

Annual Report to the European Commission

Finland

Summary

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1.1 The Regulatory Authority

1.1.1 Organization and legal basis of the regulatory authority

The Energy Market Authority is the regulatory agency for electricity and natural gas as well as the emissions trade authority in Finland. The Authority is a monocratic office, which means that it is directed by the head of agency. The head of agency is responsible for the decisions of the authority.

The legal basis for the Energy Market Authority lies within the Act (No. 507/2000) and Decree (No. 621/2000) on Energy Market Authority as well as in the Electricity Market Act (No. 386/1995), the Natural Gas Market Act (No. 508/2000) and the Emissions Trade Act (No. 683/2004).

As per the 1st of July, the total number of staff in Energy Market Authority amounted to 30 of which 27 were permanent. Of this number, 11 were occupied with the electricity market issues, 4 with natural gas market issues and 6 with emissions trading issues. The remaining staff was involved in all of these three areas providing assistance for IT, general administration and secretarial services. The total amount of the budget for 2005 is 2.7 million euros whereof 0.66 million euros are for the emissions trade.

1.1.2 Main tasks, statutory objectives and legal powers

The mission of the Energy Market Authority is to supervise and promote the operation of the electricity and natural gas markets and to create a framework for emissions trading.

As regards the electricity market, the Energy Market Authority shall

- regulate the pricing and conditions of electricity transmission and distribution;
- grant licences for electrical power networks and construction of power lines;
- supervise the obligation to develop the electrical power network;
- monitor the security of electricity supply;
- supervise the guarantee of origin system for electricity; and
- gather and publish data on prices of network services and electrical energy

In the field of natural gas market, the Energy Market Authority shall

- regulate the pricing and conditions of natural gas transmission and distribution;
- grant licences for operation of natural gas networks;
- monitor the security of natural gas supply; and
- gather and publish data on prices of network services and natural gas

The tasks of the Energy Market Authority as emissions trade authority include

- issuing and supervising emissions licences;
- establishing, maintaining and developing the national emissions trading register; and
- approving the verifiers for emissions trading

The Energy Market Authority is mandated to issue both administrative decisions and administrative regulations. The administrative regulations are binding on individual entrepreneurs (network operators, retail sellers, operators covered by the emissions trade legislation). The decisions are subject to appeal the first appellate level being either the Market Court (market supervision issues) or the Administrative Courts (licence issues). The final appeal body in both cases is the Supreme Administrative Court.

On the basis of the Electricity Market Act and the Natural Gas Market Act the Energy Market Authority is empowered to issue administrative regulations on certain clearly defined issues. The administrative decisions are binding on all the entrepreneurs who are active in the defined operation (for instance electricity distribution network operators, natural gas distribution network operators, electricity retail supplier who have the obligation to supply). The administrative regulations are not subject to appeal.

The administrative regulations cover the following issues:

- a regulation instructing the network operators on how and when to submit unbundled accounts information to the Energy Market Authority (natural gas);
- a regulation on the basis of the Authority can issue more detailed instructions on what information and which key figures the network operator has to publish and how the publication shall be carried out (electricity and natural gas);
- a regulation on the publication of technical key figures of the network operation (electricity and natural gas);
- a regulation on the itemization of bills (electricity and natural gas);
- a regulation instructing the retail suppliers on how to publish and inform prices as well as sales terms and conditions (electricity and natural gas); and
- a regulation instructing the network operators on how to publish and inform prices as well as sales terms and conditions (electricity and natural gas)

1.1.3 Independence and accountability

The agency head – director – is appointed for an undefined period of time by the Council of State. As the Energy Market Authority is in the Ministry of Trade and Industry's field of administration the appointment is made on the proposition of the Minister of Trade and Industry. The head of the Authority cannot be dismissed for political reasons.

The Energy Market Authority is overseen by the Ministry of Trade and Industry and especially by its Energy Department according to the standard principles applied in the Finnish public administration. This means agreeing on an annual basis of the objectives and results of the work of the Authority and checking the achievements bi-annually. The Authority has to present an annual report for information to the ministry.

On the other hand, the ministry cannot interfere or influence the decisions by the Authority, as they can only be appealed to the Market Court, Administrative Courts and finally to the Supreme Administrative Court. This guarantees the independence in decision-making.

The Energy Market Authority's operating expenses are financed mainly with supervision and license fees collected from electricity and natural gas network operators and the actors falling within the scope of emissions trading.

1.1.4 Overlapping jurisdictions

The Energy Market Authority has partly overlapping jurisdiction with the Finnish Competition Authority. On the basis of the Act on Competition Restrictions the Finnish Competition Authority has the general supervision mandate over all sectors of the economy including electricity and natural gas markets.

As a general rule, the Energy Market Authority does not have any powers regarding the competitive parts of the electricity and natural gas markets the exceptions being the tasks to supervise retail supply of electricity and natural gas under obligation to supply and to monitor security of supply.

The Energy Market Authority's main areas of supervision and regulation are the network operations in electricity and natural gas markets, and there especially the regulation of pricing and terms and conditions. Furthermore, an important area is the the supervisory tasks in the field of electricity and natural gas supply covered by the obligation to supply. There the Energy Market Authority can interfere with pricing or refusals to supply, for instance. On the basis of the Act on Competition Restrictions and its rules against the abuse of dominant position, the Finnish Competition Authority may investigate the pricing and terms of network services ex post. Additionally, the Finnish Competition Authority may investigate the pricing of electricity and natural gas supply as well as other competition restrictions related to them.

Since the establishment of the sector-specific regulator in 1995, the Energy Market Authority and the Finnish Competition Authority have created a good and functioning platform for co-operation within the limits of their powers and introduced a division of work to prevent forum shopping and contradictory decisions.

1.2 Main developments in the gas and electricity markets

1.2.1 Electricity market

Finland consumed 86.8 TWh electricity in 2004, which was nearly two per cent more than the previous year. Cogeneration of heat and power covered 32 per cent of the consumption of electricity, nuclear power nearly 25 per cent, hydro power 17 per cent and coal-based and other conventional condensing power a good 20 per cent. Wind power accounted for 0.1 per cent. Electricity was imported from Russia to Finland nearly according to the maximum capacity of the import connection and a substantial amount of electricity was exported to the west. Net imports of electricity covered 5.6 per cent of electricity consumption.

At the start of 2005, the Government granted a construction licence for the construction of Teollisuuden Voima Ltd's new nuclear power plant unit. The construction work was started in spring year 2004 and the Olkiluoto 3 power plant unit will be commissioned in 2009. It will be completed at the beginning of the Kyoto target period and it will improve Finland's chances of achieving the reduction targets for GHG emissions. The power plant unit to be constructed is of the pressurised water type. The power plant unit's thermal output will be 4 300 MW and net electric power output 1 600 MW.

In April 2004, the end-customer price of electric energy started to show a falling trend due to a relatively good water situation and forecast. The average end-customer price of electricity

fell by about five per cent in Finland in 2004, whereas a year before the price rose by about 20 per cent. In practice, the distribution prices of electricity have remained nearly unchanged for several years and in the first half of 2005 there was a modest decrease of one per cent. The total price of electric energy including distribution fell by 2.5 per cent in 2004. The price level of electricity fell slightly again at the start of 2005 and by June 2005 the prices had fallen some 3 per cent.

The significant increase in prices of emissions rights during the first half of year 2005 together with the water reservoir situation in the Nordic countries have affected the spot and the futures prices in the Nordic electricity market. In the absence of any change in these parameters the slight downward trend of electricity end-user prices might come to an end and change into an upward trend.

The Finnish electricity market has been an integrated part of the Nordic electricity market since the latter half of the 1990's. The work to further develop the Nordic electricity market continued in 2004. As an outcome of their meeting in Akureyri in Iceland during September 2004, the Nordic energy ministers published an Akureyri Declaration. In the Declaration they noted that the Nordic market was functioning well and that the harmonisation process should continue. The Nordic TSO's were asked to investigate how further co-ordination of the functions of the system responsibility, financing and organisation of Nordic transmission network investments as well as joint management of the power issue could be established. The collaboration organization of the Nordic transmission system operators – Nordel – published its report "Enhancing Efficient Functioning of the Nordic Electricity Market" in February 2005.

The Nordic energy market regulators, who have co-operated unofficially since the year 1999 and officially as the Forum of Nordic Energy Regulators (NordREG) after the signing of the Memorandum of Understanding in 2002, enhanced their co-operation in the year 2004 by preparing a Work Programme for the year 2005. In it four strategic objectives for the work on the Nordic electricity market were stated. The strategic objectives are the following: 1) A truly common Nordic retail market with free choice of supplier, 2) A well-functioning wholesale market with competitive prices, 3) Reliable supply and 4) Efficient regulation of TSOs.

As regards the development of the interconnections of the Finnish electricity transmission network with other EU countries' networks, there were two significant projects. In February 2005, the Finnish and Swedish TSOs published their decision to construct a new cross-border transmission line between Finland and Sweden. The connection – a DC cable of 600 - 800 MW – will strengthen transmission interconnections between the countries and contribute to a decrease in temporary electricity price differences between Finland and Sweden. The submarine cable will be ready in autumn of 2010 and the TSO's will share the ownership and investment costs of the cable, amounting to some 200 million euros.

In February 2005, the Energy Market Authority granted an exemption to Estlink – a commercial line to be built between Finland and Estonia – from certain requirements of the Electricity Market Directive (No. 2003/54/EC) and Regulation (No. 1228/2003). Estlink will be the first interconnection between the Baltic and Nordic electricity systems. The total cost of the project will be some 110 million euros. The commissioning of the Baltic-Finnish submarine DC cable is scheduled to the end of 2006.

1.2.2 Natural gas market

In 2004, natural gas consumption in Finland totalled 4.61 bcm (46.1 TWh), down approximately three per cent from the previous year. Consumption was reduced by the slightly warmer-than-average weather during the year, as well as by the continuously falling electricity price, which reduced the use of natural gas in condensing power generation. All natural gas consumed in Finland is imported from Russia.

Large users account for the bulk of natural gas consumption in Finland. Energy and power companies, which use natural gas to co-generate heat and power, use over 50 per cent and pulp and paper companies over 30 per cent of Finland's total gas consumption. Natural gas accounts for approximately 11 per cent of Finland's total energy consumption.

The gas transmission system operator Gasum Ltd is constructing a parallel pipeline to the existing transmission pipeline. This extension will increase the reliability of gas supply and the transmission capacity from the Russian border to southern Finland and Helsinki region. The length of the pipeline under construction and planning in the years 2005 - 2006 is 103 kilometres. The TSO has also plans to extend the gas pipeline to the western coast of Finland, firstly to Turku region.

1.3 Major issues dealt with by the regulator

1.3.1 Electricity

In the field of electricity, the Energy Market Authority is responsible for regulating 91 distribution network operators, 13 regional network operators and one transmission system operator at the start of 2005. Furthermore, the Authority is mandated with the supervision of altogether 70 electricity retailers with the obligation to supply.

The amendments to the Electricity Market Act, which entered into force at the end of December 2004, implemented the Electricity Market Directive's obligations in Finland. The legislative amendments significantly changed the regulation principles concerning the pricing of the electricity network business.

To enable the launch of the first regulatory period in the field of electricity networks, the Energy Market Authority started the preparation work well ahead in the latter half of 2003. In June 2004, the Energy Market Authority published guidelines¹ for reasonable electricity transmission and distribution pricing. The new type of regulation of the electricity distribution and transmission business was started within the framework of the first three-year regulatory period at the start of 2005, and the network operator-specific confirmation decisions were issued at the end of 2004. Furthermore, the methodology for the pricing of the electricity connection charges was confirmed to all distribution network operators in February 2005.

In its decision in February 2005, the Energy Market Authority exempted the Estlink Project – a submarine DC cable to link Finland and Estonia – from certain provisions of the Regulation

¹ The unofficial English translation of the guidelines is available in the Energy Market Authority's website www.energiamarkkinavirasto.fi.

of cross-border exchanges in electricity (No. 1228/2003) and of the Electricity Market Directive (No. 2003/54/EC) and notified the decision to the European Commission. Subsequently, the Commission decided not to request the Energy Market Authority to amend or withdraw its decision.

To integrate the Nordic electricity market closer with the rest of Europe the meeting of the European Regulatory Mini-Forum for the Nordic region took place in Helsinki on January 19, 2005. The representatives of the European Commission, Member States, national regulators, TSOs and Nord Pool Spot, EEX, ETSO and EuroPEX participated in the meeting of the Mini-Forum.

1.3.2 Natural gas

At the start of 2005, the Energy Market Authority was responsible for regulating 32 natural gas distribution network operators and one natural gas transmission network operator. Additionally, the Authority supervised the wholesale and retail supply activities of the operators as well.

The Natural Gas Market Act, which came into force in the year 2000, was enacted to implement the Natural Gas Market Directive (No. 98/30/EC). Finland has availed itself of the possibility of an exemption allowed by the previous and present Natural Gas Market Directives. Accordingly, the natural gas market has not been opened in the manner specified in the directives. As regards Finland, the directives allow for exemptions from licence procedure, unbundling of network operations and deregulation of market, i.e. from the rules for defining the customers which meet the requirements. The exemption is effective as long as Finland does not have a direct connection to the natural gas network of any other EU Member State and as long as Finland has only one main natural gas supplier.

The Natural Gas Market Act aims to improve the functioning of the natural gas market and to prepare the natural gas sector for the integration of the European natural gas market. The Act provides large-scale consumers, buying at least 5 million cubic metres of natural gas per year, with the possibility of mutual secondary market trading in natural gas they have purchased from an importer operating in Finland. A separate market place has been established for trading on the secondary market. Trade in the secondary market is about one percent of total demand in Finland.

The most important need to amend the Natural Gas Market Act of Finland, resulting from the latest Natural Gas Market Directive, was related to the regulatory model of network pricing. In the new Directive, ex-ante approval of the pricing methodology of network services is required. This means that the regulator will approve in advance at least the methods that all network operators will use to calculate the pricing of network services; the previous ex-post and case-specific regulation had thus to be replaced in Finland.

According to the amendment to the Natural Gas Market Act that entered into force at the start of 2005, the Energy Market Authority shall issue a decision confirming the methods that the network operator must follow when determining the level of return for the network business and the charges to be collected for network services during the regulatory period. The methods to be followed in the pricing of services shall be confirmed before they are introduced.

To enable the launch of the first regulatory period in the field of natural gas networks, the Energy Market Authority started the preparation work in the latter half of 2003. In June 2004, the Energy Market Authority published guidelines for reasonable natural gas transmission and distribution pricing. These guidelines include principles on the valuation of regulatory asset base, determination of the acceptable rate of return on capital, the method of determining the result and the correction of the profit and loss account and balance sheet.

In the natural gas sector, the Parliament ended up postponing the introduction of the new regulation model by a year. Thus the Energy Market Authority issued the network operator-specific confirmation decisions on the methodology for the pricing of natural gas network services in May and June 2005. The first four-year regulatory period will commence at the start of 2006 and end at the end of 2009.

1.3.3 Emissions trading

The Emissions Trading Act, which entered into force in August 2004, served to implement the emissions trading directive adopted by the European Council and Parliament. A number of regulatory activities related to emissions trading laid down in the Emissions Trading Act were assigned to the Energy Market Authority. As the national emissions trading authority, the Energy Market Authority is responsible for, inter alia, issuing emissions licenses to installations within the scope of the emissions trading scheme, supervising compliance with the license conditions, approving the verifiers for emissions trading, monitoring emission reports and setting up and administering an emissions trading register.

The Emissions Trading Act defines the installations falling within the scope of the emissions trading scheme. In Finland, combustions plants with an output of more than 20 MW and also smaller combustion installations connected to the same district heating network as the above mentioned bigger plants, oil refineries, coking plants, as well as some installations and processes of the steel, mineral and forest industries fall within the scope of emissions trading. In Finland, the emissions trading scheme covers around 150 operators.

Within the timeframe of four months set in the Emissions Trade Act the Energy Market Authority issued emissions licenses to about 540 plants. The national emissions trading register was taken into use at the end of February 2005.