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Committee on Industry, External Trade, Research and Energy

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on Proposal for a directive of the European Parliament and the Council
amending Directive 96/92/EC concerning common rules for the internal market
in electricity

Committee on Industry, External Trade, Research and Energy

Rapporteur: Claude Turmes

The Revision of the Electricity Market Directive

EU Parliament internal rules only allow for a 4-page explanatory. A more complete version of this memorandum with extensive statistics and examples can be found under <http://www.eu-energy.com/Electricity.html> or tel. 0032-2-2845246 (office of MEP Claude Turmes)

Quantitative issues, like the speed of market opening, have dominated the debate around liberalisation. Although harmonised dates for full market opening are a prerequisite for a well functioning market, qualitative aspects must be brought to the centre of the political debate if a truly functioning market is to be established.

1) A non-biased market for generation

The Commission's proposal puts insufficient emphasis on equal market conditions for different competing energy sources and largely ignores commercial and administrative distortions which favour some market actors.

Take care of security of supply aspects:

The California crisis shows the need to monitor the evolution of generation in liberalised markets. The measures proposed by Commission – tendering schemes, monitoring of the market – should also be followed by the Parliament. The Commission's paper largely ignores the potential of energy efficiency measures to increase security of supply, which must be redressed.

A level playing field for sustainability:

New investments in sustainable electricity production have to compete with the existing fossil fuel or nuclear generation that have received significant state aid.

The right price. In parallel to the Directive a strategy has to be developed to reduce state aid and subsidies to conventional energies and to internalise external environmental costs. Until then sustainable energy production should receive protection in the market through this Directive, through sector Directives and special EIB investment funds.

Environmental Reciprocity. Certain Member States are doing a lot of progress on renewables, CHP and DSM while others are lagging behind. In order not to bring the frontrunners in a competitive disadvantage, a sort of environmental reciprocity clause should be adopted. An environmental reciprocity clause would allow Member States to ban the import of electricity if the exporting country fails to meet targets such as those in the Renewable Energy Directive and future Directives on Combined Heat and Power or Energy Efficiency.

Electricity Importation: There was a seven-fold increase of electricity imported from countries in Central Europe between 1996-2000. A number of States (Austria and Luxembourg) have expressed concerns that this may lead to a distortion of the market and passed appropriate legislation. The European Parliament has already called for imported electricity to meet EU environmental standards. The Directive should require the same environmental and social minimum standards for imported electricity as for new generation and the same disclosure requirements.

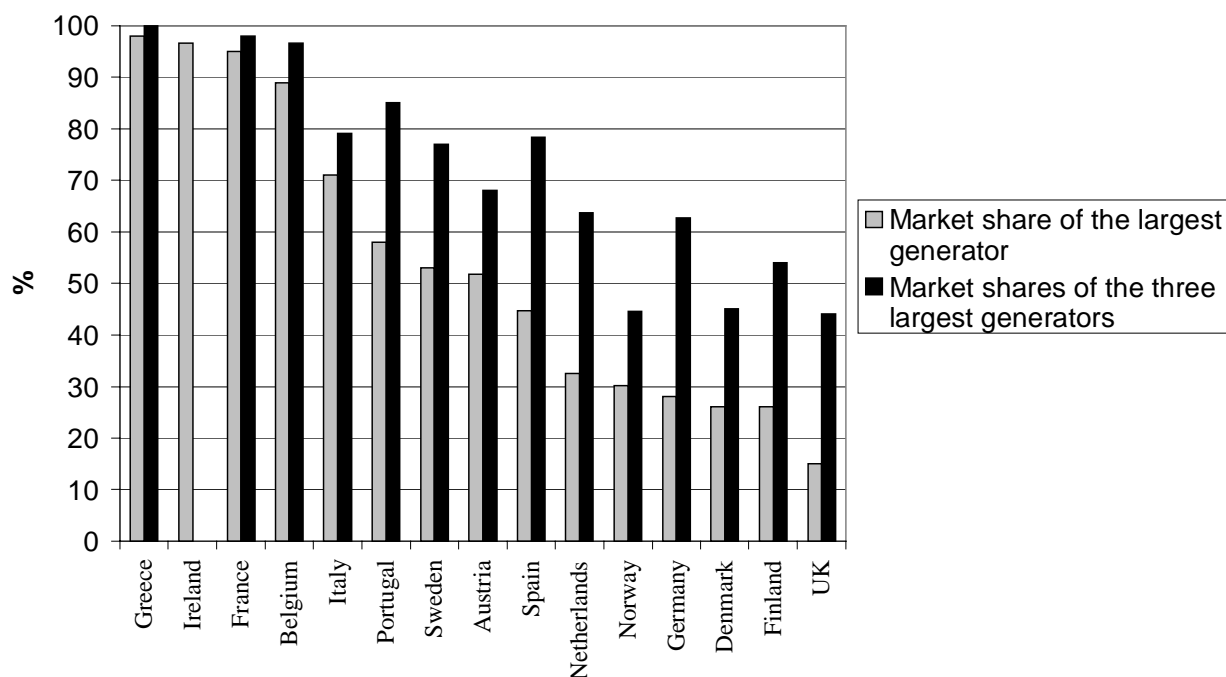
A level playing field for market actors:

In the creation of a single market from 15 national markets there is a need to harmonise the framework conditions for the different actors.

Market Concentration: The avoidance of market dominance is of particular importance in this sector as electricity cannot be stored and therefore the possibility to exercise market power is much greater than in other commodities. The revised Directive proposes that market concentration is reviewed, but clear guidelines are required. Three problems have to be addressed:

- in some Member States operators control more than 50% of the market;
- in other Member States the sale of and merger between electricity companies have been more guided by industrial policy interests rather than by transparent merger control;
- the ten largest companies control over 50% of the EU market. Further mergers of these companies are planned and it is expected that within a few years only between 5-8 companies will dominate.

Market Power of Electricity Companies in Member States



Source: Jean-Michel Glachant

In order to analyse market dominance it is crucial to define the relevant market. Due to the physical constraints of electricity the relevant market is not the EU 15 but is often limited to just one or two countries. Building more interconnection will not dramatically improve this situation.

Missing harmonisation of the economic framework conditions: Market dominance, cross subsidies from captive clients and collusion of interests between grid and generation owners give competitive advantages that have to be addressed. Other relevant market distortions are stranded cost arrangements, the disposability of funds (such as the German decommissioning fund) and divergent national regulations, e.g. decommissioning requirements.

2) A functioning retail market

If the liberalised market is to bring universal benefits then the organisation of the retail (sales) market has to be completed in a way that gives full transparency and information to the final consumers.

Complete Market opening:

As of early 2000, it was estimated that around 70% of the supply market was open to competition, rather than the 26% required under the terms of the Directive. Uneven market opening causes a distortion of competition in the energy market. The Directive calls for retail market opening for non-domestic customers by 1st January 2003 and for domestic customers by 1st January 2005. Any further delay of opening up the markets may only be tolerated under very strict cross-subsidy control by the national regulators.

More market power to small customers:

Whereas large industrial customers are able to negotiate reductions in their bills, this has not happened to the same degree for the majority of citizens. The Directive should seek to improve market power for small customers by favouring aggregation and by giving a greater role to local utilities. Monitoring transparency of contracts, maximum fees for connection costs and costs of metering should all be functions of the regulating bodies.

Table 2 Competitive Activity and Prices

	Estimated customers switching supplier (% demand)		Average prices to final customers (€/MWh) July 2001	
	large users	other	large users	households/ small commercial
Austria	5-10%		na	98
Belgium	5-10%		68	120
Denmark	n.a.		56	68
Finland	30%	10-20%	36	55
France	5-10%		51	87
Germany	10-20%	<5%	61	122
Greece	nil		54	76
Ireland	30%		60	101
Italy	10-20%		77	110
Neth	10-20%		62	94
Portugal	<5%		59	106
Spain	<5%		52	88
Sweden	100%	10-20%	34	52
UK	80%	>30%	58	91

Source: Benchmarking report of the Commission SEC (2001) 1957

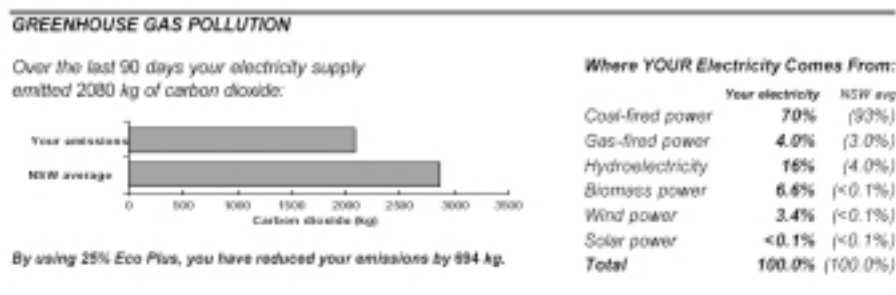
Full disclosure of information:

The proposed Directive includes a requirement for consumers to be given information about the sources, price and certain environmental impacts of fuels. The mandatory disclosure of electricity sources is increasingly common. In the USA 19 States have disclosure legislation in place. While in Austria from the October 2001 utilities have to disclose the production sources; similar legislation is expected in the Netherlands.

The Parliament should support the Commission’s initiative, but refinements are required to ensure that appropriate information is placed both on the bills of consumers and on advertising. The Directive should also ensure that in every country an independent body produces comparative information for customers.

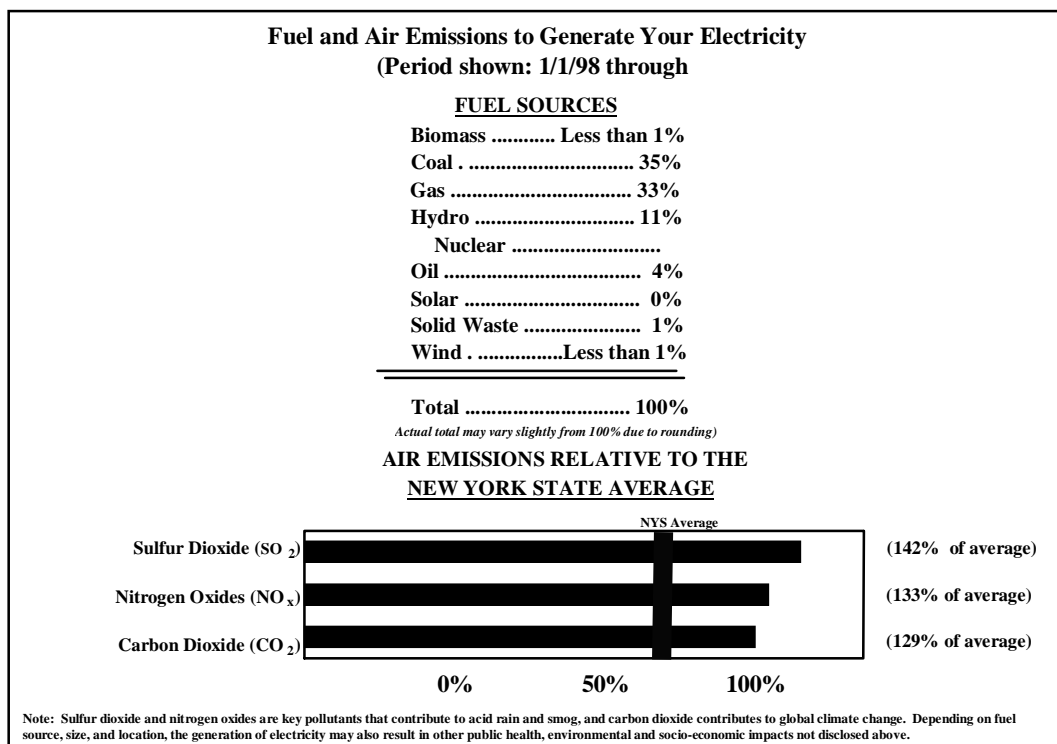
Electricity Disclosure in New South Wales (Australia)

Draft label



Source: Öko-Institut 2001

Sample Label



Source: Öko-Institut 2001

Preventing negative effects on electricity demand:

One of the biggest problems of the liberalised market is the negative impact on energy efficiency. If the EU is to take seriously the environmental and security of supply concerns, this market failure has to be addressed. In addition to technical measures, such as improving the efficiency of electric appliances, structural measures have to be included within the Directive. Increased demand side management not only for retailers but also for transmission and distribution companies is also required. Funding mechanisms to finance Demand Side Management (DSM) for small customers must be provided.

Municipal Utilities:

Local utilities are important actors in the newly created markets and can help to strengthen the market power of small customers and to implement demand side policies. The proposed Directive allows utilities supplying less than 100 000 customers to be exempt from distribution unbundling. Such a scheme should be encouraged but better defined. Therefore all utilities which have less than 200 000 customers should be exempt and it should also apply to all municipal and community utilities regardless of their size. However, it is essential that all distribution service operators (DSOs) which are majority owned, directly or indirectly, by another electricity company, in this regard are considered as one DSO.

3) A non discriminative grid

Insuring neutrality:

As not all countries have separated the ownership of grid and commercial activities in the

generation and retailing sectors, the regulating bodies have an essential role to ensure the neutrality of the grid actors. Recent experience shows that transparent ex-ante price setting is a prerequisite for a well functioning market. For better congestion management, more transparency and new instruments have to be implemented.

Guaranteeing security of supply:

The quality of the grid is key for the well functioning of the economy and society. The grid operators must be able to maintain and eventually reinforce the infrastructure.

De-Centralised Power Sources:

There is a need to address the bias in investment and operating regimes towards centralised production and the transmission systems. Decentralised power systems have significant avoided cost advantages, as new grid infrastructures can be avoided or existing ones freed up, which are not always reflected in the tariffs.

4) Competent and independent regulators

The experience of the first years of liberalisation shows that strong “referees” are needed if a fair and transparent market is to be established. In the transition to full liberalisation regulators have an important role to establish, monitor and continuously adapt the structures and rules of the market. Due to the complexity of the electricity market they have also a role to advise on competition policies. The role and the activities of the 15 national regulators have to be harmonised at a minimum and co-ordination has to be established between them.

5) Public service obligations (PSOs)

The free market will not take care of certain important aspects like social exclusion, universal service, territorial aspects, security of supply and certain environmental considerations. Special attention should be devoted to this chapter of the Directive in order to allow a certain number of PSOs and to enable the creation of funds to finance these obligations.