<%@LANGUAGE="VBSCRIPT"%> <% Dim Recordset1 Dim Recordset1_numRows Set Recordset1 = Server.CreateObject("ADODB.Recordset") Recordset1.ActiveConnection = MM_ifiec_STRING Recordset1.Source = "SELECT * FROM electricity ORDER BY volgorde DESC" Recordset1.CursorType = 0 Recordset1.CursorLocation = 2 Recordset1.LockType = 1 Recordset1.Open() Recordset1_numRows = 0 %>

INTERNATIONAL FEDERATION OF INDUSTRIAL ENERGY CONSUMERS

EUROPE

Head Office: 119 Chaussée de Charleroi B- 1060 Brussels

Tel: 32 2 542 06 87 Fax: 32 2 542 06 92

IFIEC Europe

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Public Hearing on the Completion of the Internal Energy market

Thursday, 14 September 2000
The view of the industrial energy consumers

Achieving a fully-competitive electricity market

1. Introduction

IFIEC Europe fully endorses the recommendations of the Lisbon summit in March, 2000, and the conclusions of the Council of Energy Ministers of 30 May 2000 calling for an acceleration of the liberalisation of the internal electricity market. The positive consequence for industrial energy consumers throughout Europe is the potential availability of lower prices and a larger degree of choice and flexibility in negotiating competitive supply.

Progress in achieving **effective** competition can be monitored by the take-up of alternative supply offers, the emergence of new market entrants (IPPs, traders, etc.) and the improvement of prices. In the majority of Member States throughout the EU, however, such progress has been hampered by high levels of market concentration and numerous barriers to entry, the most important of which are the lack of effective unbundling and inefficient access to the network.

IFIEC Europe urges European and National public authorities to give priority attention to transmission and distribution related issues in the current review of the liberalisation process and would like to draw attention to the following key issues to be considered for amendment.

1. Market Opening

Electricity market liberalisation serves primarily the interests of those customers who are included in the eligibility criteria. As the Member States of the European Union have so far opted for different criteria of eligibility many customers today still do not have the right to choose their supplier. The Electricity Directive (96/92/EC) only calls for a minimum market opening of about 35% of total demand by the year 2003. As many Member States already

today open their markets beyond this threshold, IFIEC Europe urges the Commission to set more ambitious targets. Following such Members as Finland, Germany, Sweden and the UK these aims should envisage a complete market opening in the very near future.

Despite the legal requirements concerning customer eligibility some Member States have still not fully implemented the Electricity Directive. Important decrees to make national laws applicable are not enacted yet. IFIEC Europe therefore asks the Commission to intensify monitoring of the effective implementation of European legislation by national authorities. Clear milestones should be set and penalties for non compliance defined.

Recommendation:

. Require full market opening for all customers in all Member States in the near future

. Set milestones, intensify monitoring and implement penalties where Member States fail to comply fully with the Directive

2. Unbundling

In liberalised markets, electricity transmission and distribution remain de-facto monopoly activities which need to be treated accordingly. As for the foreseeable future, transmission will encompass relatively scarce infrastructure resources. Availability of these resources at lowest cost is of central importance to the whole electricity market. Regulation and/or control of transmission networks needs to pay particular regard to ensuring that :

- all market participants are entitled to use the network on equal terms. Any form of discrimination between different users of the network is unacceptable,

- costs are properly controlled and accounted for, and monopoly profits from transmission and distribution service providers do not exceed the low level of risk these businesses face.

In the absence of direct competition between network operators all efforts should be made by the Commission to introduce yardstick competition by collecting and publishing price comparisons.

As a prerequisite to fulfil the above objectives the Electricity Directive demands for unbundling of the management of transmission system operators (Art. 7 para. 6) as well as for separate accounts of generation, transmission and distribution activities (Art. 14 para. 3). But from today's experience industrial energy customers consider these provisions insufficient.

It is IFIEC Europe’s experience that in cases where grid prices are becoming transparent, those prices are far from cost-efficient. We question whether all cost elements not directly related to transmission have been excluded and believe insufficient incentives exist to ensure costs are properly controlled and accounted for.

IFIEC Europe therefore reiterates its call for clear unbundling of integrated utilities. Besides accounting and management unbundling, transmission and distribution should be completely separated from the other activities (generation and supply/trading). In the Electricity Directive no clear unbundling is so far required for supply activities which are clearly open for competition. In order to ensure non-discrimination and efficiency and avoid cross-

subsidisation and conflicts of interest within integrated utilities, IFIEC Europe recommends that the network services be organised and managed as independent legal entities.

Transmission and distribution should therefore be legally unbundled from generation as well as from trading and supply activities. This is the clearest approach to ring-fence such monopoly services and to make their services available to all market participants.

In order to ensure confidentiality of highly-sensitive commercial information regarding market transactions, grid operators should be subject to a strict code of conduct in the exercise of their technical and economic functions.

Recommendations:

. Require clear separation of transmission and distribution from generation, trade, supply

. Reinforce unbundling of network operators by creation of separate legal entities

3. Access to the network

Clear legal unbundling is only one prerequisite of non-discriminatory, efficient and transparent access to the electricity system. In the electricity sector the networks constitute an essential facility that need to be open for access by all interested parties. Only under exceptional circumstances will the construction and operation of further direct lines help to open competition. Therefore, **efficient access to the network system is the key to a competitive electricity market**. This fundamental has been transposed into European law by the Electricity Directive.

At the same time the Electricity Directive is rather vague on the details of network access. IFIEC Europe therefore suggests to consider the following aspects in any further clarification:

3.1. Scope of network services:

Network services comprise three primary elements: connection, use of system and ancillary services.

Capital works relating to connections should be according to clearly defined standards and open to competitive tender. Ancillary services (frequency and voltage control, primary and secondary reserve, balancing power, reactive power and billing/measurement) need to be procured on a non-discriminatory, efficient and transparent basis.

Recommendations:

. Connection costs are best controlled through a competitive tendering process.

. Insist network services be provided for on a competitive basis.

3.2. Costs and Pricing of Network Services

Transmission costs need to be ring-fenced to exclude any charges not directly related to the grid infrastructures: costs should therefore be limited to “useful life-time” amortisation,

operating, maintenance and grid enhancement charges, including costs related to transmission losses. Ancillary services must be charged separately. Miscellaneous costs resulting from energy policy decisions must not be charged to transmission or distribution.

The management of grid investment and operations should be conducted in the most efficient manner possible, with the aim of achieving the lowest possible costs that are compatible with customer requirements. Transmission pricing needs to be globally cost-reflective and stable, based on rate-of-return and efficiency criteria. In particular, the return on investment should reflect the low level of risk associated with this activity.

All elements of network pricing need to be made transparent by the system operators through publication. Only transparency and control offer the chance of efficient operation and acceptable price levels of such monopoly activities. Therefore the current obligation resulting from the Electricity Directive Art. 17 para. 3 to publish guiding values of grid prices should be clarified. IFIEC Europe supports the Commission's recent initiatives to monitor and compare prices.

Recommendations:

. Network prices must be minimised to enable competition to flourish.

. Yardstick competition must be established quickly.

3.3. Cross-border transmission issues

In many Member States the basic prerequisites of a competitive electricity market cannot be achieved without the stimulus of cross-border exchanges. This essential issue which is currently outside the scope of the Electricity Directive must be addressed by EU structural measures as quickly as possible.

As concerns the overall assessment of costs related to cross-border exchanges, it is questionable whether the total sum suggested (over 200 Million Euros/year) is justified on the basis of actual costs incurred by the use of cross-border grids. Cross-border costs should be clearly justified on a consistent basis, in particular to avoid double counting.

Any possible cross-border costs justified under efficient operation of all concerned TSOs should not be financed by a levy on exporters. Industrial energy users are convinced that the current suggestions by the European TSOs to charge exporters of electricity from one Member State to the other with a cross-border fee of about 2 Euro/MWh is in contradiction to the common objectives of completing the internal market for electricity.

As international grid connections serve the important function of enhancing overall performance, such infrastructure is of value to all grid users who should contribute to the overall costs. Cross-border lines are frequently used to conduct power flows irrespective of any programmed exports. They are also often used to enhance system security of the interconnected system. For such reasons, placing the burden of cost-recovery exclusively on exporters would not be globally cost-reflective, and therefore not justified.

As concerns pricing methodology, IFIEC Europe suggests to finance any possible cross-border costs by revenues from regular grid prices. Grid prices for all network customers should be based on total energy being taken out or being injected into the grid irrespective of

individual commercial transactions. Such a pricing system would be completely non-transaction based and would make any specific t-component superfluous.

Industrial energy customers also support the concept of a two-term postage stamp price: a generation price component (G) should be based on electricity being supplied into, and a load price component (L) should be based on electricity being taken out of the system. Such G and L terms should be harmonised across the Internal Market.

As agreed by the last Florence Forum in March 2000, European grid operators should create an inter-TSO-compensation scheme to compensate for different cost levels through cross-border electricity flows. Such a scheme should safeguard that grid operators that are more frequently utilised to facilitate electricity transits receive payments in order that grid prices in such transit areas can be adopted accordingly. Once the internal energy market has been completed, the notion of "cross border" itself should disappear. At that time, all compensation schemes should be based on the interactions between different system operators.

Recommendations:

. Challenge the level of the overall cross-border costs already proposed

. All users benefit from, and should contribute to, cross-border costs.

. Pricing methodology should be based on harmonised components G+L.

. Cross-border prices should be non-transaction based (a "t-factor" should be rejected).

3.4. Congestion Management

Besides pricing of network services, the allocation of network capacities in cases of over-demand is of central importance for competitive access to the network. Prior to the opening of the electricity market congestion management was internalised by utilities and consumers were unaware of its impact or cost. Neither was there any attempt to allocate such costs in an equitable manner.

The introduction of competition has brought this issue into the open and it needs to be dealt with in an economically efficient way. IFIEC Europe has growing concerns that premature solutions are being proposed which may impact in a very negative manner upon competition.

IFIEC Europe believes that consistent and transparent solutions dealing with constraint management should be implemented throughout Europe, taking into account the specifics of the continental and "island" systems. The primary features of any scheme from the industrial consumers' point of view are equal treatment, transparency and efficiency resulting in low costs for all network users. In addition, it is essential that any scheme allows for maximum use of interconnector/transmission capacity to ensure that prospects for the development of cross-border trade are not inhibited.

The European TSOs have been asked by the Commission to propose a scheme before the end of 2000 whereby available transmission capacity (ATC) could be allotted among network users in a transparent and non discriminatory manner.

Among the possible solutions, the concept of capacity auctioning is under study. Theoretically, under pure market conditions, where competition is clearly established among a sufficient number of actors to render the market dynamic and fluid, and where no one network user dominates the market, an auctioning scheme might be able to function properly. In reality such a situation will clearly not exist for a long time to come.

IFIEC Europe believes that any capacity auction system will be subject to abuse by dominant utilities who are, in many cases, owners of public grids and dispose of substantial financial resources in order to influence auction bids and prices. To date, large consumers are unaware of any positive experience where auctions have been introduced in gas and electricity markets. Revenues from auctions could provide an incentive to maintain bottlenecks. For this reason, **industrial energy users strongly oppose the introduction of any auctioning scheme in Europe in the immediate future.**

IFIEC Europe suggests that approaches based on re-dispatching and counter-trading be further investigated.

Recommendations:

. Ban capacity auction schemes

. Investigate re-dispatching and counter-trading approaches

. Ensure non-discrimination, transparency and efficiency in congestion management

<% Recordset1.Close() Set Recordset1 = Nothing %>