

**National Report of the Energy Regulatory  
Office on the Electricity and Gas Industries  
in the Czech Republic in 2013**

July 2014

## List of frequent abbreviations and acronyms

<b>Czech</b>	<b>English</b>	
ČR	CR	Czech Republic
ERÚ	ERO	Energy Regulatory Office
MPO	MIT	Ministry of Industry and Trade of the Czech Republic
ČEPS	ČEPS	The Czech transmission system operator (electricity)
OTE	OTE	The market operator (OTE, a.s.)
PXE	PXE	Power Exchange Central Europe, a.s.
EEX	EEX	EEX Leipzig Energy Exchange
ÚOHS	ÚOHS	Office for the Protection of Competition
PPS	TSO	Transmission system operator
PDS	DSO	Distribution system operator
MC	MC	Market coupling
PCI	PCI	Projects of common interest
CEER	CEER	Council of European Energy Regulators
ACER	ACER	Agency for Cooperation of Energy Regulators
CEE	CEE	The Central and Eastern Europe region
EU	EU	European Union
VVN	EHV	Extra high voltage
VN	HV	High voltage
NN	LV	Low voltage
EZ	--	The Energy Act
REMIT		Regulation on wholesale energy market integrity and transparency
OZE	RES	Renewable energy sources

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# 1 Foreword

For the tenth time, the Czech Republic is presenting, through the Energy Regulatory Office, its National Report on the Electricity and Gas Industries to the European Commission, thereby meeting its reporting and notification obligation set out in the applicable Directives and Regulations.

In 2013, the activities of the Energy Regulatory Office (“Office”, “ERO”) continued to be based on Act No 458/2000 on Conditions for Business and State Administration in the Energy Industries and Amending Certain Laws (the Energy Act), in which the Czech Republic had implemented the relevant provisions of the third package. During the year, an amendment to the Energy Act was being drafted; it was necessitated by, among other things, new European legislation (most notably Directive 2012/27/EU of the European Parliament and of the Council of 25 October 2012 on energy efficiency) and the need to boost the protection of customers and consumers, which is one of the main lines of the Office’s activities.

In the past period, the Office took a number of steps to arrest energy price rises, and so mitigate the financial burden on final consumers. These mainly included measures to reduce the financial support for renewable energy sources and capping final customers’ contribution to RES.

In connection with implementing Regulation (EU) No 1227/2011 of the European Parliament and of the Council (REMIT), in 2013 the Office joined the preparations for a bill on wholesale energy market integrity and transparency, the purpose of which is to ensure well-working competition in wholesale energy markets. The bill also provides for certain issues of the Office’s cooperation with the Agency for the Cooperation of Energy Regulators and with regulatory authorities of the EU member states.

In respect of regional initiatives, the Office was actively involved in the integration of day-ahead electricity markets. In addition to market coupling in the region of seven central and eastern European countries, the Office also focused on closer Czech-Slovak-Hungarian market coupling with the outlook of Rumania joining in 2014. The Czech Republic also had to continue to devote considerable attention to the unplanned loop flows, which pose a risk to the safety of the grid and complicate the process of creating the common market. At the bilateral level, agreement was reached between the Czech and German transmission system operators on installing phase shifting transformers intended to protect the Czech transmission system against the unplanned flows.

The Czech Republic was also actively involved in discussions on the new format of the regional gas market. With a view to enhancing the security of gas supply in central Europe and diversifying sources, the key project was the Gazelle high-pressure gas pipeline, which was connected to the NET4GAS, s.r.o. transmission system.

With a view to intensifying the cooperation between national regulators in the Visegrád Four countries in the interest of enhancing a transparent regulatory environment and improving customer protection, the Office initiated the June 2013 meeting of the four regulatory authorities’ representatives in Prague. The delegates agreed to set up a permanent functional platform for exchanges of experience and consultations, and signed a Joint Statement in Budapest in November 2013 with this objective on their minds.

In 2013, the Energy Regulatory Office also granted an independence certificate to the gas transmission system operator, NET4GAS, s.r.o., which opted for the ITO model. (The independence certificate was granted to the electricity transmission system operator, ČEPS a.s., which is a fully unbundled entity in terms of ownership, as early as 2012).

## **2 Main developments in the electricity and gas markets**

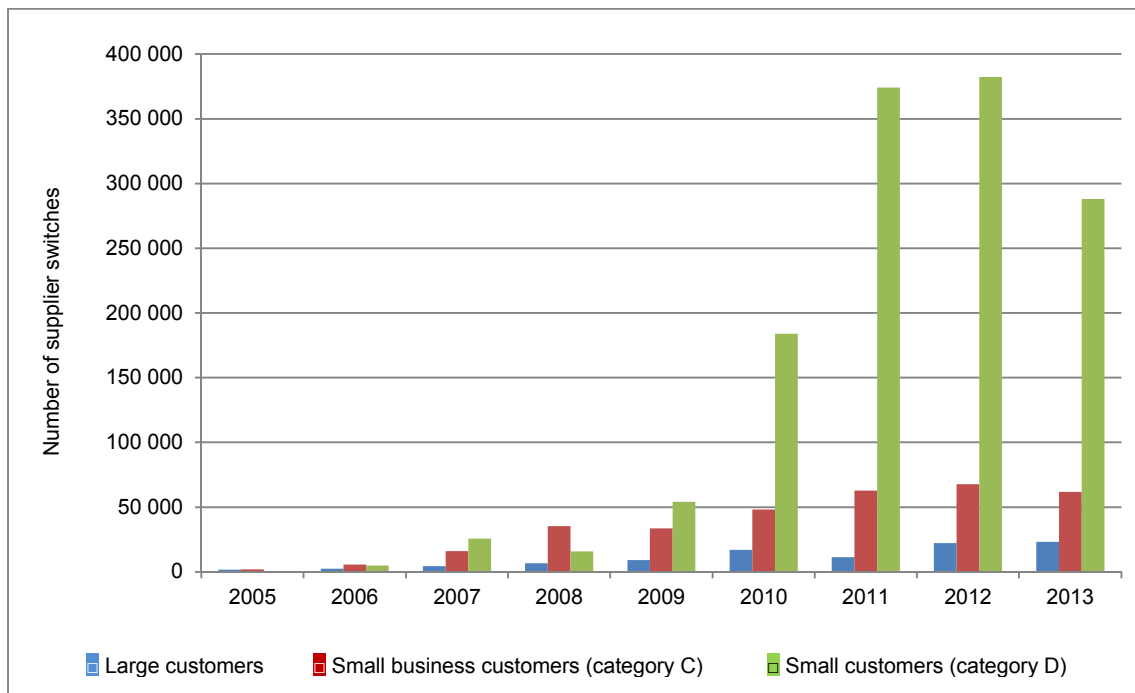
The open electricity market experienced major changes in 2013, mainly as regards supplier switches, the number of which was somewhat smaller compared with the preceding period that saw a record number. While in the preceding years companies mainly relied on peddling for customer acquisition, they have recently started to use some other tools for their growth on the energy market, such as advertising campaigns, participation in mass-scale electronic auctions for groups of customers, and acquisitions of weaker competitors. As regards the integration of the wholesale electricity market, Rumania and Poland also joined the successfully running project for day-ahead market integration in the Czech Republic, Slovakia and Hungary (Czech-Slovak-Hungarian market coupling, CZ-SK-HU MC) with prospects for their future participation. A major development in the electricity market was also the discontinuation of operating support for renewable electricity plants commissioned in 2014 and beyond.

As regards the gas market, last year saw major changes in the ownership structure of some gas companies. Compared with 2012, the rise in the number of new traders was not so steep, since the retail gas market is saturated now. Compared with the preceding period, the number of supplier switches decreased, and new traders were not able to win customers as easily as at the beginning of the gas market liberalisation. The reason is that customers who were not satisfied with their suppliers had already switched them earlier. Because of the unfair practices associated with peddling, some municipalities have prohibited this form of marketing within their limits. As regards the integration of the wholesale gas market, one of the priorities was cooperation with the Polish regulator in respect of the project for the Stork II Czech-Polish gas pipeline. The Office was also actively involved in the area of regional projects intended to create a trading region covering several countries. The integration project based on the Visegrád 4 and the Central East Europe Trading Region (CEETR) are the most relevant for the Czech Republic.

### 3 The electricity market

In 2013, the number of supplier switches dropped by approximately 100,000 customers, i.e. a decline of one-fifth. While 449,000 customers changed their electricity supplier in 2011, and the figure was 473,000 in 2012, it was only 374,000 customers in 2013. This situation can be attributed to the complications faced by customers when they want to terminate a fixed-term contract, which is liable to high penalties. A detailed view shows that the decline in supplier switching mainly concerns households. A year-on-year increase in the transfer of supply points to a different supplier was only registered in the segment of corporate customers. Chart 1 shows electricity supplier switching.

**Chart 1 Annual electricity supplier switching in the main customer categories**



Source: OTE, a.s.

On its website, the Office continuously provided the information that could help to serve for a qualified selection of suppliers. It provided information concerning the customers' options and the procedure in electricity supplier switching, the structure of the offered services, and the suppliers' prices using an interactive ready reckoner for electricity prices, and also information about the feedback received by the Office from the liberalised market. During 2013, the ready reckoner was one of the most visited applications on the Office's website. While in the preceding years most of the electricity supplier switches were attributable to customers migrating from vertically integrated companies' incumbent suppliers to alternative suppliers, in recent years the market has been so liquid that it is no longer possible to identify the main direction of supplier switches. In general, customers followed the lowest price.

Thanks to the Office's proactive effort, the charge covering the costs incurred in support for renewable electricity was capped by a law.

At the LV level, the same range of tariffs, including the conditions for awarding them, as in 2012 was maintained for small business customers (category C) and households (category D) for 2013. Special rates for electric vehicles were added.

Suppliers usually adjusted their offering prices of electrical energy once a year, i.e. as from 1 January of the new calendar year. Some suppliers also offer a product where the price of

energy depends on electricity prices at energy exchanges during the year for small customers as well, or offer a better price when the customer enters into a contract for both electricity and gas supply with the trader.

### **3.1 Network regulation**

#### **3.1.1 Unbundling**

The electricity transmission system operator, ČEPS, a.s., was fully unbundled from electrical energy producers and distributors as early as 3 September 2009, which the ERO confirmed by granting the company an independence certificate in 2012.

In respect of the unbundling of distribution system operators, Article 26 of Directive 2009/72/EC had been implemented through an amendment to the Energy Act in the preceding period, specifically through Section 25a and Section 11(1)(m) of the Energy Act.

#### **3.1.2 Technical functioning**

The rights and obligations of producers, including renewable electricity producers, are laid down in Section 23 of the Energy Act. Under Section 23(1)(a), every producer has the right to connect its installation to the electricity grid subject to the connection conditions and commercial conditions. Under Section 23(1)(b) and (c) of the Energy Act, producers also have the right to supply electricity to other market participants, to other countries, and for their own consumption.

Renewable electricity producers' entitlement to support is provided for in Act No 165/2012 on promoted energy sources and amending certain laws, as amended. The law specifies the form of support for each particular type of installation and, if applicable, for the size of installed capacity. In 2013, an amendment, enacted in Act No 310/2013, to Act No 165/2012 on promoted energy sources and amending certain laws came into force; some of its provisions entered into effect as of 2 October 2013 or 31 December 2013. In this connection there were some changes in the system of support disbursement, operating support for new RES plants was discontinued, and the final customers' contribution to RES was capped.

The new law and the change of the system necessitated a new regulatory method, which was laid down in a new public notice, no. 436/2013 on regulatory methods and procedures in the electricity and heating industries and amending no. 140/2009 on regulatory methods in the energy industries and procedures for price controls, as amended, which replaced, in respect of the electricity industry, no. 140/2009 on regulatory methods in the energy industries and procedures for price controls, as amended.

The responsibility for balancing energy rests with ČEPS, a.s., which ensures the quality and reliability of electricity supply at the level of the transmission system by means of system services. The funds to pay for these services are provided by final customers through a regulated contribution contained in the price for electricity consumed by final customers.

As regards electricity supply quality, the Office focused on preparing the inputs into electricity quality regulation for the fourth regulatory period. At the same time it set the quality indicators and their parameters in electricity distribution for the regulatory year 2014. The objective of quality regulation is to reduce the number and duration of interruptions in electricity distribution.

The ERO also focused on monitoring compliance with the standards of electricity supply quality set out in public notice no. 540/2005 on the quality of electricity supply and related services in the electricity industry. The results of this monitoring will be used for amending

this public notice to tighten the prescribed limits or to introduce more targeted standards and, above all, for introducing incentive-based quality regulation. For the first time ever, the data returned under this public notice was audited.

From the perspective of electricity quality and supply monitoring, 2013 was an unfavourable year in terms of emergencies. It saw a rise in the number of unplanned interruptions in electricity supply due to failures caused by inclement weather, which distribution system operators experienced mainly in July and August, when they were caused by storms and strong and persisting rainfall; and in December due to windstorms and rime. In addition, a large part of the Czech Republic was hit by floods in June 2013, resulting in the declaration of a state of emergency in the whole of Prague, and also in the districts of Mělník, Litoměřice, Ústí nad Labem and Děčín. These episodes caused higher values of discontinuity indicators compared with preceding years.

### **3.1.3 Network tariffs for connection and access**

Under the Energy Act and public notice no. 436/2013 on regulatory methods and procedures in the electricity and heating industries and amending no. 140/2009 on regulatory methods in the energy industries and procedures for price control, as amended, the Office sets the charges for regulated services related to electricity supply on an annual basis. These charges are heavily influenced mainly by the level of overall consumption, the price of electrical energy for covering network losses, the agreed value of booked capacity, inflation factors, and, last but not least, the increase in renewable electricity generation.

Charges for network services are composed of charges for transmission and distribution services, which are further broken down to the charge for network use per unit of electricity taken and the charge for booked network capacity, which is set as a fixed monthly charge.

The charge for using transmission system networks is influenced by losses in the transmission system and the price of energy for covering these losses. The expected level of losses increased by almost 19 per cent year-on-year, mainly due to the unplanned cross-border energy flows, while a favourable factor influencing this charge was the drop in the price for energy to cover losses by 9.51 per cent. The result of these two factors was an increase in the charge for using transmission system networks by 11.63 per cent. The charge for capacity booking in the transmission networks rose by 2.95 per cent year-on-year.

As in transmission, the charge for network use in distribution serves for covering network losses. Its amount for 2013 was also favourably influenced by the drop in the price of electrical energy, but this drop was partly offset by the reintroduction of the contribution to distributed (decentralised) generation. This fact had different impacts on each of the voltage levels. The charge for network use at the EHV level therefore rose by 4.08 per cent year-on-year while it declined by 3.04 per cent at the HV level compared with 2012. The charges for booked capacity at the various voltage levels are mainly influenced by the agreed technical parameters of booked capacity, the volume of investment at the respective voltage level, and the charge for capacity booking in the higher-level transmission system. In 2013, the unit price for booked capacity at the EHV and HV levels increased by 2.49 per cent and 2.85 per cent respectively year-on-year.

Electricity distribution charges also include the controlled price to meet the extra costs incurred in support for electricity from renewable energy sources, high efficiency combined heat and power generation and secondary sources (“charge for promoted sources”). Because of the growth in expected costs of supported plants to CZK 44.44 billion in 2013, and therefore a year-on-year growth in the costs of supported plants by 27.21 per cent, the charge for supported sources was originally calculated at CZK 788.91/MWh. The year-on-year



increase in the costs of supported plants was primarily caused by the planned large amount of electricity generated by photovoltaic plants, and also at biogas plants, biomass firing plants and wind power plants. Nevertheless, thanks to a CZK 11.6 billion subsidy from that national budget, the originally calculated charge was reduced to CZK 583/MWh, which implies a year-on-year increase by 39.1%. In spite of that, this item still considerably contributed to the overall growth in the regulated components of the price.

The charge for the provision of system services is billed by the transmission system operator (TSO). System services help to secure the Czech electricity grid and to balance electricity generation and demand. The transmission system operator arranges for system services primarily by purchasing ancillary services. The charge for system services dropped by 8.2 per cent year-on-year to CZK 132.19/MWh, thanks to bargain purchases and optimising the mix of the various types of ancillary services.

No changes occurred in connection conditions in 2013. The conditions for connecting a new electricity customer or generator to the distribution or transmission system, including the method of calculating the applicant's share of the costs incurred in the connection and in supplying the required power, are set out in ERO public notice no. 51/2006 on the conditions of connection to the electricity grid, as amended. The technical conditions for connection are stipulated in the rules of the transmission/distribution system operation.

With a view to preventing cross subsidies, regulatory reporting has been put in place which, following the accounting and legal unbundling, strictly requires the reporting of the costs directly allocable to each of the regulated activities. As part of secondary legislation, the ERO also sets the rules for the allocation of overhead costs for companies that operate more than one regulated activity.

### **3.1.4 Cross-border issues**

#### **Access to cross-border infrastructure**

The Czech electricity grid is synchronised with the rest of continental Europe (formerly the UCTE system). Cross-border interconnections exist with all neighbouring countries, i.e. Germany, Poland, Slovakia and Austria, and with five transmission systems: 50 Hertz and TenneT (Germany), PSE (Poland), SEPS (Slovakia) and APG (Austria). At the respective cross-border point, transmission capacities are allocated on the basis of coordinated calculation within the Central and Eastern European region (known as Central Eastern Europe, CEE),<sup>1</sup> which also includes Slovenia and Hungary in addition to the neighbouring countries.

Coordinated capacity allocation for the whole of the next subsequent year and month (annual and monthly capacities) and for the individual trading hours on the next subsequent day (day-ahead capacities) is organised by Central Allocation Office (CAO), a subsidiary of the eight regional transmission system operators. Capacity allocation takes place under the Rules for Coordinated Auction of Transmission Capacity in the CEE Region (auction rules<sup>2</sup>), which set out the conditions for access to cross-border infrastructure within the meaning of Article 37(6)(c) of Directive 2009/72/EC. The transmission system operation rules, which are subject to approval by the ERO, refer to these auction rules. Informal coordinated assessments of the auction rules take place through the CEE regional coordination committee. The above-described capacity allocation method is used for cross-border interconnections with the 50

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<sup>1</sup> Regions for coordinated congestion management are defined in point 3.2 of Annex I to Regulation (EC) No 714/2009

<sup>2</sup> Rules for Coordinated Auction of Transmission Capacity in the CEE Region, available at [http://central-ao.com/images/uploads/Auctions2014/20131009\\_Auction\\_Rules.pdf](http://central-ao.com/images/uploads/Auctions2014/20131009_Auction_Rules.pdf)

Hertz, TenneT, PSE and APG transmission systems. For interconnection with Slovakia, a different cross-border capacity allocation method is used, see below.

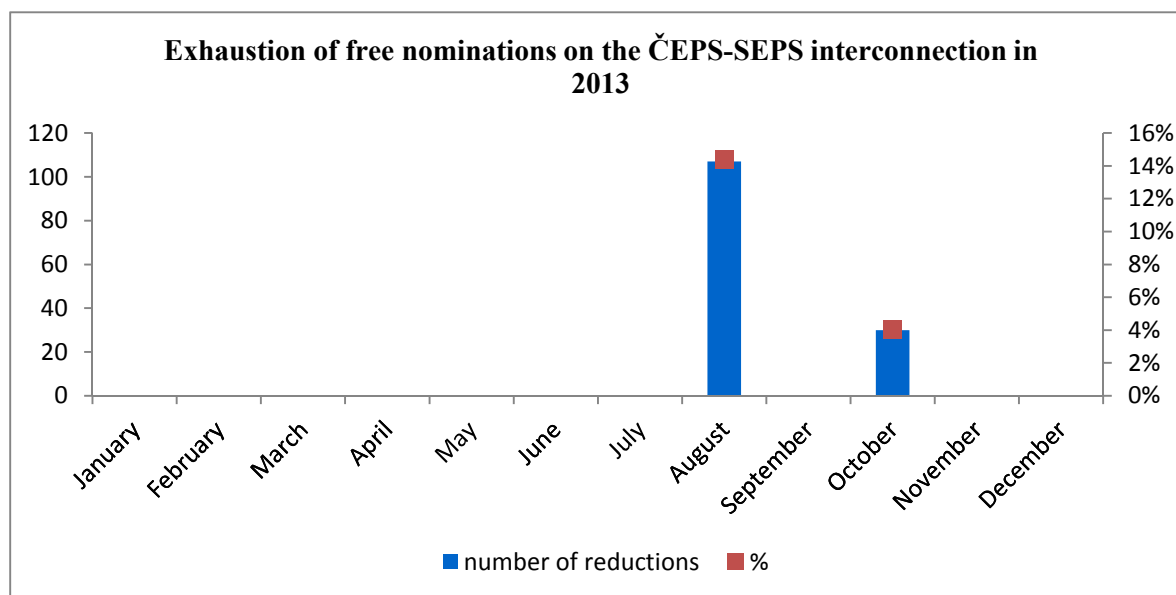
The auction rules are fully compliant with Article 16 of Regulation No 714/2009 (EC), and support, in particular, netting, i.e. the satisfaction of requirements for transmission in opposite directions. In line with the trend to book long-term transmission capacities, mainly as hedges against price volatility, long-term transmission rights are allocated with an option of no use and subsequent resale in day-ahead auctions (the Use It or Sell It, UIOSI, principle). This approach is in line with the target model for the electricity industry.

Capacities on the national border with Slovakia (the interconnection with SEPS) are allocated differently. Market participants can send long-term nominations without having to book cross-border transmission capacity separately, not later than two days before the cross-border transmission is to take place. The transmission capacity so used is free of charge. Should the aggregate volume of nominations exceed the capacity earmarked for the long-term timeframe, all nominations are cancelled and the entire available cross-border capacity is released for day-ahead implicit allocation through market coupling with Slovakia and Hungary.

Thanks to the historical interconnection between the Czech and Slovak transmission systems, high transmission capacity is available in the cross-border interconnector with SEPS, and contractual congestions therefore occur only infrequently. The ČEPS-SEPS interconnection therefore cannot be described as structurally congested within the meaning of point 1.4 of Annex I to Regulation (EC) No 714/2009. This is confirmed by the low occurrence of reductions in long-term nominations and also the strong price convergence between the Czech and Slovak spot markets (see below). In the case of congestions, capacities are allocated in a non-discriminatory manner – implicit auctions for each of the trading hours on the following day. The ERO therefore regards the congestion management method employed on the national border with Slovakia as fully compliant with Article 16 and Annex I of Regulation (EC) No 714/2009.

In 2013, long-term nominations were reduced only in 1.56 per cent of cases, i.e. almost 6 per cent fewer than in 2012. The occurrence of such reductions in 2013 was related to the planned outages of lines, which caused reductions in available transmission capacity. The cases of the reductions in each month of 2013 can be seen in Chart 2. The ERO continuously monitors the situation and should a structural congestion occur on the Czech-Slovak interconnector, it is ready to initiate the implementation of an adequate congestion management method.

**Chart 1: Exhaustion of free nominations on the ČEPS-SEPS interconnection in 2013**



Source: ČEPS, a. s.

On all cross-border interconnectors, intra-day transmission capacities are allocated on the First Come First Served basis until the available capacity is exhausted. Coordinated capacity allocation for all cross-border interconnectors is organised by ČEPS, a.s. The current system does not make charges possible, and therefore does not make efficient pricing of the limited transmission capacities possible. Since 2012, intra-day transmission capacity has been allocated for individual trading hours on the interconnector with SEPS. On other interconnectors, transmission capacity is allocated for six four-hour intervals (“sessions”).

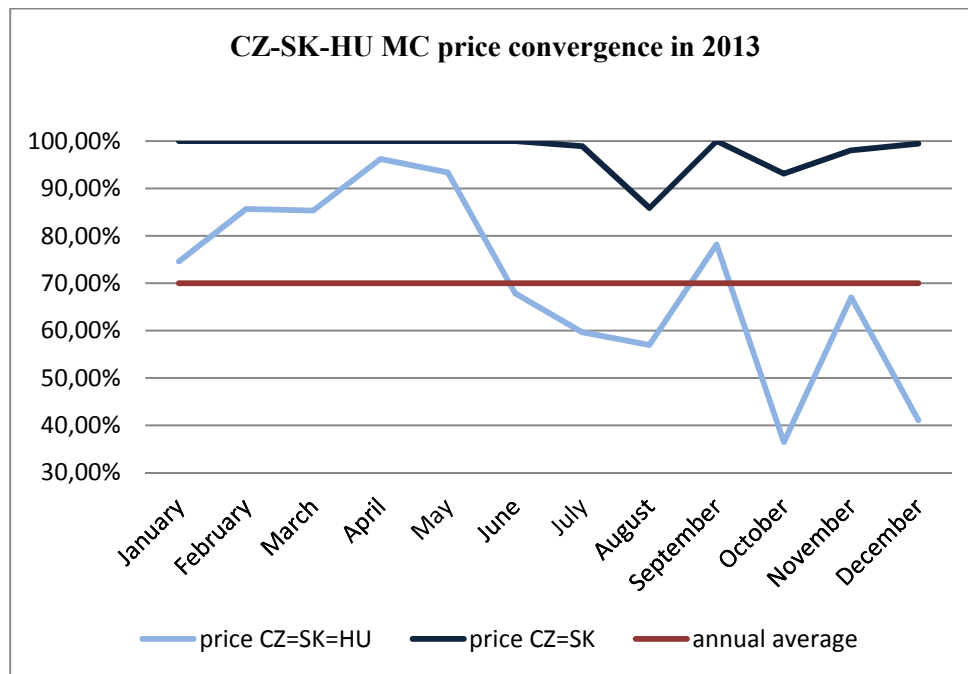
Since 2010, transmission capacities have been allocated by means of implicit auctions through market coupling on the national border with Slovakia. In 2013, market coupling of day-ahead markets in the Czech Republic, Slovakia and Hungary (CZ-SK-HU MC) continued successfully.

Work on expanding CZ-SK-HU MC to include additional countries, specifically Poland and Rumania, continued in 2013. The business solution applied in Poland and the existing CZ-SK-HU MC project are not compatible and the decision has therefore been adopted that implicit allocation of day-ahead capacities on Polish interconnector points will only be put in place when the project for market coupling throughout the CEE region is implemented. Nevertheless, the Polish side has remained a project member with an observer status. On the other hand, the activities undertaken in 2013 to expand CZ-SK-HU MC to include Rumania can be viewed as successful and the launch of the expanded project is planned for the fourth quarter of 2014 (“4M MC project”).

Transmission capacity allocation through energy exchanges (implicit allocation) has considerable advantages over explicit allocation, which takes place on other cross-border interconnection sites. First of all, market participants are not exposed to the risk stemming from procuring the commodity separately from the capacity for its transmission. What cannot happen is that a trader procures electrical energy, but has no transmission capacity for exporting it, and vice versa. When using implicit allocation, cross-border exchanges are also carried out in the direction of the price differential at all times, which supports the most economical dispatch and maximises social welfare. An important indicator of the success of implicit allocation is the occurrence of identical prices at the participating spot markets, i.e. price convergence. It was 70 per cent on average in the Czech Republic, Slovakia and

Hungary in 2013. Taking into account prices in the Czech Republic and Slovakia only, this ratio is even higher, almost 98 per cent. Compared with 2012, price convergence in these three markets declined by 8 per cent. A marked decrease in price convergence is visible mainly in the latter half of 2013.

**Chart 2: CZ-SK-HU MC Price convergence in 2013**

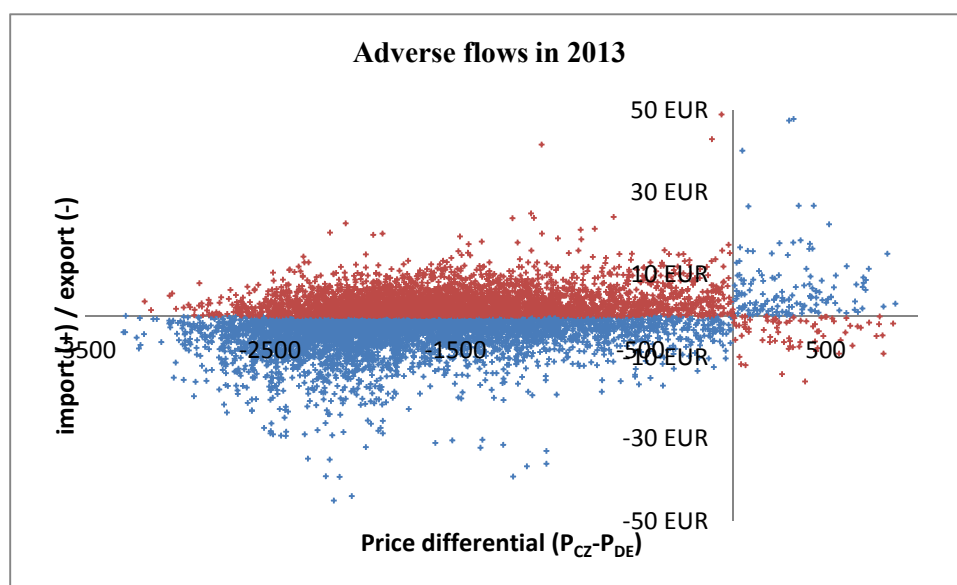


Source: OTE, a.s., ERO's own calculations

As mentioned above, capacity at other cross-border interconnectors is allocated in explicit auctions. Since capacity is allocated separately from energy trading, situations may occur when electricity is exported from a higher price market to a lower price market, i.e. it flows against the price differential (which is also known as adverse flows). This situation is undesirable from the economic perspective. Chart 4 shows the size of this phenomenon on the Czech interface with the German-Austrian trading zone (i.e. all interconnectors with 50Hertz, TenneT and APG).<sup>3</sup> Quadrants 1 and 3 (red points) represent the situation where commercial exchanges flow against price differential; this situation occurred in 43 per cent of times in 2013. The average size of these adverse flows amounted to 1,504 MW from the Czech Republic into the German-Austrian commercial zone and to 333 MW in the opposite direction.

<sup>3</sup> Commercial exchanges at each of the interconnectors equal the balance of total nominations in both directions and the price differential is determined as the difference between the hourly price at OTE's intra-day market and the Epexspot intraday market for the German-Austrian trading zone.

**Chart 1 Adverse flows in 2013**



Source: OTE, a.s., Epexspot, ČEPS, a.s., ERO's own calculation

Since ČEPS, a.s. is a TSO that is fully unbundled in terms of ownership within the meaning of Article 9 of Directive 2009/72/EC, the ERO does not conduct any systematic monitoring of the use of congestion charges (i.e. proceeds from cross-border capacity auctions). On the other hand, the ERO approved the use of a part of the revenues from auctions for reducing the allowed revenues from electricity transmission pursuant to the second point of Article 16(6) of Regulation (EC) 714/2009.

### **Cooperation with other regulatory authorities and ACER**

The ERO's employees who are responsible for the electricity industry attend the meetings of ACER working groups and sub-groups and of the Council of European Energy Regulators (CEER) on a regular basis. Because of the important powers vested in ACER, especially in relation to the preparation of network codes and newly also in the context of Regulation (EC) No 347/2013 on guidelines for trans-European energy infrastructure, the Electricity Industry Department mainly focuses on activities within ACER. The ERO also systematically takes part in the cooperation related to the collection and evaluation of data on and analysis of the conditions of the internal energy market and in the preparation of ACER's and CEER's reports and studies.

Regional cooperation within the CEE region primarily takes place in respect of coordinated congestion management and capacity calculations and is formalised through regional initiatives and the regional coordination committee. The regional implementation group serves for consultations with regional TSOs, energy exchanges and market operators. In 2013, work continued on the implementation of the target model in the CEE region, which consists of the joint implementation of MC using the flow-based method of capacity calculation and allocation. On the basis of the guidelines provided by the national regulatory authorities, TSOs and market operators have drafted a plan for target model implementation. Because of the problems caused by loop flows, the regulatory authorities also requested the TSOs to modify the flow-based method in a way helping to mitigate the impacts of the loop flows. The TSOs have suggested two options: an option focused on operating safety and that focused on compensation for economic loss. The latter half of 2013 saw the finalisation of the

Memorandum of Understanding that sets out further steps required for the target model to be implemented in our region.<sup>4</sup>

As mentioned in general, intensive preparations for expanding CZ-SK-HU MC to include Rumania were undertaken simultaneously with the effort to create a region-wide flow-based MC. In addition to clarifying a number of technical and legal issues related to the new project, the main task was to select the platform for matching trading transactions. The selected variant, PCR, is fully compatible with the system that is used for MC in North West Europe (NWE) and that is the basis for the pan-European model. It was therefore ensured that the selected solution would be fully compatible with the target model for the entire EU and that any obstacles and costs associated with the integration of 4M MC into the regional flow-based MC and subsequently the EU-wide MC would be minimised. The parties' determination to complete the 4M MC project successfully in accordance with the principles of the EU's internal market and with a view to enhancing the integration of European electricity markets was expressed in the Memorandum of Understanding of 11 June 2013, see above.

In the first half of 2013, the ERO and the market operator, OTE, a.s., joined the implementation of the target model for intra-day trading. The main objective was to select the supplier of the technical solution for the trading platform and cross-border capacity allocation. Because of the unsatisfactory allocation of the costs to the participants, the ERO was compelled to suspend its support for this project.

Unfortunately, continued integration of markets in the CEE region, and therefore the implementation of the target model, is being hindered by the heavy occurrence of loop flows in the CEE region, which mainly affect the Czech and Polish transmission systems. Unplanned flows are inevitable in densely interconnected electricity grids if a zone-based approach to congestion management is employed. If loop flows exceed a tenable threshold they pose considerable risk for the safe operation of transmission systems. Unplanned flows also impair the reliability of transmission capacity calculations and can ultimately result in deteriorated conditions for cross-border trading. In 2013, the ERO participated, at the bilateral and European levels, in activities geared towards mitigating this problem.

Chart 5 indicates that unplanned flows enter the Czech electricity grid from the north via the interconnections with 50Hertz and PSE and exit the Czech Republic in the south to Austria (the interconnection with APG). Unplanned flows totalled more than 1,300 MW on average in 2013. On the basis of analyses carried out by the TSOs concerned<sup>5</sup> and independent consultants<sup>6</sup> the Office believes that the increased occurrence of loop flows in the CEE region is related to the size and topology of the German-Austrian trading zone and also to wind power development in northern Germany.

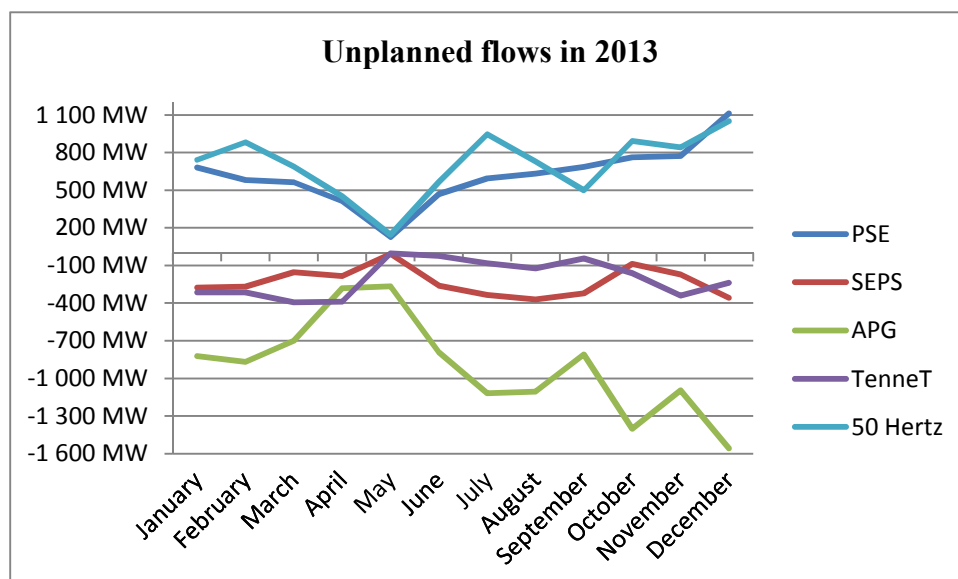
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<sup>4</sup> The Memorandum of Understanding was signed in January 2014. See *Memorandum of Understanding on the implementation of the day-ahead congestion management target model in the CEE REGION in conjunction with other European regions*. Available from ACER website at [http://www.acer.europa.eu/Electricity/Regional\\_initiatives/Cross\\_Regional\\_Roadmaps/Documents/memorandum-of-understanding-CEE.pdf](http://www.acer.europa.eu/Electricity/Regional_initiatives/Cross_Regional_Roadmaps/Documents/memorandum-of-understanding-CEE.pdf)

<sup>5</sup> See, e.g., *Joint study by ČEPS, MAVIR, PSE and SEPS regarding the issue of unplanned flows in the CEE region*. Available from PSE website at [http://www.pse.pl/uploads/pliki/Unplanned\\_flows\\_in\\_the\\_CEE\\_region.pdf](http://www.pse.pl/uploads/pliki/Unplanned_flows_in_the_CEE_region.pdf)

<sup>6</sup> A study prepared for the European Commission by Thema Consulting Group, *Loop flows – Final advice*. Available at [http://ec.europa.eu/energy/gas\\_electricity/studies/doc/electricity/201310\\_loop-flows\\_study.pdf](http://ec.europa.eu/energy/gas_electricity/studies/doc/electricity/201310_loop-flows_study.pdf)

**Chart 2 Unplanned flows in 2013**



Source: ČEPS, a.s., ERO's own calculations

Another area on which the ERO and its international partners focused in 2013 was the development of the trans-European infrastructure in line with Regulation (EU) 347/2013. The first half of the year saw the finalisation of the selection of projects of common interest (PCI), which was completed on 14 October 2013 by the adoption of the EU's list of projects of common interest.<sup>7</sup> In the electricity sector, the PCI status was granted to five projects submitted by ČEPS, a.s. On 31 October 2013, the ERO received a request for cross-border cost allocation under Article 12 of Regulation (EU) No 347/2013 from the promoter of project 3.11.4. In compliance with the Regulation, the request was transmitted to ACER for information and the ERO started to take steps conducive to the issuance of a coordinated decision by all the regulatory authorities concerned. However, the applicant withdrew the request in March 2014 and the proceedings were then discontinued in accordance with the Rules of Administrative Procedure.

### **Monitoring of the investment plan and assessment of its compliance with the Community-wide network development plan**

Section 24(10)(j) of the Energy Act requires ČEPS, a.s. to prepare a ten-year plan for the development of the electricity transmission system, which is subject to the ERO's approval under Section 17(7)(i) of the Energy Act. In 2013, the ERO assessed the plan for the development of the Czech transmission system for 2014-2023, which was submitted by ČEPS, a.s. on 23 August 2013 and then updated on 12 December 2013.<sup>8</sup> Unlike the plan for the development of the gas transmission system, compliance with the Community-wide network development plan is not subject to assessment. The plan for the development of the electricity transmission system is only assessed *mutatis mutandis* under Section 58k(3) of the Energy Act, i.e. taking into consideration the needs of the Czech electricity grid. In the respective administrative proceeding, the ERO did not find any non-compliance with

<sup>7</sup> Commission Delegated Regulation (EU) No 1391/2013 of 14 October 2013 amending Regulation (EU) No 347/2013 of the European Parliament and of the Council on guidelines for trans-European energy infrastructure as regards the Union list of projects of common interest

<sup>8</sup> Available on ČEPS's website at <http://www.ceps.cz/CZE/Cinnost/Technicka-infrastruktura/Documents/Rozvoj%20PS/2013/Pl%C3%A1n%20rozvoje%20p%C4%9Aenosov%C4%9A%20soustavy%20%C4%8Cesk%C4%9A%20republiky%202014%20-%202023.pdf>

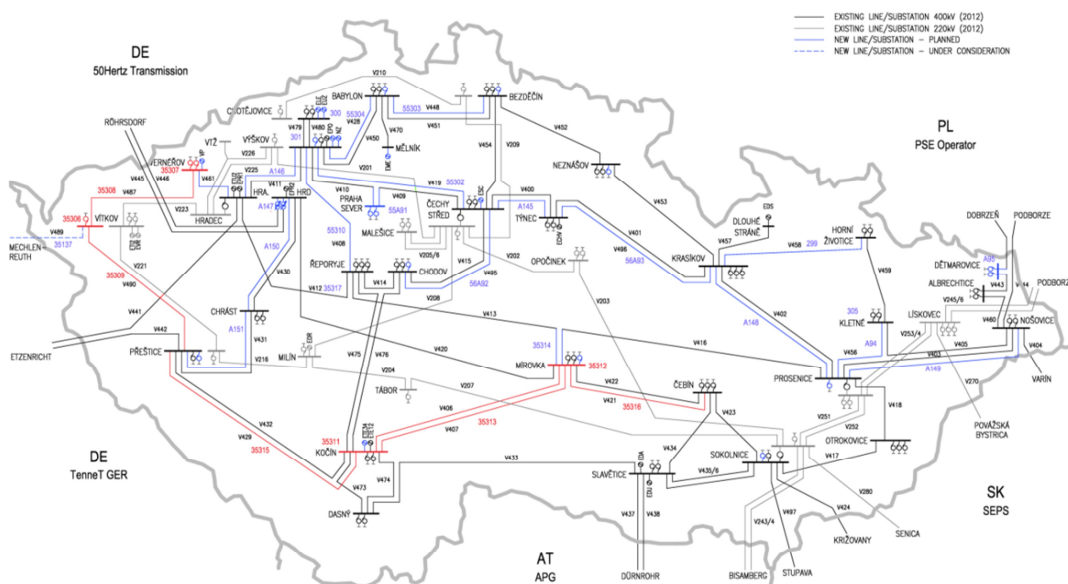
the requirements of Section 58k(3) of the Energy Act and approved the submitted development plan by its decision of 30 December 2013.

An assessment of the plan for the development of the electricity transmission system for the purpose of this National Report under Article 37(1)(g) of Directive 2009/72/EC suggests that the plan is in line with the EU's TYNDP, Ten-year Network Development Plan, and no shortcomings can be noted. Almost all capital projects contained in TYNDP 2012 are part of the plan for the development of the Czech transmission system from 2014 to 2023. The following capital projects (under TYNDP 2012 numbers) are not part of the national ten-year development plan for the following reasons:

- 35.137 The project was cancelled; the plan to reinforce the interconnection with TenneT in the future is still in place
- 35.138 The projects the implementation of which is expected over the long term (after 2023), going beyond the scope of the development plan
- 55. 310 The project was cancelled and replaced with other projects
- A150, A151 The projects the implementation of which is expected over the long term (after 2023), going beyond the scope of the development plan

In connection with Regulation (EU) No 347/2013 it is to be assessed whether the PCIs in the Czech Republic are also part of the national ten-year development plan (Article 3(6)). The first PCI list includes five projects that concern the Czech Republic (projects 3.11.1-5). Although the various capital projects included in the national development plan are not structured in the same way as PCIs, it can be deduced that all of the PCIs are included in the national development plan. The map below shows the PCIs in red. The other planned projects are shown in blue.

**Figure 1: Map of PCIs in the Czech Republic**



Source: ČEPS, a.s.

In connection with the heavy occurrence of unplanned flows through the Czech transmission system's cross-border interconnections, a phase shifting transformer (PST), to be erected at the cross-border interconnection with 50 Hertz (Germany) at the Hradec station, is planned for 2016 to 2017. This transformer will support more efficient control of flows in the interconnected transmissions systems in the CEE region, thereby significantly boosting



security of supply; the operation of the transformer will be coordinated with the neighbouring TSOs. This approach is also expected to help optimise cross-border transmission capacities.

### **3.1.5 Compliance**

The ERO exercises its powers on the basis of the relevant provisions of the Energy Act, which lay down the rights and obligations arising from the relevant provisions of the EU legislation, i.e. Directive 2009/72/EC, Regulation No 714/2009/EC, Regulation No 713/2009/EC and Directive 2006/32/EC. Already the 2011 amendment to the Energy Act harmonised Czech national legislation with EU law in the third package. Czech law therefore fully complies with these EU regulations thanks to the amendments to the Energy Act and implementing acts.

The Office ensures that the TSO and DSOs, and, if applicable, the relevant owners of the systems, and also all electricity utilities perform their obligations under the relevant legislation at the European and national levels. The Office also monitors compliance with the rules governing the TSO's, DSO's, traders', customers' and other electricity market participants' obligations.

The Office exercises its supervisory powers under the relevant provisions of the Energy Act so as to ensure the efficient monitoring of all electricity market participants' compliance with EU and Czech law and with the ERO's and ACER's relevant legally binding decisions, and imposes effective, proportionate and dissuasive penalties on the electricity utilities that breach their obligations.

All changes to laws and regulations that the ERO carried out in 2013 were consulted with all the stakeholders. In developing and amending legislation, the ERO at all times places emphasis on the maximum transparency, non-discriminatory approach and elimination of negative impacts on the Czech electricity market.

An amendment to Act No 165/2012 on promoted energy sources and amending certain laws, which was sponsored by the Ministry of Industry and Trade and in the development of which the ERO also participated, was initiated, and enacted through Act No 310/2013, in 2013. The amendment entered into effect in October 2013.

Work was under way to draft a new amendment to the Energy Act, mainly in view of the need to ensure compatibility with the new Czech legislation in the field of civil law and also the recently adopted new inspection rules, and also with a view to boosting consumer protection and in connection with the need to remedy the discrepancies identified thanks to the experience gained by the energy market participants. The amendment of the Energy Act has also been necessitated in connection with the new EU legislation that has to be implemented in Czech law, in particular Directive 2012/27/EU of the European Parliament and of the Council of 25 October 2012 on energy efficiency and repealing Directives 2004/8/EC and 2006/32/EC.

In accordance with its authorisation under the Energy Act and the amended law on promoted energy sources, the Office promulgated new implementing acts within its remit.

The Office also promulgated public notice no. 350/2013, amending no. 347/2012 laying down the technical and economic parameters of renewable energy sources for electricity generation and the useful life of plants generating electricity from supported energy sources. It specifies the technical and economic parameters, which include, under the law, primarily the costs per installed unit of output, the efficiency of using the primary energy content in the renewable source, the load factor and, in the case of generating plants using biomass, biogas or bio-liquids, the cost of fuel.

The Office also promulgated a new statutory instrument, public notice no. 436/2013 on regulatory methods and procedures in the electricity and heating industries and amending no. 140/2009 on regulatory methods in the energy industries and procedures for price control, as amended. The reason was the above amendment to the law on promoted energy sources, in particular with regard to recouping the costs of support for promoted energy sources through the electricity price; the cost of support for promoted energy sources is no longer part of the electricity transmission and distribution charges, but is included in a separate regulated charge for electricity, specifically the charge for meeting the costs incurred in support for electricity generated from promoted energy sources. Another reason for promulgating the public notice for price controls in the electricity industry was to adjust the terminology and set the input parameters entering the calculation of the charge for covering support for electricity and operating support for heat in connection with the amendment to the law on promoted energy sources.

In order to achieve the EU's energy and environmental targets, the integration of renewable energy within the electricity grid must be promoted. Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directives 2001/77/EC and 2003/30/EC therefore requires the member states to take the necessary steps for the development of electricity transmission and distribution networks to ensure the safe and reliable operation of the electricity grid that enables the development of renewable electricity generation. This objective is also reflected in Directive 2009/72/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in electricity and repealing Directive 2003/54/EC, in the recitals of which the member states are to encourage the modernisation of distribution networks, such as through the introduction of smart networks, which should be built in a way that encourages decentralised generation and energy efficiency. Under Article 36 of Directive 2009/72/EC, the Office, as the national regulatory authority, is required *inter alia* to achieve, in the most cost-effective way, the development of secure, reliable and efficient non-discriminatory systems that are consumer oriented, and promoting system adequacy and, in line with general energy policy objectives, energy efficiency as well as the integration of production of electricity from renewable energy sources in both transmission and distribution networks. The Office therefore has to ensure that system operators and system users are granted appropriate incentives, for both the short and the long term, to increase efficiencies in system performance and foster market integration.

The importance of electricity infrastructure development has recently been highlighted by the adoption of Regulation (EU) No 347/2013 of the European Parliament and of the Council on guidelines for trans-European energy infrastructure. This regulation introduces a system of incentives for projects of common interest, i.e. projects that *inter alia* contribute to supply sustainability and security at the EU level. The ERO regards the new regulation as inspiration for achieving the above-described goals, given to the Office by the EU legislation, at the national level as well.

In order to ensure uninterrupted energy supply for affordable prices, major investment in the energy infrastructure was and is required, mainly with regard to the integration/impacts of distributed electricity generation (including loop flows from adjacent systems) into/on the operation of the transmission system and distribution systems and preserving the reliability of supply to consumers.

Thus, the public notice responds to the above situation and defines a new parameter for the TSO and DSOs: the investment development factor, which is part of incentive-based regulation and is intended to motivate entities to invest in capital projects related to the above

areas. In order to pursue long-term and strategic plans for developing a high-quality, reliable and safe energy network ensuring a sufficiently high quality of supply for final customers, a legal and regulatory environment that is stable for the long term must be put in place. For this reason, and in relation to the introduction of the investment incentive factor, the public notice extends the current regulatory period for the electricity industry by one year.

## 3.2 Promoting competition

### 3.2.1 Wholesale markets

#### 3.2.1.1 Monitoring the level of prices, the level of transparency, and the level and effectiveness of market opening and competition

In the Czech Republic, electricity is traded at Power Exchange Central Europe, a.s. (“PXE”) under bilateral contracts and on spot markets organised by OTE, a.s. While standard products traded at PXE and the products on the spot market of OTE, a.s. have fixed expiry dates, these rules do not apply to bilateral contracts. The terms of bilateral contracts vary; an electricity producer and an electricity trader, or a trader and a customer, usually enter into one-year agreements. Since February 2009, physical products with delivery in the Slovak grid, and since March 2009 physical products with delivery in the Hungarian grid have also been traded at PXE. In addition to physical products PXE has also introduced financial products without an obligation of physical supply. The year 2013 saw a significant year-on-year increase in liquidity at PXE, above all as regards financial products without physical supply. The CZ-SK-HU MC is currently working, and the plan for the future is to extend this integrated market to include Romania.

Electricity traders can use any combination of bilateral contracts and energy exchange products, including OTE, a.s. platforms and foreign exchanges, including the Leipzig energy exchange, EEX, for buying and selling. It is therefore not feasible to clearly determine the structure of electricity procurement for final customers after the supplier has bought or re-sold electricity in various market places in Europe.

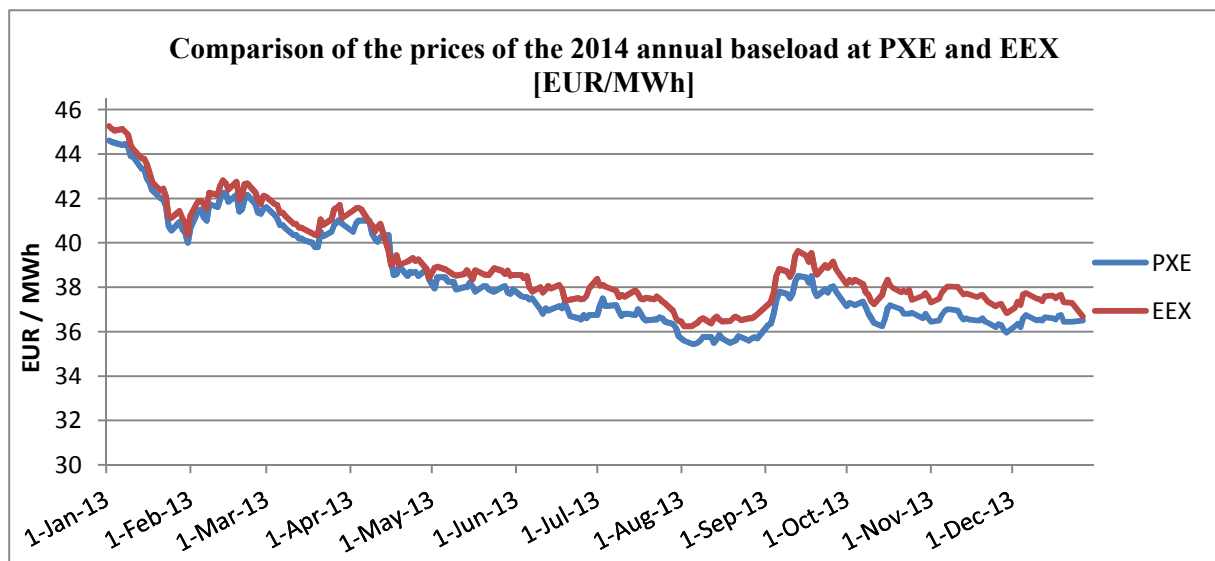
The following tables and charts show PXE liquidity indicators (volumes traded, number of contracts etc.), including average prices in 2013.

**Table 1: Liquidity indicators at PXE with futures for the Czech Republic**

	Volume [MWh]	Volume [€m]	Number of contracts
<b>BASE products</b>	24,744,375	947.099	7,385
<b>PEAK products</b>	545,544	27.215	909
<b>Total</b>	25,289,919	974.313	8,294

Source: PXE

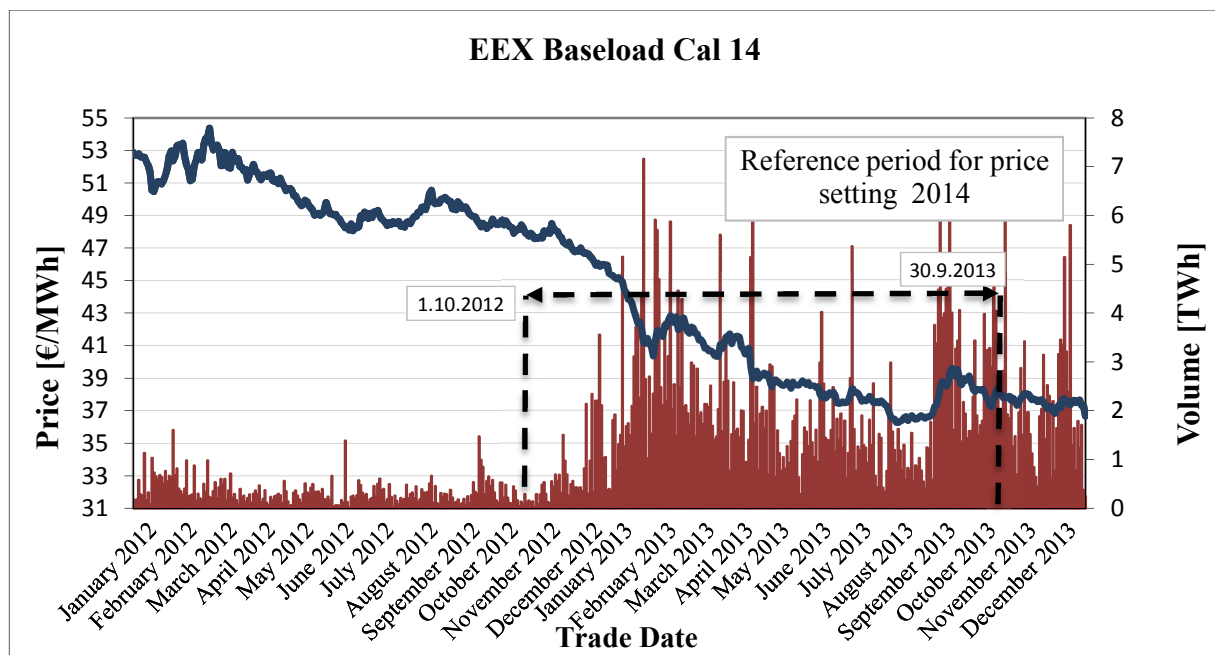
**Chart 6: Futures 2014 prices, annual base load**



Source: PXE, EEX

Chart 6 indicates that the prices of the products traded at PXE are closely correlated with those at the Leipzig energy exchange, EEX, for products to be delivered to the German and Austrian electricity grids. The development at the Leipzig energy exchange, EEX, is shown in Chart 7.

**Chart 7: Prices and volumes of traded 2014 futures, annual base load, at EEX**



Source: EEX

A part of the volume of electricity is traded under OTC (bilateral) contracts and also in the spot market (day-ahead and intra-day markets) organised exclusively by OTE, a.s. since February 2009. In 2013, a total of 101,999 GWh was traded under bilateral contracts registered in the OTE system; 11 GWh was traded in the block market; and 417 GWh of electricity was traded on the intra-day market. All cleared entities, i.e. not only traders and producers but also the customers who are responsible for imbalances, can go to the spot market to procure electricity.

In this segment, the ERO did not carry out any checks in 2013.

The ERO and the Ministry of Industry and Trade have drafted a bill on wholesale energy market integrity and transparency (REMIT), the key objective of which is to adjust Czech law to the directly effective *acquis* in REMIT: provide for state administration in the wholesale energy market.

### **3.2.2 Retail market**

As regards electricity traders' market position, this market is fully liberalised in the Czech Republic at both wholesale and retail levels. Electricity traders are therefore not legally constrained at all in buying electricity directly from producers (generators) or at exchanges or spot markets in the Czech Republic and in other countries. They also have the right to sell electricity to market participants to other countries. Traders must provide distribution system operators with identification details of the customers whom they supply under agreements on bundled supply services. Traders must also provide electricity transmission and distribution system operators with information required for the safe and reliable operation and development of these systems. Electricity traders' obligation is to promote energy services and offers thereof. Electricity traders have the right to receive from the market operator, the information that they need for billing their electricity supply to customers whose supply point is registered with OTE.

#### **3.2.2.1 Monitoring the level of prices, the level of transparency, and the level and effectiveness of market opening and competition**

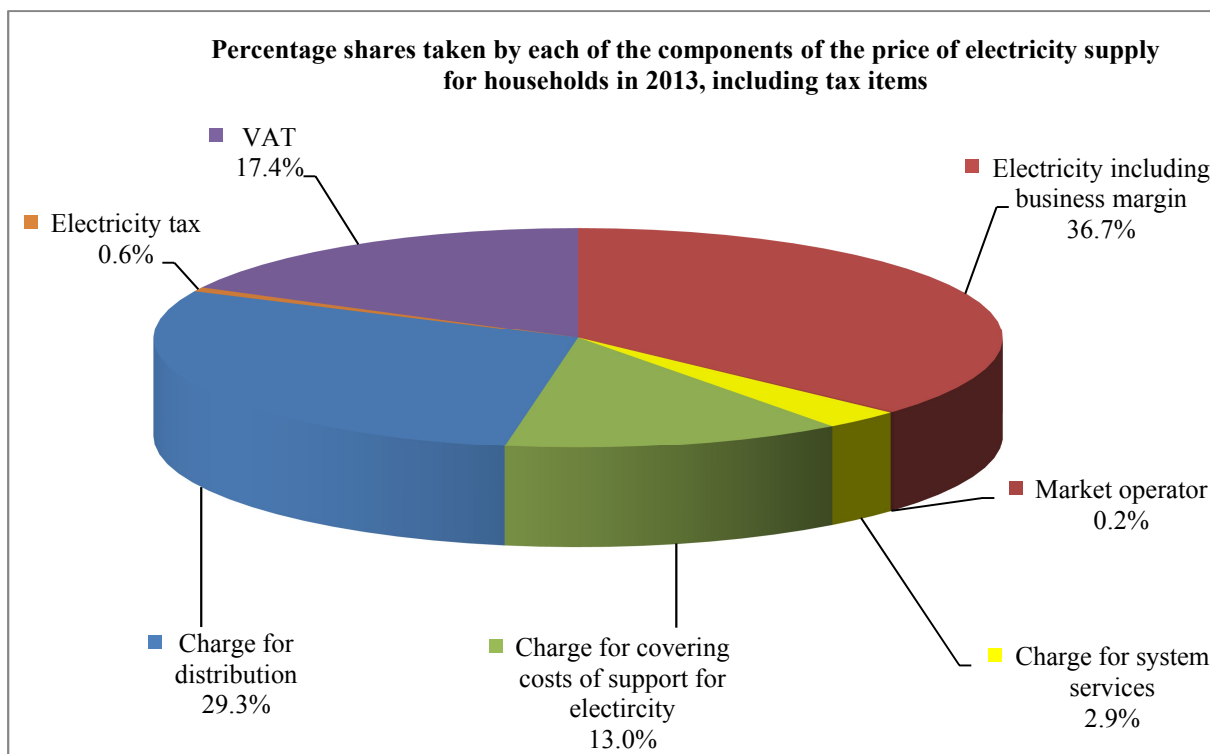
The overall price of electricity supply for customers at the LV level is made up of the regulated items of charges for distribution and related services and the unregulated prices of electrical energy products, which are determined by the supplier selected by the customers.

The ERO sets out the regulated items of the price in its binding price decisions. Changes of these prices for customers at the LV level also reflect the external factors that influence network operation in technical and economic terms (in particular the development of electricity production from promoted clean sources, line losses, the development of the size and structure of consumption, and the rate of inflation).

For 2013, the average year-on-year increase in the overall price of electricity supply for households was 2.4 per cent and for low-demand business customers it was 3.1 per cent (net of tax items). The change in electricity supply price for each individual customer could differ from the above values due to the selected tariff, rated current of the main switch upstream of the electricity meter, nature and size of consumption and, last but not least, in relation to the supplier of the energy.

Chart 8 shows the percentage shares (including VAT and electricity tax) of the various components in the resulting price of electricity supply for households for 2013.

**Chart 8 Percentage shares taken by each of the components of the price of electricity supply for households in 2013**



Source: ERO

### 3.2.2.2 Recommendations on supply prices, investigations and measures to promote effective competition

Customers have the right to select, at their own discretion, any supplier of electrical energy and the most suitable product on offer with regard to the nature and size of their demand.

Customers can proactively influence some of the costs of electricity at the LV level by selecting their energy supplier; the balance of the costs is made up of regulated charges for distribution and other regulated items. The shares taken by each of the items generally differ for each individual final customer and depend on the type of the tariff and size of demand; on average, regulated items account for almost 60 per cent of the resulting price of supply for household customers (but only 20 per cent for some tariffs).

On the contrary, payments for distribution depend on the point of connection, i.e. the relevant distribution company to whose network the supply point is connected. Thus, customers cannot select their distributor. However, customers at the LV level can change their distribution tariff subject to meeting the conditions for obtaining the tariff; or by changing the main switch upstream of the electricity meter they can influence the fixed components of the regulated payments for transmission and distribution. Most customers in the Czech Republic are connected to the electricity grid through regional distribution companies: ČEZ Distribuce, a.s., E.ON Distribuce, a.s., or PREdistribuce, a.s.

Customers are also unable to influence the charges for the other regulated items; the charge for system services, the charge for meeting the extra costs incurred in support for electricity generation from renewable energy sources and high efficiency combined heat and power generation and secondary sources, and the charge for the market operator's service of the clearing of imbalances, are the same for all final customers in the Czech Republic regardless of the point of connection, voltage level or selected supplier.

Under Article 37(1)(o) of Directive 2009/73/EC, the ERO publishes, in accordance with Section 17(7)(l) of the Energy Act, recommendations in relation to electricity supply prices for households.

Section 17c of the Energy Act lays down the ERO's cooperation with the Office for the Protection of Competition (ÚOHS). This provision requires the two authorities to provide each other with suggestions, information and other forms of cooperation required for the performance of their tasks, such exchanges being subject to the same level of confidentiality on the receiving side as the disclosing side guarantees.

The ERO is also required to advise ÚOHS of market participants' practices that there exist good reasons to believe that they distort or restrict, or result in the distortion or restriction of, competition, of the use of constraining or unfair terms and conditions in contracts on the electricity market, and of the methods of electricity pricing for households.

The ERO also carried out periodical checks, using its findings from market monitoring and suggestions received from consumers and final customers, preferentially focused on electricity traders' practices, mainly in the electricity supplier switching process. Investigation also focused on electricity traders' adherence to their rights and obligations, including compliance with the standards of supply and service quality in the electricity industry.

The ERO also carried out (on the basis of suggestions from the outside) checks for suspicion of violations of consumer protection legislation, in particular prohibition of unfair business practices, in respect of the rights attached to contract rescission, including checks specifically focused on licence holders' obligation to provide, when offering and selling electricity to consumers, complete information enabling consumers to know the final offering price (covering all taxes, customs duties and charges) prior to executing agreements on bundled services of electricity, and on the obligations related to the publication of changes in electricity supply prices.

## **4 The gas market**

### **4.1 Network regulation**

The past year 2013 was important in terms of changes in the ownership structure of some gas companies.

On 2 August 2013, the entire ownership interest in NET4GAS, s.r.o. was transferred from RWE Gas International N.V. to HYX Czech, s.r.o., subsequently renamed NET4GAS Holdings, s.r.o., which now is therefore the sole member of and controls NET4GAS, s.r.o.

Ownership interests in NET4GAS Holdings, s.r.o. are held by two members, Allianz Infrastructure Czech HoldCo II S. à r.l. and Borealis Novus Parent B.V. The owners of NET4GAS Holdings, s.r.o. are therefore companies in Allianz and Borealis portfolios.

1 November 2013 saw a merger of regional DSOs in the RWE Group to form a single successor organisation. The acquiring company is RWE GasNet, s.r.o.

In the first step of this merger, a group of funds headed by a Macquarie European Infrastructure Fund bought minority stakes held by E.ON, SPP and GDF SUEZ in RWE's regional trading companies Východočeská plynárenská, a.s., Severomoravská plynárenská, a.s. and Jihomoravská plynárenská, a.s. These minority stakes were then swapped with RWE for an approximately 35% stake in RWE Grid Holding, a.s. RWE Grid Holding, a.s. then absorbed all of RWE's gas distribution businesses, i.e. JMP Net, s.r.o., SMP Net, s.r.o., VČP Net, s.r.o. and RWE GasNet, s.r.o., and the servicing company RWE Distribuční služby, s.r.o.

Since this merger, three regional distribution companies have been providing gas distribution in the Czech Republic: E.ON Distribuce, a.s., Pražská plynárenská Distribuce, a.s., member of the concern Pražská plynárenská, a.s., and RWE GasNet, s.r.o.

#### **4.1.1 Unbundling**

NET4GAS, s.r.o. was legally unbundled from RWE Transgas, a.s., a gas importer and supplier, as of 3 September 2009. However, it was part of a vertically integrated undertaking together with this company. With regard to the cost intensity, interferences with and exercise of ownership rights, impacts on the regulation of gas transmission charges (and, in turn, impacts on customers) and the time required for implementation, the option of an independent transmission system operator, ITO, emerged from the evaluation of the feasible options for an effective unbundling.

Having met the independence conditions laid down in the Energy Act and having demonstrated the same to the Office, NET4GAS, s.r.o. was granted an independence certificate by the Office on 28 January 2013.

Following the issue of the above decision NET4GAS, s.r.o. notified the Office of the forthcoming sale of the ownership interest in NET4GAS, s.r.o. This plan was notified to the European Commission on 17 May 2013. Subsequently, the European Commission noted in its opinion that it did not find a reason for re-certification due to the change of ownership.



## **4.1.2 Technical functioning**

### **The gas transmission system**

The services offered to customers using the Czech gas transmission system were not curtailed at all in 2013.

In 2013, the TSO completed and put into operation new connections and interconnections enhancing energy market integration and improving the security of supply in Central Europe.

Following completion in 2012, in January 2013 NET4GAS, s.r.o. put into operation the Gazelle high pressure gas pipeline; it has a length of 166 km and connects to the Nord Stream and OPAL pipelines, which bring natural gas to the Czech national border via the northern route. Gazelle is connected with OPAL near the village of Brandov and it is further connected via the Rozvadov-Waidhaus BTS with the MEGAL transmission system that serves for supplying the south of Germany and the east of France.

Thus, Gazelle has become part of a new strategic path for natural gas flows to western Europe and is regarded as a major contribution to a higher diversification of natural gas transport routes and sources for central and western Europe.

On 1 January 2013, BRAWA, a.s., a wholly-owned subsidiary of NET4GAS, s.r.o., became the owner of the Gazelle pipeline. NET4GAS, s.r.o., as the exclusive holder of the gas transmission operation licence in the Czech Republic, operates Gazelle under transparent contracts.

In June 2013, a new gas pipeline was put into operation to connect the Tvrdonice underground gas storage facility to the transit part of the gas transmission system. The new connecting line has helped to boost the transmission capacity and also gas withdrawal from the UGS facility back into the transit part of the transmission system, which is desirable for improving security of supply above all. The Tvrdonice storage capacities will therefore also be physically available for other central and eastern European countries in case of need.

As part of the Uhřice II and Dambořice UGS projects, in 2013 the TSO put in place some technical measures supporting an increase in connection capacity for smooth supply to North Moravian UGS facilities and ensuring gas supply to the transfer station now under construction.

Bi-directional gas transmission from the Dolní Dunajovice UGS facility to the transmission system was put in place in technical terms at the Uherčice site.

Under the long-term development plan, the TSO decided to discontinue the operation of the Hostim compression station as of 31 December 2013. On the basis of this decision the Hostim compression station will be converted into a new line closing valve.

### **Distribution system**

Any natural or juristic person who holds a gas distribution licence awarded by the Energy Regulatory Office under the Energy Act is authorised to distribute gas in the Czech Republic. If more than 90,000 supply points are connected to a distribution system, it is called a regional distribution system. Otherwise (fewer than 90,000 customers are connected), such system is called a local distribution system. Nevertheless, licences awarded for gas distribution do not make such distinction and no differences are made between these two types of systems in terms of the rights and obligations set out in the Energy Act.

In 2013, six regional distribution companies distributed gas in the Czech Republic. Because of the merger of the DSOs in the RWE Group into a single successor company (see point 4.1), since 1 November 2013 three regional distribution system operators have been providing gas

distribution in the Czech Republic: E.ON Distribuce, a.s., Pražská plynárenská Distribuce, a.s., a member of the concern Pražská plynárenská, a.s., and RWE GasNet, s.r.o.

In 2013, regional distribution system operators distributed gas through pipelines with a total length of 73,671 km.

### **Gas storage facilities**

Three storage system operators operate in the Czech Republic: RWE Gas Storage, s.r.o., MND Gas Storage, a.s. and SPP Storage, s.r.o. RWE Gas Storage, s.r.o. operates six underground gas storage facilities: Dolní Dunajovice, Lobodice, Štramberk, Třanovice, Tvrdonice and Háje. MND Gas Storage, a.s. operates the Uhřice UGS facility in Southern Moravia. Another UGS facility in Southern Moravia, Dolní Bojanovice owned by SPP Storage, s.r.o., is connected to the Slovak gas network and does not serve for supplying the Czech Republic. The effective storage volume in the facilities intended for the Czech Republic totals 2.921 bcm.

As in 2012, UGS storage capacities were not used to capacity during the 2013 injection season. Compared with the 2012 injection season, traders injected smaller gas volumes into UGS facilities. The first factor that may have caused this was the below-average temperatures in the second quarter of 2013, which extended the withdrawal season until May 2013. Gas injection into the facilities was therefore started later. This delay was partly offset in the second half of 2013, which allowed a longer injection period, helping to achieve a higher level of operating gas stores before the heating season in late 2013.

Another major factor was traders' weaker demand for storage services due to abundant gas quantities offered on spot markets, which helped them buy the required volumes for lower prices.

The operating gas stores peaked in the first half of November 2013 at a level of approximately 94.5 per cent in the case of RWE Gas Storage, s.r.o., and at a level of 80 per cent in the case of MND Gas Storage, a.s.

### **Requirements for quality of service**

Due to the June 2013 floods, distribution system operators declared emergency in Prague, in the Central Bohemian Region and in the Ústí Region under applicable legislation. The emergency had to be declared to protect the health and property of the residents in the affected localities. All distribution system operators carried out their statutory duty and under public notice no. 344/2012 of 10 October 2012, on emergencies in the gas industry and methods of providing for the security standard of gas supply, notified the Office of declaring the emergency within one hour from starting the required operations for preventing emergency. The distribution system operators also proceeded in compliance with legislation when they notified the Office of discontinuing the operations for preventing emergency and of ending emergency. The constraints arising from declared emergency affected the quality of gas supply and related services until early July 2013, when emergency was lifted in the last locality. The floods caused the disconnection of 478 supply points in the distribution area served by Pražská plynárenská Distribuce, a.s. and 1,922 supply points in distribution areas served by RWE GasNet, s.r.o. Following the end of emergency, all those disconnected supply points were duly connected again.

With the exception of this event 2013 did not see any gas supply curtailment in the Czech Republic.

## **System balancing**

The TSO is responsible for the physical balancing of the gas system. The TSO balances the system in cooperation with DSOs. For balancing, it uses the line pack in the gas system and the flexibility service, and/or gas purchase and sale from/to cleared entities; it bids for and offers this gas on the organised gas spot market.

The flexibility service consists in a flexible gas supply/take for keeping the balance between gas offtake and supply from and into the transmission system. The scope of the service is defined by the overall flexibility service and the maximum daily quantity that the provider of this service is obliged to supply to or take from the TSO for one gas day. The service is provided by the gas trader who wins the public tendering procedure for the current year. The Office monitors the baseline parameters of the service and the tendering process with a view to guaranteeing transparency and a non-discriminatory approach to all the entities involved.

### **4.1.3 Network and LNG tariffs for connection and access**

#### **Tariffs**

The Office regulates charges for gas transmission and distribution and charges for the market operator's services under Section 17(11) of the Energy Act. The prices charged by the supplier of last resort are also subject to ERO regulation by way of cost-plus pricing.

The Office sets regulated prices under public notice no. 140/2009 on regulatory methods in the energy industries and procedures for price controls, as amended, under which the methodology for calculating gas transmission and distribution charges is also determined. The regulatory method remains unchanged for a regulatory period. The method for gas distribution pricing is the same for all DSOs.

The regulatory method is based on the revenue cap principle; this principle consists in setting each of the parameters at the beginning of the regulatory period and modifying them every year. On the basis of the parameters so determined, 'adjusted allowed revenues' are determined; they include eligible costs, depreciation, profit, correction factors and, possibly, some other eligible variables. The relevant charges are calculated from the adjusted allowed revenues so determined.

The resulting charges for gas transmission are calculated from the adjusted allowed revenues for the TSO, and are allocated to the entry and exit points in the transmission system based on their expected use. These entry and exit points include the Czech Republic's border points, the virtual gas storage facility point, supply points of customers directly connected to the transmission system, and the aggregate of the delivery points between the transmission and distribution systems, which serve for gas supply to supply points of customers within the Czech Republic, i.e. 'the domestic point'. The charge determined for gas transmission to the domestic point is billed to customers as part of the distribution charge.

Gas transmission charges are double-component prices, i.e. they have a fixed and a variable component. The fixed component of the gas transmission charge relates to the booked firm transmission capacity and represents the payment for booked firm transmission capacity at the respective entry or exit point of the transmission system. The variable component of the charge is determined, with the help of a coefficient, so as to cover the costs incurred in fuel gas (gas consumption for driving compressor stations, which are needed for controlling pressure in the network and smooth supply to customers).

The adjusted allowed revenues set for each of the DSOs are used for calculating the resulting gas distribution charges for each of the distribution areas. Gas distribution charges are set for

each of the following customer categories: high-demand customers, medium-sized demand customers, low-demand customers and households. Distribution charges are double-component charges for all customer categories, as transmission charges. For customers in the high demand and medium-sized demand categories the fixed component of the charge depends on the total daily booked capacity. The charge for booked daily capacity is calculated using an equation described in the applicable ERO price decision. For these customer categories, the fixed component of the charge constitutes the larger part of payment for gas supply. For customers in the low demand and household categories, the fixed component of the charge is determined in the form of the standing monthly charge at each particular supply point. For these customer categories, the fixed part makes up approximately one-third of the regulated payment for gas supply services. Variable components of the charges for all customer categories depend on the gas quantity consumed and are set as fixed CZK/MWh rates for gas taken.

The Office also regulates the charges for the market operator's services. Network tariffs include the charge for the clearing provided by the market operator; this charge is also based on the value of the adjusted allowed revenues set for the market operator for the gas industry. The particular amount of the fixed charge for clearing is tied to the gas quantity taken by customers in the Czech Republic in the respective year.

Due to the fact that the Czech gas market has been liberalised, the Office only sets the prices for the above activities, which are necessary for ensuring gas supply to customers' supply points. Gas prices on the wholesale or retail market are not subject to regulation. The unregulated part of the gas supply price includes the commodity and trade charge and the charge for supply structuring and flexibility. Calculating the shares taken by the various parts of the unregulated price and the overall amount thereof are completely at relevant gas trader's discretion and fully depend on its business strategy.

### **Prevention of cross subsidies**

The legal unbundling of the respective entities, holders of gas transmission, distribution and storage licences, from each other under Directive 2009/73/EC concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC has resulted in the creation of an environment prohibiting cross-subsidies between transmission, distribution, storage, and supply activities. The Office sees to it that rules ensuring the separate performance of the various licensed activities are observed.

In 2013, the Office did not find any indications of violations of the rules for the unbundled performance of the various licensed activities.

### **Regulated and unregulated access to storage**

In the Czech Republic, access to underground gas storage facilities is based on the principle of negotiated third party access. In respect of access to storage capacities, national legislation imposes a duty on storage system operators to sell released or new storage capacity in online auctions.

The Office does not interfere with storage system operators' business strategies in any manner whatsoever. Nevertheless, in its public notice no. 365/2009 on Gas Market Rules, as amended, the Office lays down the minimum required terms and conditions for storage capacity auctions. On the other hand, the Office evaluates the level to which available storage capacities are used and on the basis of this evaluation and the public consultation process modifies the conditions for access to UGS facilities with a view to promoting a higher use of the storage capacities.

In 2013, SSOs called ten auctions to sell their storage capacity for subsequent storage years. RWE Gas Storage, s.r.o. organised nine auctions of a total annual capacity of 40.9 mcm. MND Gas Storage a.s. called one auction for 4.3 mcm. The opening bids were very low due to the low prices on spot markets. This situation can be viewed positively from the perspective of gas traders and final customers.

Globula a.s. (now Moravia Gas Storage a.s.) allocated, on the basis of a successful auction and in line with the Capacity Allocation and Management Rules, 90 per cent of the storage capacity in the Dambořice UGS facility under construction to a future customer, specifically Gazprom Export. The capacity was allocated for 15 years beginning 1 July 2016. The total capacity is 448 mcm, with a maximum withdrawal rate of 7 mcm/day and a maximum injection rate of 4 mcm/day.

#### **4.1.4 Cross-border issues**

##### **Access to cross-border infrastructure**

In 2013, access to cross-border infrastructure was based on Regulation (EU) No 347/2013 of the European Parliament and of the Council on guidelines for trans-European energy infrastructure (TEN-E). This Regulation defines a list of projects of common interest (PCI), the purpose of which is to diversify the gas routes and sources and to enhance the security of gas supply in EU member states. In the gas industry, these projects largely concern the development of new cross-border gas pipelines that will help to reduce countries' dependence on a single gas source. The most important of them include the north-south interconnection, which will help to increase the number of gas sources and routes both for the Czech Republic and other EU countries.

The first PCI list, prepared by the EU in cooperation with regional initiatives, also includes three Czech projects for gas pipelines, which were nominated by the Czech TSO, NET4GAS, s.r.o.: the ONI pipeline (Oberkappel), BACI (Bidirectional Austrian-Czech Interconnection) and STORK II.

The ONI project will connect the southern branch of the Czech transmission system with the Austrian WAG pipeline and will terminate at Oberkappel, the interconnecting point between the German and Austrian transmission systems. It will further diversify the gas supply routes and enhance supply security through the 7Fields and Haidach storage facilities. ONI will also contribute to the integration of the gas markets in central Europe and boost supply security in terms of the diversification of gas sources and routes. It will also help to remove the potential physical shortfall in transmission capacities in the Austrian WAG pipeline and the German MEGAL-South pipeline.

BACI will interconnect the Czech and Austrian gas systems at a point between Lanžhot and Baumgarten, which is also the interconnecting point between the Austrian and Slovak transmission systems. The project is also intended as a continuation of the planned Moravia gas pipeline, through which Austria will gain easier access to gas storage facilities in the Czech Republic. Shippers using the Czech gas system will gain easier access to two gas storage facilities on the Austrian side and the CEGH Central European Gas Hub at the Baumgarten interconnecting points.

Another planned project is the STORK II gas pipeline to interconnect the Czech and Polish transmission systems. Its objective is to reinforce the cross-border capacity between the two countries and enhance security of supply. It will also help to transport gas from the Polish LNG terminal at Świnoujście, now being completed.

For the Czech Republic, SPP Storage, s.r.o. nominated a project for connecting the Dolní Bojanovice UGS facility to the Czech transmission system. However, this proposal was assessed as ineligible, and therefore was not granted the PCI status.

In October 2013, NET4GAS, s.r.o. and the Polish TSO (GAZ-SYSTEM) submitted a joint investment request for the STORK II pipeline to the Energy Regulatory Office and the Polish regulator, Urząd Regulacji Energetyki.

Due to lack of interest on the part of the participating German TSOs in further development, effective from 1 October 2013 the project of the GATRAC platform for booking bundled cross-border capacity products was terminated; originally, it brought together three TSOs: NET4GAS, s.r.o. for the Czech Republic, ONTRAS-VNG Gastransport, GmbH for Germany, and Eustream a.s. for Slovakia.

### **Cooperation with other regulatory authorities and ACER**

In 2013, the Office did not adopt any administrative decisions with cross-border importance requiring consultation with the other member states' regulatory authorities or the Agency under Section 17(7)(o) of the Energy Act (and therefore under Article 41(1)(c) of Directive 2009/73/EC concerning common rules for the internal market in natural gas).

The Office and the Polish regulator have opened consultations on the project for the Polish-Czech STORK II gas pipeline, which received the PCI status in 2013. In October 2013, the Office and the Polish regulator received the Czech and Polish TSOs' joint investment request for this gas pipeline. Thereupon the two regulators launched their cooperation and started to evaluate this request with a view to issuing a coordinated decision approving the mechanism of cross-border capacity allocation.

The Office participated in talks focused on tackling the issue of the regional projects geared towards creating a trading region across several countries. For the Czech Republic, the project for integration on the basis of the Visegrád 4 countries and the CEETR remain relevant.

Cross-border cooperation in respect of informal issues takes place on a daily basis. This mainly includes cooperation in data collection and evaluation, analysis of the status of the internal gas market, etc. ERO employees also take part in the Agency's working groups on gas on a regular basis. In these working groups, in 2013 they were mainly involved in the drafting of the framework guidelines and network codes under Article 6 of Regulation (EC) No 715/2009 on conditions for access to the natural gas transmission networks and in the evaluation of projects of common interest, PCI.

### **Monitoring of the investment plan and assessment of its consistency with the Community-wide network development plan**

In 2013, NET4GAS, s.r.o., the gas transmission system operator, submitted a ten-year plan for the development of the gas transmission system in the Czech Republic to the Office for approval. Following the publication of this plan on its website, the Office did not receive any comments from the stakeholders during the public consultation process. The ten-year plan analyses the development of gas demand and the adequacy of the capacities for entry into and exit from the Czech Republic's domestic zone for the period from 2014 to 2023. In preparing the plan, the TSO proceeded from the current and foreseeable gas supply and demand in the future. Each of the investment plans was examined from the perspective of ensuring the safe operation of the gas system and gas supply reliability, and also from the perspective of environmental impacts, technologies, and economic effectiveness. The Office assessed the consistency of the ten-year plan with the EU's Ten-Year Network Development Plan, TYNDP. Since it did not find any inconsistencies between these two documents or any

conflict with the Energy Act, the Office approved the ten-year development plan submitted by NET4GAS, s.r.o. within the meaning of the respective provision of the Energy Act.

The projects intended to reinforce cross-border capacity are at the stage of expected investment decisions. These currently include, in particular, the development of the new STORK II gas pipeline to interconnect the Czech and Polish transmission systems. An integral part of the STORK II pipeline is the planned Moravia pipeline, which is to help to reinforce the exit capacity for northern Moravia and diversify gas sources and routes through the north-south interconnection between central and south-eastern European countries.

An interconnection between the Czech transmission system and the border transfer point at Oberkappel on the German-Austrian national border and an interconnection between the Czech and Austrian transmission systems via the BACI pipeline are being planned. On the basis of the data and contexts contained in the document, agreement can be expressed with the published conclusion that the existing transmission system, including the forthcoming investment projects, has sufficient entry capacity to meet the maximum daily demand in the Czech Republic for the ten-year period covered by the plan.

#### **4.1.5 Compliance**

The Office exercises its powers on the basis of the relevant provisions of the Energy Act, which lay down the rights and obligations arising from the relevant provisions of the EU legislation, i.e. Directive 2009/73/EC, Regulation No 715/2009/EC, Regulation No 713/2009/EC and Regulation No 994/2010. Already the amendment to the Energy Act, which was enacted in Act No 211/2011, harmonised Czech national legislation with EU law in the third package. Czech law therefore fully complies with these EU regulations thanks to the amendments to the Energy Act and implementing acts.

The Office ensures that the TSO and DSOs, and, if applicable, the relevant owners of the system, and also all gas utilities perform their obligations under the relevant legislation at the European and national levels. The Office also monitors compliance with the rules governing the obligations of the TSO, DSOs, traders, customers and other gas market participants.

The Office exercises its supervisory powers under the relevant provisions of the Energy Act so as to ensure the efficient monitoring of all gas market participants' compliance with EU and Czech law, and the ERO's and ACER's relevant legally binding decisions, and imposes effective, proportionate and dissuasive penalties on the gas utilities and other market participants that breach their obligations.

All changes, or plans for changes, to laws and regulations that the ERO carried out in 2013 were consulted with all the stakeholders. In developing and amending legislation, the Office at all times places emphasis on the maximum transparency, non-discriminatory approach and elimination of negative impacts on the Czech gas market.

In 2013, the Office launched preparations for the new regulatory period in the gas industry, which will begin in 2015. Preparations of and the related consultations with the regulated entities on the proposals for the new regulatory methodology for the fourth regulatory period for the gas industry were started. In this connection, preparations were started for promulgating a new public notice on price controls and methods of price controls in the gas industry. The promulgation is planned for 2014.

In 2013, the Ministry of Industry and Trade also participated in the development of new gas legislation. Under the Energy Act, it promulgated two statutory instruments influencing the gas market: public notice no. 289/2013 amending no. 108/2011 on gas metering and on the method of calculating damages for unauthorised gas offtake, unauthorised gas supply,

unauthorised gas storage, unauthorised gas transmission or unauthorised gas distribution, as amended, and public notice no. 325/2013 amending no. 19/2010 on methods of producing statistics and scope of the data provided to the market operator in the gas industry.

## **4.2 Promoting competition**

### **4.2.1 Wholesale markets**

#### **4.2.1.1 Monitoring the level of prices, the level of transparency, and the level and effectiveness of market opening and competition**

In 2013, a total of 25 entities imported gas into the Czech Republic. Some of the imported gas was re-exported to other countries. The largest quantities of gas were imported by RWE Supply & Trading CZ, a.s., WINGAS GmbH and Vattenfall Energy Trading GmbH.

In 2013, some of the gas imports took place under long-term contracts with Russian and Norwegian producers. Long-term contracts contain formulae for calculating the price of gas supply, usually monthly. The price formulae under which Gazprom Export supplies gas to some traders in the Czech Republic were modified in 2013. Gas price indexation to oil product and coal prices is being abandoned because it fails to reflect the situation in the gas market adequately. Now, these formulae better reflect the movements of prices at energy exchanges.

Gas is also bought at spot markets of energy exchanges for the current or the following day. Gas is also available through futures, offering the supply of agreed fixed gas quantities usually for a month, quarter, season or the whole year. For the Czech Republic, the NCG platform of the EEX Leipzig energy exchange is used the most frequently.

Gas bought under long-term contracts or at energy exchanges is priced in EUR/MWh or USD/MWh, and the resulting price for Czech consumers is therefore also influenced by the CZK/EUR and CZK/USD exchange rates.

Marginal gas quantities come from indigenous production in the Czech Republic; here, the procurement costs may be much lower than in the case of other methods of gas procurement. However, the volume of the gas so obtained is not really significant and accounts for less than 2 per cent of the country's total annual demand. Indigenous production therefore does not have any major impact on the prices in the Czech wholesale or retail gas markets. In this respect, the Office did not make any checks in 2013.

The Office and the Ministry of Industry and Trade have drafted a bill on wholesale energy market integrity and transparency (REMIT), the key objective of which is to adjust Czech law to the directly effective *acquis* in REMIT: provide for state administration in the wholesale energy market.

### **4.2.2 Retail market**

#### **4.2.2.1 Monitoring the level of prices, the level of transparency, and the level and effectiveness of market opening and competition**

In 2013, the Office registered 62 active traders who supplied gas to customers. Since the retail gas market is saturated now, 2013 did not see such a significant increase in the number of traders compared with 2012 as the preceding years. New traders are not able to win customers as easily as at the beginning of the gas market liberalisation. Customers who were not satisfied with their traders' pricing policy or services have already switched their supplier in most cases. The number of customers who sign fixed-term gas supply contracts is also



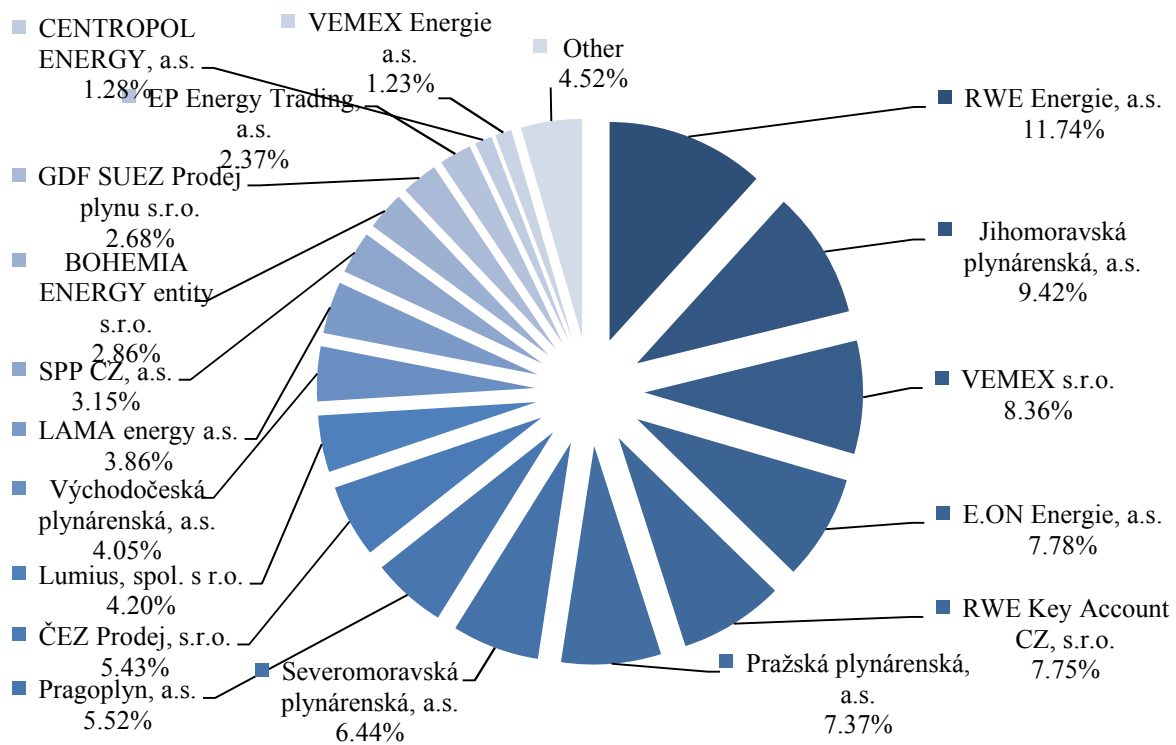
continuously rising, and when they want to switch suppliers, they are therefore more constrained by the contract terms. Energy legislation also allows supplier switching for these customers. However, a condition for supplier switching is the termination of the contract with the current supplier in accordance with the commercial terms and conditions that are part of the existing contract. An early termination of a fixed-term contract can attract a financial penalty under the commercial terms and conditions.

In the past, a major part of supplier switching was carried out on the basis of contracts signed on the basis of door-to-door sales by sales representatives. However, in such cases the customers were frequently not provided with complete and true information about the product offered and a number of cases entailed unfair commercial practices, resulting in damage to customers' rights. Certain municipalities have therefore prohibited peddling within their limits, including offers of gas supply services through sales representatives.

E-auctions organised by municipalities started to be used in 2013 as a new method for bidding a price for gas supply. Citizens are invited to and can participate in these auctions. E-auctions can bring savings of gas supply costs, but those intending to participate are well advised to consider the potential risks that can result in accepting disadvantageous contract terms and, ultimately, in the disconnection of supply. Another feature of this way of buying the gas supply service is the fact that customers do not know the e-auction winner in advance, or the contract terms the winner proposes. In most cases, the quality of the supplier is only assessed on the basis of the lowest price bid, disregarding the other criteria in supplier selection. The Office has found the conditions of e-auctions non-transparent in many cases, and the customers will therefore not achieve the required savings. In addition, firms having no prior experience with gas supply, in respect of which a risk exists that they will not be able to honour their contractual obligations, have started to crop up on the market.

The RWE Group's traders supplied the largest quantity of gas to customers in 2013, i.e. they had the largest market share. They supplied customers with 39.4 per cent of the gas consumed in the Czech Republic. The second largest supplier in terms of gas quantity was VEMEX, s.r.o. with a market share of 8.36 per cent, followed by E.ON Energie, a.s. with 7.78 per cent and Pražská plynárenská, a.s. with 7.37 per cent. Chart 9 shows a more detailed overview of traders and their respective shares of gas supply.

**Chart 3 Traders' shares of gas supply in 2013**



Source: ERO

The Office registered a total of 2,858,874 customers taking gas in 2013. Compared with 2012, there were 9,209 less customers, i.e. a loss of 0.3 per cent.

In 2013, the household category had the largest number of customers, 2,649,092, followed by the low demand category (i.e. natural and juristic persons carrying on a business and taking up to 630 MWh per year) with 201,188 customers. The medium-sized demand category (i.e. natural and juristic persons carrying on a business and taking between 630 and 4,200 MWh per year) had 6,958 customers and the high demand category (i.e. customers taking more than 4,200 MWh per year) had 1,636 customers.

In 2013, 297,281 customers switched their supplier, i.e. 50,000 less than in 2012. The largest number of supplier switches, 264,680, took place in the household category, accounting for 89.03 per cent of all changes.

In the low demand category, 29,091 supplier switches took place, i.e. 14.46 per cent of the total number of changes; the medium-sized demand customer category saw 3,061 supplier switches, i.e. 43.99 per cent of their total number; and 449 high demand customers switched their supplier, i.e. 27.44 per cent of these customers.

In the low demand, medium-sized demand and high demand categories the largest number of supplier switches took place in January. The reason is that these customers often have gas supply agreements in place for a calendar year and as of 1 January change their trader for the following 12 months.

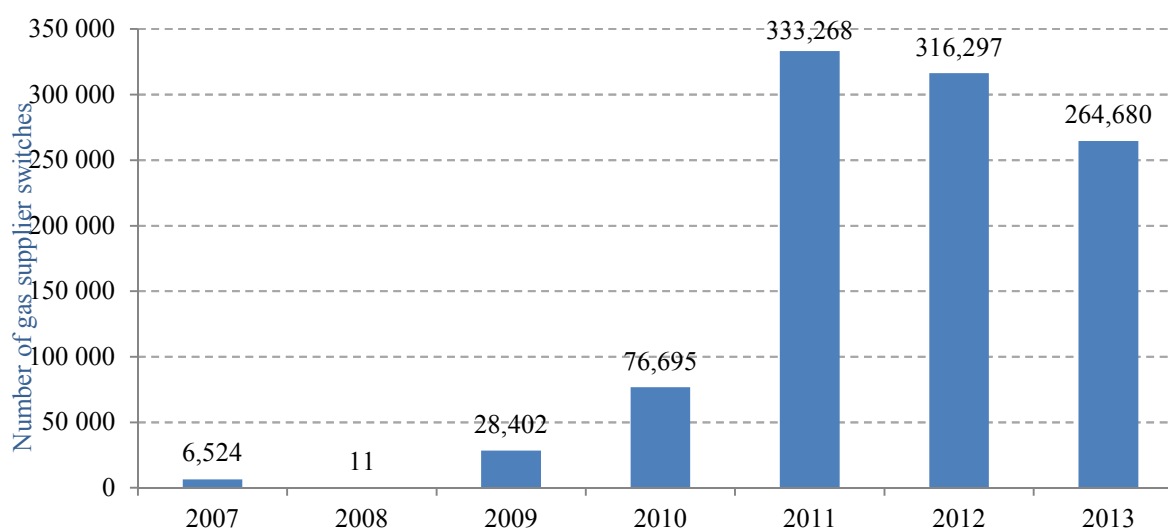
Table 2 shows supplier switches between 2012 and 2013 in the household category.

**Table 2 Gas supplier switches**

Type of demand	2012	2013	2013	2013
	Number of supplier switches	Number of supplier switches	Total number of supply points	Switching (%)
High demand	979	449	1,636	27.4
Medium-sized demand	2,951	3,061	6,958	44.0
Low demand	27,829	29,091	201,188	14.5
Households	316,297	264,680	2,649,092	10.0
Total	348,056	297,281	2,858,874	10.4

Source: ERO

Note: Switching – ratio of the number of gas supplier switches per year and the total number of supply points in that year

**Chart 3: Annual gas supplier switches in the household category**

Source: ERO

**Table 3 Prices of gas supply to customers by Eurostat categories as at the first day of a quarter in the Czech Republic in 2013**

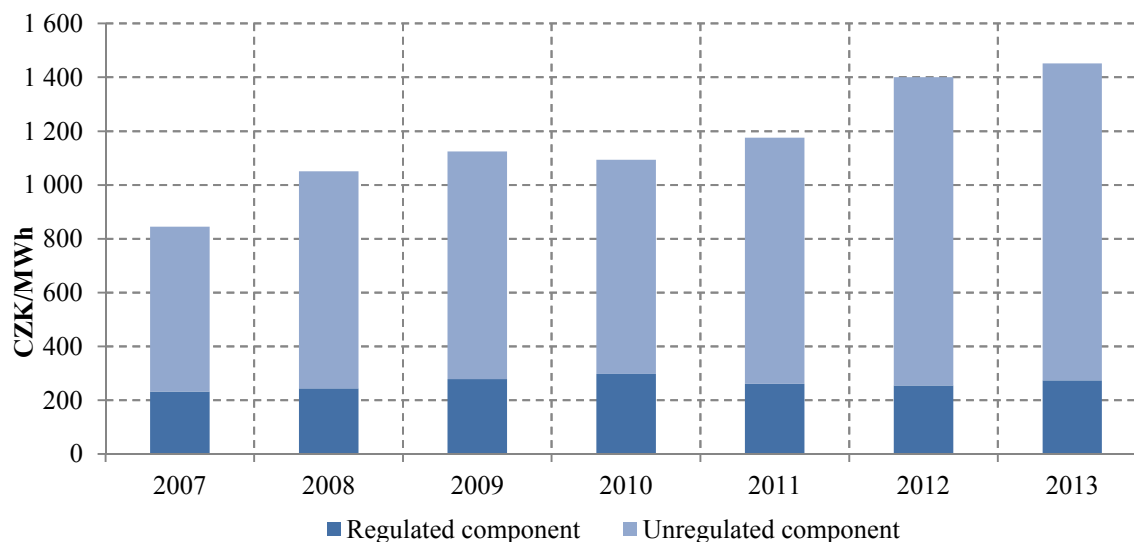
2013	Standard consumer, Eurostat					
	D3		I1		I4	
	Households taking more than 56 MWh annually		Industrial customers taking less than 278 MWh annually		Industrial customers with annual consumption between 27,778 and 277,778 MWh	
	CZK/MWh without VAT	CZK /MWh with VAT	CZK /MWh without VAT	CZK /MWh with VAT	CZK /MWh without VAT	CZK /MWh with VAT
I Q	1,310.91	1,586.20	1,128.37	1,365.33	761.76	921.73
II Q	1,256.72	1,520.63	1,150.65	1,392.29	768.41	929.78
III Q	1,220.04	1,476.25	1,164.28	1,408.78	765.23	925.93
IV Q	1,220.04	1,476.25	1,119.47	1,354.56	777.06	940.24

Source: Czech Statistical Office

Note: The prices are net of the gas tax

The regulated component of the gas supply price increased somewhat in 2013. This increase approximately constitutes the percentage increase in the final prices for household customers. The regulated component accounts for less than 20 per cent of the resulting prices. The final price for customers therefore heavily depends on the unregulated component, mainly comprised of the commodity charge.

**Chart 11 Average regulated and unregulated components of gas supply prices for households without tax items**



Source: ERO

### Regulated parts of the price

Gas transmission and distribution companies are natural monopolies and the Office therefore has the competence to regulate gas transmission and distribution charges, the charges for the market operator's services and also the prices for gas supply provided by the supplier of last resort. The Office applies the cost-plus method of price controls.

The above regulated prices are set out in ERO price decisions that the Office promulgates every year, by 30 November in recent years. The prices set out in the price decision are effective from 1 January of the subsequent calendar year.

The key purpose of price controls is to prevent disproportionate development of prices in an environment in which competition is not feasible.

### Gas transmission

The TSO's allowed revenues for 2013 dropped by 11.4 per cent compared with 2012. This drop is attributable to a considerable extent to the negative value of the correction factor for gas transmission, which represents the difference between the planned and actual revenues from transmission in 2011. The negative value of the correction factor implies that the operator collected money in excess of the plan and will return it to the market through the correction factor. Another factor contributing to the drop in allowed revenues was the year-on-year decrease in the costs incurred in procuring services needed to ensure the stability of the system.

In the Czech Republic, the charge for gas transmission to customers therefore dropped by 16.8 per cent for 2013.

Regulated charges for booking standard firm transmission capacity, i.e. at the entry and exit points on the national borders and at the entry and exit points of the virtual gas storage facility, stayed at the 2012 level.

### Gas distribution

Regulated charges for gas distribution are set as fixed charges. The regulatory method and the pricing procedure are laid down in public notices promulgated by the Office under its authorisation by the Energy Act. These public notices are applicable to all regulated entities in the gas industry.

The parameters for calculating the distribution charges are based on the configuration of the specific system, the required efficiency of regional distribution system operators' activities, the development of the Czech economy and the data reported by gas distribution licence holders under secondary legislation.

The charge for gas distribution, which also includes gas transmission to the domestic point, increased by 4.32 per cent on average in 2013 compared with 2012.

Table 4 shows average gas distribution charges, including transmission, for 2013 for selected customer categories based on their annual gas consumption, ranging from the least to the most expensive regional distribution system. These average prices contain both the fixed and the variable component, and also the component covering gas transmission to the domestic point.

**Table 3: Average distribution charges, including transmission in 2013**

Annual demand	Charge for distribution, including transmission	
	min CZK/MWh	max CZK/MWh
55 to 63 MWh	184.87	274.08
over 63 MWh	194.73	280.74

Source: ERO

### Charges for the market operator's services

The holder of the market operation licence is OTE, a.s., which has been working in the gas industry since 2010.

The regulated services provided by OTE, a.s. include activities related to clearing, provision of actual values to gas market participants, and the organisation of the spot gas market.

Three charges are associated with the clearing provided by the market operator: the charge for the registration of cleared entities, which is paid by cleared entities on a one-off basis. Then there is the fixed charge for the clearing service, which is paid by registered cleared entities. The third charge in this category is the fixed charge for clearing, the level of which depends on the gas quantity consumed.

The fixed charge for clearing, in place since 1 January 2013, was set at CZK 2.16/MWh; it therefore increase slightly and already includes a special charge for the ERO's operation under the Energy Act, amounting to CZK 1/MWh of gas consumed.

Other charges for the market operator's services, which are subject to regulation, stayed at the 2012 level for 2013.

### **4.2.3 Recommendations on supply prices, investigations and measures to promote effective competition**

Under Article 41(1)(p) of Directive 2009/73/EC and under Section 17(7)(l) of the Energy Act, the Energy Regulatory Office shall publish recommendations on gas pricing for households.

The Energy Act and the implementing acts based thereon guarantee the right to switch their gas supplier to all customers. This switching is free of charge and the supplier switching process itself takes ten business days. Subject to observing the commercial terms and conditions with the current supplier, every customer therefore has the opportunity to select a supplier whose prices and other conditions of the gas supply service will be the most convenient for them.

In the market segment in which competition is not possible for technical or organisational reasons, the Office regulates and sets prices for customers. Customers can therefore be sure that only usefully spent costs related to the provision of each particular service will be reflected in the charges that the customers are unable to influence.

Should any of traders be declared insolvent, companies appointed by the law provide the services of the supplier of last resort, who supplies gas for up to six months to customers who took up to 60,000 cu m for the last 12 months, whose trader has lost the ability to supply gas.

In the gas industry, the Office's checks primarily focused on gas traders' practices in arrangements for gas supplier switching. The Office also monitored adherence to gas traders' rights and obligations and the conditions of adherence to the quality standards for supply and services in the gas industry, together with checking the technical condition of equipment through which gas is supplied to final customers.

A special area of oversight in the gas industry included checks of the responsibilities of owners of properties into which gas is supplied for customers in the properties, which were made to see whether shared consuming equipment serving for gas supply was maintained in a condition consistent with legislation, technical standards and technical rules facilitating safe and reliable gas supply, to prevent such equipment from causing a risk to life, health or property.

The Office also carried out (on the basis of suggestions from the outside, contained in consumers' submissions) checks specifically focused on licence holders' obligation to provide, when offering and selling gas to consumers, complete information enabling consumers to know the final offering price (covering all taxes, customs duties and charges) prior to executing an agreement on bundled services of gas supply, and on the obligations related to the timely publication of changes in gas supply prices.

## **5 Consumer protection and dispute settlement in electricity and gas**

### **5.1 Consumer protection**

The Czech Republic empowered consumers to a greater extent some time ago, broadening their rights with a view to ensuring a high level of consumer protection, in particular as regards the transparency of contractual terms and conditions, general information and easier process of supplier switching, primarily through the provisions contained in Section 11a of the Energy Act, which transposes Article 3(7) of Directive 2009/72/EC and Article 3(3) of Directive 2009/73/EC, taken together with Annex I, into Czech law.

In view of the above, and in respect of consumer protection, Section 11a of the Energy Act establishes certain rights for consumers and imposes matching obligations on traders. Under this Section, traders shall publish, in a manner allowing remote access, their terms and conditions of electricity and gas supply and electricity and gas supply prices no later than 30 days before the effective day of changes. Section 11a of the Energy Act also requires traders to offer consumers a choice of non-discriminatory systems of payment for gas or electricity supplied, and as regards the billing of advance payments for gas or electricity supply, traders are required to set advance payments reflecting consumption in the preceding comparable billing period, however, no more than gas or electricity consumption reasonably expected in the following billing period.

As regards consumers' rights, this Section also establishes consumers' right to withdraw from the contract without any contractual penalty in the case of their disagreement with a change to the contract terms and conditions, or an increase in the unregulated part of the price for gas or electricity supply, and sets out the time limits for exercising the right to withdraw from the contract and the effect of such withdrawal. In its valid and effective wording, the Energy Act does not define 'vulnerable customer'; for consumers who can be regarded as 'socially disadvantaged', certain measures for their protection and support for their rights are provided for at the level of generally applicable legislation in the domain of social security law.

Another aspect conducive to improved protection is consumers' ability to access objective and transparent information about their consumption of energy, the related prices, and the costs of services.

The Office is authorised under Section 98a(2)(j) of the Energy Act, for the purpose of securing consumers' justifiable interests in connection with their right to be properly informed of their energy consumption, to lay down the particulars of the billing of electricity, gas and thermal energy supply and related services in implementing regulations. On the basis of this authorisation the Office had earlier promulgated public notice no. 210/2011 on the scope, essentials and dates of the billing of energy supply and related services.

In connection with the broadening of legislation on consumer protection, the Office had earlier set up a Consumer Protection Unit tasked with receiving and addressing submissions, questions, suggestions and complaints from consumers.

Intensive preparations were launched in 2013 to set up the position of an independent Energy Ombudsman for addressing consumer disputes.

Furthermore, under Section 17(7)(l) and (q) of the Energy Act, the Office publishes recommendations in relation to gas supply prices for households and cooperates with civic associations and other juristic persons established for the purpose of protecting consumer rights in the energy sector.

## 5.2 Dispute settlement

As part of its competences, the Office primarily protects customers' and consumers' justifiable interests in the energy industries.

The Office's powers to adjudicate such disputes arise from Article 3(7) of Directive 2009/72/EC (and similarly from Article 3(3) of Directive 2009/73/EC), under which Member States shall ensure high levels of consumer protection also with regard to dispute settlement mechanisms.

In this connection, an amendment to the Energy Act, enacted in Act No 211/2011, had earlier transposed the relevant provisions of Directive 2009/72/EC and Directive 2009/73/EC, taken together with Annex I, into the provisions of the Energy Act.

Under Section 17(7)(e) of the Energy Act, the Office shall adjudicate disputes between customers and licence holders ('customer disputes'), i.e. disputes over the performance of obligations under contracts the subject matter of which is gas supply/distribution, disputes seeking a declaration of whether or not a legal relationship between the customer and the holder of a licence for electricity or gas supply/distribution has come into existence, continues to exist, or has ceased to exist, and also disputes over compensation for failure to keep the set quality standards for supply and services in the gas industry.

Under these provisions, the necessary precondition for instituting proceedings before the Office (within the limits of its jurisdiction *in rem*) on consumer disputes is the customer's motion, and such motion is also the only possible means of instituting proceedings (the procedural principle of a final disposal of the matter [*as the parties may wish to settle it*]). Thus, it is for the benefit of customers that they enjoy the discretion to decide whether they will undertake court proceedings on the matter at issue and bring an action before a court, or whether they will resort to the Office with a motion for adjudicating the dispute over the matter.

Under Section 17(7)(f) of the Energy Act, the Office is also competent to carry out checks and inspections in the energy industries, and supervision over the performance of the duties laid down by the law on consumer protection in respect of business in energy industries (use of unfair business practices, prohibition of discrimination of consumers, and performance of the duties related to providing consumers with information about prices for provided services).