation of production/supplies from transmission activities, which will enable the member countries to choose between full ownership separation, already existing in a number of member countries today, and a new option based on the function of an independent system operation (ISO), which will, of course,

be more demanding from the regulatory point of view and will include in the national and community level a further regulatory link permitted to ensure competitive pricing and equal access to energy networks.

Depending on the outcome of the EU Council and EU Parliament deliberations, the new proposed legislative package presented by the European Commission on 19/09/2007 might have far reaching consequences on both the internal and the external dimensions of the energy and natural gas markets⁴⁻⁵⁾. It is necessary to give supports the Commission's aim to achieve a fully functioning internal market. This requires⁶⁻⁸⁾ :

- effective application of the current legislation,
- non discriminatory access and system operation,
- stable regulatory framework conducive to support investment needs for Europe's supplies,
- improved regulatory process,
- improved TSO co-operation,
- the need for investments to secure supplies in Europe,
- The lack of legal unbundling and insufficient managerial separation of transmission and distribution system operators to ensure their independence,
- Insufficient legal unbundling of TSO/DSO to guaranty independence,

On the question on unbundling is necessary stressed the following:

- any solution must be implemented coherently and must be proportioned,
- ISO is a possible alternative to be studied,
- other feasible solutions may exist,
- better, well targeted regulation should be sought.

Any future legislation should aim at a well functioning internal market and at preserving the ability of energy companies to become globally competitive, to invest and to determine their portfolios and their long term strategies. In this respect, I see it is necessary the need for EU external policy to support dialogue and partnership under a general umbrella of reciprocity with producing countries as a way to strengthen European security of supply.

EFFECTIVE AND EFFICIENT UNBUNDLING OF TRANSMISSION SYSTEMS OPERATORS (TSO)

First case:

Assets, equipment, staff and identity ⁹⁾

2. TSOs shall be equipped with all human, physical and financial resources of the vertically integrated undertaking necessary for the regular business of electricity transmission; in particular;

2.1. Assets that are necessary for the regular business of electricity transmission shall be owned by the TSO.

2.2. Personnel necessary for the regular business of electricity transmission shall be employed by the TSO.

2.3. Leasing of personnel and rendering of services from to any branch of the vertically integrated undertaking performing functions of generation or supply shall be limited to cases with no discriminatory potential and be subject to approval by national regulatory authorities in order to exclude competition concerns and conflicts of interest

2.4. Appropriate financial resources for future investment projects shall be kept available in due time.

The activities deemed necessary for the regular business of electricity transmission mentioned in paragraph 2 shall at least include:

- a) representation of the TSO and contacts to third parties and the regulatory authorities ,
- b) granting and managing third party access,
- c) Collection of the access charges, congestion rents and payments under the inter transmission system operator compensation mechanism in compliance with Article 3 of Regulation (EC) No. 1228/2003,
- d) Operation, maintenance and development of the transmission system,

- e) Investment planning ensuring the long-term ability of the system to meet reasonable demand and guaranteeing security of supply,
- 3. TSOs shall be organized in the legal form of a joint – stock company,
- 4. The TSOs shall have its own corporate identity, significantly different from the vertically integrated undertaking with separate branding, communication and premises,
- 5. TSOs account shall be audited by another auditor than the one auditing the vertically integrated undertaking and all its affiliated companies.

Independence of the TSO management, chief executive officer / executive board

- 6. Decisions on the appointment and on any premature termination of the employment of the chief executive officer/members of the executive board of the TSO and the respective contractual agreements of the employment and its termination shall be notified to the regulatory authority or any other competent national public authority. These decisions and agreements may become binding only if, within a period of 3 weeks time after notification, to the regulatory authority or any other competent national public authority has not used its right of veto. A veto may be issued in cases of appointment and respective contractual agreements if serious doubts arise as to the professional independence of the nominated chief executive officer/member of the executive board, or in the case of premature terminations of employment and respective contractual agreements, if serious doubts, exist regarding the reasoning for this measure.
- 7. Effective rights of appeal to the regulatory authority or another competent national public authority or to a court shall be guaranteed for any complaints by the management of the TSO against premature terminations of their employment
- 8. After termination of employment in the TSO, chief executive officers/members of the executive board shall not participate in any branch of the vertically integrated undertaking performing functions of generation or supply for a period of not less than 3 years.

9. The chief executive officer/members of the executive board shall not hold any interest in or receive any compensation from any undertaking of the vertically integrated company other than the TSO. His/their remuneration shall in no part depend on activities of the vertically integrated undertaking other than those of the TSO.

10. The chief executive officer or the members of the executive board of the TSO may not bear responsibility, directly or indirectly, in the day-to-day operation of any other branch of the vertically integrated undertaking.

11. Without prejudice to the provisions above, the TSO shall have effective decision making rights, independent from the integrated electricity undertaking, with respect to assets necessary to operate, maintain or develop the network. This should not prevent the existence of appropriate coordination mechanisms to ensure that the economic and management supervision rights of the parent company in respect of return on assets, regulated indirectly in accordance with Article 22 c, in a subsidiary are protected in particular, this shall enable the parent company to approve the annual financial plan, or any equivalent instrument, of the transmission system operator and to set global limits on the levels of indebtedness of its subsidiary. It shall not permit the parent company to give instructions regarding day-to-day operations, nor with respect to individual decisions concerning the construction or upgrading of transmission lines, that do exceed the terms of the approved financial plan, or any equivalent instrument.

Grid development and powers to make investment decisions

TSOs shall elaborate a 10-year network development plan at least every two years. They shall provide efficient measures in order to guarantee system adequacy and security of supply.

12. The 10-year network development plan shall particular

a. indicate to market participants the main transmission infrastructures that ought to be built over the next ten years.

b. contain all the investments already decided and identify new investments for which an implementation decision has to be taken in the next three years.

13. In order to elaborate this 10-years network development plan, each TSO makes reasonable hypothesis about the evolution of generation, consumption and exchanges with other countries, and takes into account regional and European-wide existing network investment plans. TSO shall submit in due time the draft to the competent national body.

14. The Competent national body shall consult all relevant network users on the basis of a draft for the 10 year network development plan in an open and transparent manner and may publish the result of the consultation process in particular possible needs for investments.

15. The competent national body shall examine whether the 10- year network development plan covers all investment needs identified in the consultation. This authority may oblige the TSO to amend his plan.

16. Competent national body in the sense of paragraphs 24, 25 and 26, may be the national regulatory authority, any other competent national public authority or a network development trustee constituted by TSO's. In the latter case, TSOs shall submit the drafts of the statutes, of the list of members and of the rules of procedure to the approval of the competent national public authority.

17. If the TSO rejects to implement a specific investment listed in the 10-year network development plan to be executed in the next three years. Member States shall ensure that the regulatory authority or any other competent national public authority have the competence for one of the following measures, either:

1/ request by all legal means the TSO to execute his investment obligations using his financial capacities, or,

2/ invite independent investors to tender for a necessary investment in a transmission system and may oblige the TSO:

- to agree to financing by any third party,
- to agree to building by any third party or to build the respective new assets and
- to operate the respective new asset.

The relevant financial arrangements shall be subject to the approval of the regulatory authority or any other competent national authority.

In both cases, tariff regulation shall allow for revenues that cover the costs of such investments.

18. Competent national public authority shall monitor and evaluate the implementation of the investment plan.

Decision making powers regarding the connection of new power plants to the transmission grid

19. TSOs shall be obliged to establish and publish transparent and efficient procedures for non-discriminatory connection of new power plants to the grid. Those procedures shall be subject to the approval of national regulatory authorities or any other competent national public authority.

20. TSOs shall not be entitled to refuse the connection of a new power plant on the grounds of possible future limitations to available network capacities, e.g. congestion in distant parts of the transmission grid. The TSO shall be obliged to supply necessary information.

21. TSOs shall not be entitled to refuse a new connection point, on the sole ground that it will lead to additional costs linked with necessary capacity increase of grid elements in the close-up range to the connection point.

Regional cooperation

22. When the cooperation between several countries at a regional level encounters significant difficulties, following the joint request of these countries the Commission may designate, in agreement with all Member states concerned, a regional coordinator.

23. The regional coordinator shall promote at a regional level the cooperation of regulatory authorities and any other competent public authorities, network operators, power exchanges, grid users and market parties. In particular, he shall:

- a) promote new efficient investments in interconnections. To this end, he shall assist TSOs while elaborating their regional interconnection plan and contribute to the coordination of their investments decisions and where appropriate, of their open season procedure.
- b) promote the efficient and safe use of the networks. To this end, he shall contribute to the coordination between TSDs national regulatory authorities and other competent national public authorities with the elaboration of common allocation and common safeguard mechanisms.
- c) submit a report to the Commission and Member states concerned every year on the progress achieved in the region and on any difficulty or obstacle that may hinder progress.

Proposal for a directive of the European Parliament and of the council amending Directive 2003/54/ec concerning common rules for the internal market in electricity - how to resolve the dispute between member states in order the package is adopted in 2008

For example:

1) Justification

Some of Member states EU give support the efforts of the European Commission regarding the creation of a functioning single market with electricity. It simultaneously considers as a fundamental prerequisite for the functioning of the market, besides the sufficient production capacities, also the sufficient and accessible pan-European transmission capacities. Therefore, these states promote harmonisation of the regulation procedures and regional coordination of the transmission systems. With regard to these aims, some of Member states EU support the objectives and intentions of the European Commission in the area of cross border trade with electricity with a view to create a single market at least at regional level. The cooperation at regional level is fundamental ¹⁰⁾.

Nevertheless, some of Member states EU are not sure whether the appropriate instruments were chosen to achieve this goal. It considers that some of the proposed solutions do not take into account the differences in functioning of the national markets with electricity, previous experiences during the integration of national markets, as well as the different approaches of the Member States, as regards the investments into the transmission networks. Too much emphasis is given to the ownership of the assets and not to the operation and functioning of the grids. At the present time, the assets become less important than the system services, cross border issues and cooperation amongst TSOs.

The current approaches regarding the transmission or distribution, their tasks and the role in the electricity market were formed at the time when, in Europe, there were many individual electricity „markets“ (or in other words, the markets did not exist) within individual Member States and the international cooperation of transmission system and their interconnection did not, in fact, exist. Currently, we are in a situation where the EU has fixed as one of the fundamental objectives of the energy policy the security of supply, sustainability, environmental protection and the creation of a single functioning electricity market at the European level.

According to some of Member states EU it is necessary to reconsider the definition and designation of roles and tasks notably of transmission system. In a view to ensure sufficient and accessible transmission capacities for international trade with electricity, this redefinition should enable that the role and the tasks of the transmission system (necessary for functioning of a single electricity market at the European level) regarding the international interconnection and cooperation of transmission systems are set apart from the roles and tasks that are being ensured by the transmission systems only at the level of a Member State. Subsequently, it will be easier to ensure necessary degree of cooperation of the transmission system at the European level (firstly, at regional level at least) and de facto the transfer of liability, management and control over the relevant roles of transmission system from national to the European level.

Therefore, some of Member states EU consider as important to modify the proposal for a Directive of the European Parliament and of the Council amending Directive 2003/54 in a way that in every Member State, it will be possible to build such a model of the market with electricity and such a structure of the market participants enabling the cooperation of the

transmission system operators at the European level throughout the creation of the European Network for Transmission System Operators for Electricity, but also throughout the creation of a pan-European transmission system operator responsible for cross border transmissions and connected activities.

The gist of the amendments consists in the fact that the both options of ownership unbundling and the ISO should be brought on the same footing. The Member States should have the right to choose – at the moment of entry of the Directive into force – between these options irrespective of the structure of the market within their territory at the given time. This option will better enable the creation of the regional, and subsequently, pan-European system operator responsible for cross border issues.

The amendments stated below reflect the afore mention opinion and simultaneously result in a simpler and shorter formulation of the wording of the directive.

For an example:

- b) Amendment 2.
Article 8 (1) a):

To be deleted

(a) each undertaking which owns a transmission system acts as a transmission system operator,

Justification:

The deletion of this letter in Article 8 implies that the transmission system operator could be not only the owner of the transmission assets as a whole, but also could have no assets at all or could be the owner of part of transmission assets. Nevertheless, and in any case, the same requirements would apply.

- f) Amendment 6.
Article 10 (1) c):

*Where the transmission system belongs to a vertically integrated undertaking **on entry into force of this Directive or where a Member state considers as appropriate in a view to ensure the conditions for effective functioning of the European Network for Transmission System Operators (TSO) for Electricity or the creation of a supra-national transmission system operator.** Member States may grant derogations from Article 8(1), provided that an independent system operator is designated by the Member State upon a proposal from the transmission system owner and subject to approval of such designation by the Commission. Vertically integrated undertakings which own a transmission system may not in any event be prevented from taking steps to comply with Article 8(1).*

Justification:

The objective of this amendment is to bring the TSO and ISO models on the same footing as a way to provide a coherent model for system operation throughout Europe and to facilitate the establishment to region or pan – European system operators. The Member States should have the possibility to choose between two equal options (ownership unbundling and creation of the independent system operator - ISO).

CONCLUSION:

The agreement regarding unbundling on the territory of EU will be not easy and the discussion will last for just a longer time. I have shortly focused on two different points of view about solving this problem of unbundling, namely by a group of EU states which doesn't directly support separating from vertical corporations and another group of EU states in the second part of this essay which support separating. In my opinion it is necessary to reconsider the definition and designation of roles and tasks notably of transmission system (TSO).

Vertically integrated dominant energy companies are designated as the major disrupters of the market environment impeding market access to competitors. Therefore proposals for either forced separation or so called independent system operator (ISO) have been raised. Alternative Proposal of 8 EU countries for ownership unbundling and independent ISO operator – so called Effective and Efficient Unbundling ¹¹⁾ – (EEU). In principle, the EEU defines making the current system more rigorous by introducing duty to elaborate so called

compliance program for each TSO (a kind of TSO functioning Codex) and regulators' supervision over its performance. Though the Commission formally welcomed this proposal and promised discussion over it, its current position towards this proposal is negative.

Probably ISO regarding gas unbundling is not a real alternative from reason:

- has never been implemented in gas industry,
- leads to a loss of all competencies (for example technical,...
- creates problems of repatriation of responsibilities, industrial and financial risks.

As says Anders Pleydrup about unbundling ¹²⁾:

The spot exchanges must be unbundled, when implicit auction becomes the day-ahead congestion management system:

- As they get a monopoly: only the spot exchanges can carry out day-ahead cross border power trading. Naturally, you may install a system granting the players the opportunity to compete with the spot exchanges for day-ahead cross-border capacity.
 - However, even with such a system in place, the spot exchanges are granted a special status.
- Hence, they become regulated entities like the TSOs!

SOURCES:

1. COMMISSION OF THE EUROPEAN COMMUNITIES, Commission Staff Working Document, Brussels, 10.1.2007,
2. ČEZ info, www.cez.cz
3. <http://www.europa.eu.int/eur-lex/en/index.html>
4. EUROPEAN UNION, Rada Evropské unie, Závěry předsednictví, Akční plán Evropské rady 2007-2009, Energetická politika pro Evropu, CONCL 1, 7224/07, Brusel 9.3.2007,
5. EUROPEAN PARLIAMENT, Committee on Industry, Research and Energy, Working Document on Prospect for the internal gas and electricity market 2004-2009, Committee on Industry, Research and Energy, DT/662867EN.doc. PE 388.364v02-00, 16.4.2007
6. CONSTELLATION ENERGY, Third Liberalization Package 19th September 2007, Emart energy Conference, Amsterdam, November 21st, 2007,
7. ENERGY COMMUNITY, General problems in opening markets properly, EMART energy Conference, Amsterdam, November 21st, 2007,
8. Pierre BORNARD, ETSO Steering Committee Chairman, Will there be a single ISO for part of continental Europe? Amsterdam, 2007,
9. SLOVENIAN PRESIDENCY OF THE EU 2008, Some Member States EU, Effective and Efficient Unbundling of Transmission System Operators, Ljubljana, 2008
10. ČEZ, JUDr. Zuzana KREJČÍŘÍKOVÁ, proposal for a directive of the European parliament and of the council amending directive 2003/54/ec concerning common rules for the internal market in electricity - how to resolve the dispute between member states in order the package is adopted in 2008, Prague, March 2008
11. Tomáš HÜNER, Ministry of Industry and Trade, Issues discussed between EU and CZ, Prague, March 2007,
12. Anders Plejdrup HOUMØLLER – Director Business Development Nord Pool Spot AS, Linking Nordic and Continental markets, How to establish a single European power market, EMART Energy Amsterdam, November 21,2007,

Florian MARGAN,
f.margan@quick.cz
Ševčíkova 2728/7
130 00 Praha 3