

National Report of the Energy Regulatory Office on the Electricity and Gas Industries in the Czech Republic for 2011

July 2012

Most frequent abbreviations

Czech	English	
ČR	CR	Czech Republic
ERÚ	ERO	Energy Regulatory Office
MPO	MIT	Ministry of Industry and Trade of the Czech Republic
ČEPS	ČEPS	Czech transmission system operator (electricity)
OTE	OTE	Market Operator
PXE	PXE	Power Exchange Central Europe, a.s.
EEX	EEX	EEX Leipzig Energy Exchange
SEI	SEI	State Energy Inspectorate
ÚOHS	ÚOHS	Office for the Protection of Competition
APG	APG	Austrian TSO (electricity)
CEER	CEER	Council of European Energy Regulators
ACER	ACER	Agency for Cooperation of Energy Regulators
ENTSO	ENTSO	European Networks of TSOs
CEE	CEE	Central and Eastern Europe region
PDS	DSO	Distribution system operator
PZP	UGS facility	Underground gas storage facility
SAIDI	SAIDI	System Average Interruption Duration Index [minutes/year/customer]
SAIFI	SAIFI	System Average Interruption Frequency Index [interruptions/year/customer]
CAIDI	CAIDI	Customer Average Interruption Duration Index [minutes/interruptions]
VVN	EHV	Extra high voltage
VN	HV	High voltage
NN	LV	Low voltage
OZE	RES	Renewable energy sources
EEPR	EEPR	European Energy Programme for Recovery

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1 Foreword

For the eighth time, the Czech Republic is presenting, through the Energy Regulatory Office, its National Report on the Electricity and Gas Industries, thereby meeting its reporting and notification obligation as set out in the applicable Directives and Regulations. This report mainly describes the Czech Republic's achievements in the implementation of the third energy package.

The year 2011 saw the adoption of an extensive amendment to the Energy Act. The Czech Republic transposed the relevant provisions of the third energy package into the amendment. The amendment has boosted the national regulator's powers of supervision over the functioning of the electricity and gas markets, and transferred inspection competences from the State Energy Inspectorate to the Energy Regulatory Office (ERO). The amendment also contains a number of new provisions that are important in terms of the protection of customers' rights, in particular as regards the execution of agreements on supply terms and conditions.

This implementation of the EU's regulations contained in the third package into the Czech law came into effect as of 18 August 2011 in the form of Act No 211/2011 Amending Act No 458/2000 on Conditions for Business and State Administration in the Energy Industries and on Changes to Certain Laws (the Energy Act), as Amended, and Other Related Laws (hereinafter also referred to as "the Transposition Amendment"). In the electricity industry, this concerns 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 Regulation (EC) No 714/2009 13 July 2009 of the European Parliament and of the Council on conditions for access to the network for cross-border exchanges in electricity; in the gas industry, Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009, concerning common rules for the internal market in natural gas and Regulation (EC) No 715/2009 13 July 2009 of the European Parliament and of the Council on conditions for access to the natural gas transmission networks; last but not least, the package contains Regulation (EC) No 713/2009 13 July 2009 of the European Parliament and of the Council establishing an Agency for the Cooperation of Energy Regulators (ACER).

Reflecting the obligations under Directives 2009/72/EC and 2009/73/EC, the amendment to the Energy Act has markedly reinforced the ERO's powers, in particular in respect of supervision, oversight, and penalisation, and remedial measures in cases of violations of legal regulations, and enforcement of sanctions. The Transposition Amendment has also helped to enhance the ERO's independence of the government (this mainly involves a change in the appointment of ERO Chairperson, who is now appointed by the President of the Republic, and provisions for the ERO's maximum possible financial independence), all of this with a view to increasing the efficiency of regulation in energy industries.

The Transposition Amendment has extended the ERO's competences to include completely new areas of oversight and supervision, which are specified in Section 17 (7) (h), (j) and (m) of the Energy Act, namely investigations concerning the functioning of the electricity and gas markets. It permits the imposition of measures to ensure the proper functioning of these markets when shortcomings are identified, monitoring of restrictive or unreasonable terms and conditions in contracts on the electricity and gas markets, monitoring of technical co-operation between electricity and gas transmission system operators in the European Union and vis-à-vis third countries, monitoring of the situation in competition on wholesale and retail electricity and gas markets, and publication of yearly reports on the results of

monitoring in energy industries, and yearly and monthly reports on the operation of the electricity grid and the gas system.

The Transposition Amendment has also significantly strengthened the ERO's supervisory and oversight powers in relation to supervision over the transparency and openness of the energy market, because Sections 18a and 18b of the Energy Act now allow the ERO to conduct inquiries on the electricity and gas markets into the working of effective competition and to conduct investigations in local business premises. Thus, the ERO now has the duty to supervise compliance with Czech and EU legislation providing for efficient and transparent functioning on electricity and gas markets.

In connection with the ERO's power to oversee the functioning of competition, the Energy Act now contains a new Section 17c, which provides for the ERO's co-operation with the Office for the Protection of Competition (ÚOHS) in relation to the ERO's above competences. The two Offices are therefore obliged to provide suggestions and information to one another, and to adopt any other suitable forms of their collaboration, to ensure effective and efficient oversight over competition in the electricity and gas markets.

2 Main developments in the electricity and gas markets

The electricity market experienced rapid development in 2011. As regards the completely open electricity market, its characteristic feature was a considerable increase in the number of supplier switches. In the case of households, the number of supplier switches doubled in 2011 over 2010, and the overall number of supplier switches in all customer categories rose by two fifths over the preceding period. The integration of the wholesale electricity markets in central Europe (the CEE region) registered significant progress. One of the highlights of the year was the signing of a Memorandum of Understanding on 30 May 2011, which marked the launch of a project for integrating the day-ahead electricity markets in the Czech Republic, Slovakia and Hungary. This project is an expansion of the successful coupling between the Czech and Slovak day-ahead markets and was supported by the national regulators with a view to advancing the integration of the European electricity market. Intensive work on the tackling of specific technical details was running for the whole year. The final coupling of the markets is expected at the beginning of the fourth quarter of 2012.

As regards the gas market, it also developed dynamically in the year under review. In relation to the plans to enhance the flexibility and diversification of the gas flows in the gas transmission system, several capital projects were completed in 2011. Some parts of the transmission system have also been modified to support the reverse flow of gas from the west to the southeast of the Czech Republic in the direction of Slovakia, Hungary, Austria and southern Germany. The purpose of these adjustments was to reinforce the transmission capacity of the system from the German/Czech national border to the Czech/Slovak national border, thereby ensuring a safe and flexible distribution of gas flows in Europe.

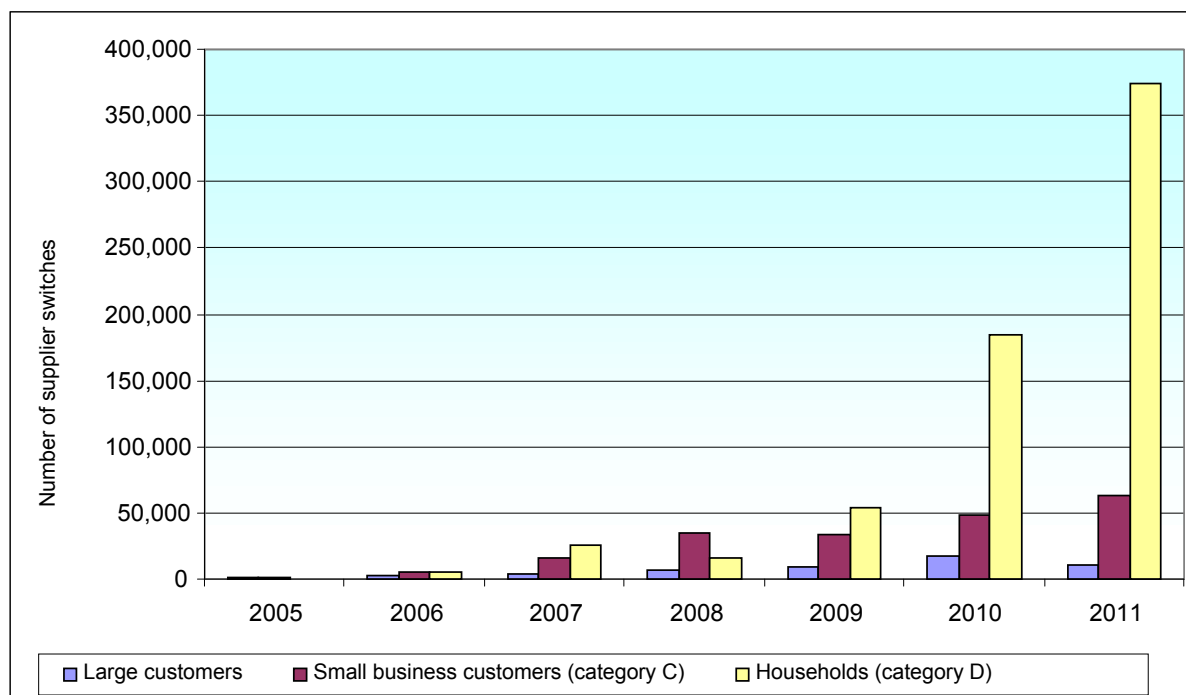
The GAZELLE gas pipeline was a major capital project also in 2011. On the basis of the ERO's decision of 28 July 2011, this interconnector was exempted from the obligation to allow regulated third-party access under the conditions laid down in the Energy Act. An approving decision on ownership unbundling was delivered on 2 August 2011. Both of these decisions were upheld by the European Commission's decision of 1 December 2011.

The visible increase in liquidity, primarily in connection with the considerable differences between the prices charged by the various suppliers, resulted in a steep rise in the number of gas supplier switches. Most of these supplier switches took place in the segment of small business customers and households: compared with 2010, the number of switches almost quadrupled. In the large customer segment, almost one third of customers changed their gas supplier. A major highlight in the gas sector was also the commissioning of the new STORK gas pipeline, the very first gas pipeline interconnecting the Czech Republic and Poland. This gas pipeline has helped to deepen the integration of regional energy markets and also to enhance energy security and diversification of gas sources for the Czech Republic.

3 The electricity market

Intensive use of the fully opened market, a trend started in 2010, continued in 2011, with the number of supplier switches increasing again. According to the data recorded by OTE, a.s. for households, two times more households switched their supplier last year (374,000 in 2011 versus 184,000 in 2010). On the whole, almost 450,000 customers changed their electricity supplier in 2011 (in 2010 the figure was approximately 250,000). Development in the number of electricity supplier switches can be seen in Chart 1.

Chart 1 Annual electricity supplier switching in the main customer categories



Source: OTE, a.s.

On its website, the Office sought to provide all 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, 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. In 2011, it repeatedly published warnings against door-to-door salesmen and provided information about ongoing inquiries at certain traders. During 2011, the above ready reckoner was not only one of the most visited applications on the Office's website; traders' increased interest in this application was also registered. While in the preceding years most of the electricity supplier switches were attributable to customers migrating from incumbent suppliers of vertically integrated companies to alternative suppliers, in 2011 the market was so liquid that it was no longer possible to identify the main direction of supplier switches. In general, customers followed the lowest price.

Electricity supply prices for low-demand customers connected to the LV level were generally negatively affected by the amount of subsidies paid to renewable energy sources in 2011.

At the low voltage level, the same range of tariffs, including the conditions for awarding them, as in 2010 was maintained for small business customers (category C) and households (category D) for 2011.

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 offered a product where the offering price of energy depends on electricity prices at energy exchanges during the year for small customers as well.

3.1 Network regulation

3.1.1 Unbundling of the transmission and distribution systems

The transposition amendment has significantly modified and extended the legislation on unbundling. It also has a fundamental importance not only from the perspective of the statutory provisions on the unbundling itself of the electricity transmission system operator but also in terms of supervision, inspection and penalisation for violations of the rules of ownership unbundling thanks to the ERO's extended competences.

The electricity transmission system operator, ČEPS, a.s., was fully unbundled from electrical energy producers and distributors as early as 3 September 2009.

In respect of the unbundling of distribution system operators, Article 26 of Directive 2009/72/EC maintains the concept of the legal and functional unbundling of distribution system operators, with some formal changes concerning the position of the person responsible for monitoring the compliance programme of the distribution system operator. Implementation of these formal modifications is the subject of Section 25a(3) to (5) of the Energy Act.

Under Article 26(2)(c) of Directive 2009/72/EC, in the electricity industry the distribution system operator shall have at its disposal the necessary resources including human, technical, physical and financial resources. Since such a requirement can also be applied to any system operator and other energy business entities, this provision of the Directive has been implemented through a new provision, Section 11(1)(m) of the Energy Act, which applies to all licence holders.

3.1.2 Technical functioning

In 2011, the ERO focused in this area mainly 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, if needed, this public notice to tighten the prescribed limits or introduce more targeted standards and, above all, for introducing motivational regulation of quality.

Under the quality public notice, the ERO monitors and evaluates the continuity of electricity transmission and distribution in the transmission and distribution systems. Conclusions derived from the data received from the transmission system operator and regional distribution system operators are outlined in the following.

Electricity transmission

Under the Energy Act, transmission system facilities are understood to be 110 kV lines and plant that are not part of a distribution system, and 400 kV and 220 kV lines and plant serving for electricity transmission in the Czech Republic, including the I&C, protection, and ICT systems.

The level of quality in the transmission system is defined by standards of electricity transmission continuity, set out in Section 21 of the quality public notice. The following ratios are set out for the transmission system operator in the public notice:

- a) Average duration of an interruption in electricity transmission in the calendar year (min)
- b) Electrical energy not supplied in the calendar year (MWh)

Table 1 Electricity transmission continuity ratios in 2011

Transmission continuity ratios in 2011	
Number of electricity transmission interruptions in the year [-]	6
Total duration of electricity transmission interruptions in the year [min]	121
Average duration of an electricity transmission interruption in the year [min]	20.2
Electrical energy not supplied in the year [MWh]	225.3

Source: ČEPS, a.s.

Electricity distribution

The data reported by the respective companies can be categorised into two groups. One category includes information about the continuity of electricity supply in networks, i.e., data affected by failures and planned events in operated distribution systems. The other category includes information about the ‘commercial quality’, which characterises the distributor’s or supplier’s ability to respond to final customers’ requirements and which is not directly related to the physical operation of the systems.

The level of quality in distribution systems is defined by electricity distribution continuity ratios set out in Section 21 of the quality public notice. The following ratios are set out for continuity in the public notice:

- a) Average frequency of sustained electricity distribution interruptions per customer in the period under review (SAIFI)
- b) Average duration of electricity distribution interruption per customer in the period under review (SAIDI)
- c) Average time needed to restore electricity distribution to the average customer per sustained interruption in the period under review (CAIDI)

The continuity ratios have been computed in line with Appendix 5 to the quality public notice. In the case of electricity distribution continuity ratios, the values of system ratios are stated. These ratios cover all categories of electricity transmission/distribution interruption under Appendix 4 to the public notice.

Table 2 Electricity distribution continuity ratios in 2011

Indicator*	ČEZ Distribuce	E.ON Distribuce	PREdistribuce	CR
SAIFI [interruptions/year]	2.88	2	0.65	2.36
SAIDI [min/year]	296.7	314.4	46.79	268.82
CAIDI [min]	103.15	157.26	72.13	113.87

Source: Regional distribution companies

* System indicators that include all categories of interruption under Appendix 4 to public notice no. 540/2005

3.1.3 Network tariffs for connection and access

Under the Energy Act and public notice 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 incidental to electricity supply on an annual basis. These charges are heavily influenced mainly by inflation factors, the level of overall consumption, the price of electrical energy for covering network losses, and, last but not least, the rapid increase in renewable electricity generation, primarily in photovoltaic plants.

Charges for network services are composed of charges for transmission and distribution services, which are further broken down to the charge for network use and the charge for booked network capacity.

The charge for using the 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 almost did not change year-on-year and so the main factor is the drop in energy prices on the wholesale market. The charge for capacity booking in the transmission network rose by 1.1 percent year-on-year, mainly due to inflationary factors.

As in transmission, the charge for network use in distribution serves for covering network losses. Its level for 2011 was also favourably influenced by the prices of electrical energy. At the level of EHV distribution networks, this item was stable and at the HV level it declined to about 94 percent of the charge in 2010. The charges for booked capacity at the various voltage levels are mainly influenced by the agreed technical parameters of capacity, the volume of investment at the respective voltage level, and the charge for capacity booking in the higher-level transmission system. Reflection of inflation and the decrease in the capacity booked by customers, together with the correction factors for 2009, had an unfavourable effect on the unit charge for capacity booking in distribution networks. For this reason, in 2011 this item increased by 8.1 percent at the EHV level and by 6.3 percent at the HV level year-on-year.

The electricity distribution charges also include the controlled price to meet the extra costs incurred in support for electricity from renewable energy sources (RES), combined heat and power generation (CHP) and secondary sources (SeS). The considerable rise in extra costs in 2011 was mainly caused by the large amount of electricity planned to be produced in photovoltaic plants, but also from biogas, biomass and wind. Overall extra costs of RES, CHP and SeS, together with the correction factor and the calculated imbalance, amounted to about 32 billion crowns compared to the less than 8 billion crowns in 2010 prices. This surge in the extra costs for support of RES, CHP and SeS electricity therefore had a heavy impact on the final customers' uniform nationwide contribution to this support. Thanks to the successfully completed legislative process concerning the amendment to Act No 180/2005, on Support for Electricity Generation from Renewable Energy Sources, and the measures subsequently adopted before the end of 2010, a government subsidy of CZK 11.7 billion could be included in the resulting prices, thereby reducing the contribution to CZK 370/MWh from the originally calculated CZK 578/MWh. However, this item continues to take a major share in the overall growth in controlled prices.

No changes occurred in connection conditions. 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. The technical conditions for connection are stipulated in the rules of the transmission/distribution system operation (the grid code). All of these documents are available on the respective companies' websites.

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 has also set the allocation rules for the allocation of overhead costs for companies that operate more than one regulated activity.

3.1.4 Cross-border issues

Under Section 24 (10) (f) of the Energy Act, the Czech transmission system operator, ČEPS, a.s., follows the transmission system operation rules, which also provide the algorithms for calculating and allocating cross-border capacities and congestion management at cross-border interconnection points.

In connection with the liberalisation of the electricity market in the EU, in operations control ČEPS actively cooperates with foreign transmission system operators within the European Networks of Transmission System Operators (ENTSO-E). This co-operation entails exchange of operating data, which results in forecasting models for each of the systems and analyses of dangerous situations. On the basis of such analyses harmonised cross-border measures are arranged to ensure safe operating conditions.

The volume of available cross-border capacities depends on the physical flows of electricity and also the commercial utilisation of the particular cross-border interconnection point. ČEPS calculates transmission capacities using the NTC method in line with the approved transmission system operation rules.

All available cross-border capacities in electrical lines are offered via non-discriminatory market mechanisms, i.e., at all interconnector points, with the exception of the ČEPS-SEPS interconnection; annual, monthly and daily explicit auctions are organised and held by the Central Allocation Office.¹ Detailed conditions for transmission capacity allocation are described in the Central Allocation Office's auction rules. In the case of the ČEPS-SEPS interconnection, capacity need not be booked for long-term cross-border transmission. At this point, daily transmission capacity is allocated in implicit auctions, which is a part of the mechanism that couples the Czech and Slovak spot markets. This means that up to the reserved cross-border transmission capacity, cross-border transmission can take place without the need to book.

Another highlight of 2011 was the signing of a Memorandum of Understanding on 30 May 2011, which marked the launch of a project for the integration of the Czech, Slovak and Hungarian day-ahead electricity markets. This project is an extension of the successful coupling of the Czech and Slovak day-ahead markets and has been supported by national regulators with a view to boosting the integration of the European electricity market. Throughout the year, the specific technical details were intensively tackled, and the final integration of these markets is expected at the beginning of the fourth quarter of 2012.

In Section 19a(1), the Energy Act sets out that in regulating electricity transmission prices, the ERO “shall take into account the plan for the development of the electricity transmission system and the plan for the development of the gas transmission system, approved by the ERO, and the predictable future demand and requirements for the operating safety of the electricity transmission system...”. These development plans reflect the Community-wide transmission system development plans and the infrastructure projects that are implemented as part of thereof, and therefore contribute to electricity market integration. All investments

¹ Central Allocation Office GmbH is a company with its registered office in Freising, established jointly by 8 TSOs in the CEE region.

are based on non-discriminatory motivation in line with the third package.

In the Czech Republic, there is no independent electricity transmission system operator within the meaning of Article 13 of Directive 2009/72/EC; the ERO therefore has no obligation to monitor the use of the congestion charges under Article 37(3)(f).

In 2011, the ERO assessed the transmission system development plan primarily with regard to its future impact on regulated prices, and requested the rationale for the amount of capital expenditure earmarked for each of the envisaged projects.

The investment plan submitted by ČEPS, a.s. covered the period 2011-2024 and proposed an extension of the system by about 20 percent and average capital expenditure at CZK 4.7 billion every year. The investment programme included the construction of new 400 kV substations and lines.

The assessment also included an analysis of the reasons cited for the various investment plans and evaluation of the risks arising from their non-acceptance. From the perspective of the national plan's compatibility with the Community-wide network development plan, no shortcomings were found. Further, in respect of some of the investments necessitated by customers, the method of funding capital expenditure and the procedure of executing letters of intent or connection agreements were also subjected to scrutiny.

In 2011, transmission system operators and, in turn, regulators in the CEE region were unable to reach agreement on the further procedure for implementing the flow-based method of capacity allocation (disagreement persisted primarily in respect of the question of whether explicit flow-based auctions, or market coupling based on the ATC method², should be implemented first). Nevertheless, December 2011 saw a high-level meeting of regulators and with the assistance provided by ACER, intensive talks were opened with a view to reaching a compromise solution. The purpose is to clarify further steps and ensure the preparation of a plan for the implementation of the target model of electricity market in the CEE region. The ERO took an active part in these talks.

3.1.5 Compliance

In 2011, the ERO drafted and promulgated some new implementing legal regulations, or amendments to earlier regulations, necessitated by the experience with their application on the liberalised energy markets and also by the passing of the transposition amendment, which substantively amended the Energy Act. In 2011, the ERO promulgated a new public notice under no. 210/2011 on the scope, essential particulars and dates of the billing of electricity, gas and thermal energy supply and related services.

During 2011, the ERO also amended the following implementing legal regulations: Public notice no. 371/2011, amending no. 541/2005, on Electricity Market Rules and principles of pricing the electricity market operator's activities and on the execution of certain other provisions of the Energy Act, as amended; Public notice no. 392/2011, amending no. 426/2005 on the details of licensing for business in energy industries, as amended; Public notice no. 393/2011, amending no. 140/2009, on regulatory methods in the energy industries and procedures for price control, as amended by no. 264/2010. In 2011, the ERO also drafted a new public notice on regulatory reporting.

The ERO exercised its authority to request any information from undertakings in the electricity industry, several times in various contexts, in particular for the purpose of initiating

² Available transmission capacity

ex post checks of compliance with obligations under the Energy Act and/or the law on consumer protection, or the law on prices; see Section 15a of the Energy Act.

The ERO generally oversees compliance with the obligations imposed on licence holders under the Energy Act. For this purpose, in 2011 it carried out a number of inspections, although the inspection remit passed to the ERO only as of 18 August 2011.

3.1.6 Dispute settlement

In 2011, the ERO did not adjudicate any disputes in the electricity industry falling under Article 37(5)(c) of Directive 2009/72/EC. No dispute falling under Article 37(11) or Article 37(4)(e) of Directive 2009/72/EC was addressed in the electricity industry in 2011.

3.2 Promoting competition

3.2.1 Wholesale markets

3.2.1.1. Price monitoring

In the Czech Republic, electricity is traded at the energy exchange, Power Exchange Central Europe, a.s. (hereinafter also “PXE”), under bilateral contracts, and in spot markets organised by the market operator (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 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. Spot products are traded through the PXE system on the OTE platform. In addition to physical products, PXE has also introduced trading in financial products without an obligation of physical supply.

Due to the co-existence of PXE, OTC bilateral contracts, and spot markets organised by the market operator it is not feasible to clearly determine the percentage of consumption “originating” from each of these markets. A physical supply of 1 MWh of electricity taken by a final customer may originate from several earlier transactions between the market players. This principle is also apparent from the products themselves at the energy exchange, where an annual product automatically falls apart into shorter products (a quarter, a month). Market participants can therefore use shorter products for continuously balancing their trading positions prior to the physical supply/take.

For the above reasons, PXE data shown below has been left without further comments.

Table 3 Overall trading at PXE in 2011

Number of trading sessions			253
Overall PXE futures market CZ, SK, HU			
Volume traded		[MWh]	24,343,699
of which	BASE LOAD	[MWh]	23,972,119
	PEAK LOAD	[MWh]	371,580
Volume traded		[EURm]	1,327.433
of which	BASE LOAD	[EURm]	1,301.863
	PEAK LOAD	[EURm]	25.57
Traded contracts		[MW]	8,693
of which	BASE LOAD	[MW]	7,878
	PEAK LOAD	[MW]	815
Number of trades			1,242
of which	BASE LOAD		1,137
	PEAK LOAD		105
Average daily volume		[MWh]	96,220.15
of which	BASE LOAD	[MWh]	94,751.46
	PEAK LOAD	[MWh]	1,468.70
Spot product market			
Volume traded		[MWh]	31,355
Volume traded		[EURm]	1.656
Traded contracts		[MW]	1,315
Number of trades			113

Table 4 Trading in Czech physical products at PXE in 2011

Number of trading sessions			253
Czech physical futures market			
Volume traded		[MWh]	2,181,269
of which	BASE LOAD	[MWh]	2,179,889
	PEAK LOAD	[MWh]	1,380
Volume traded		[EURm]	116.567
of which	BASE LOAD	[EURm]	116.484
	PEAK LOAD	[EURm]	0.084
Traded contracts		[MW]	661
of which	BASE LOAD	[MW]	656
	PEAK LOAD	[MW]	5

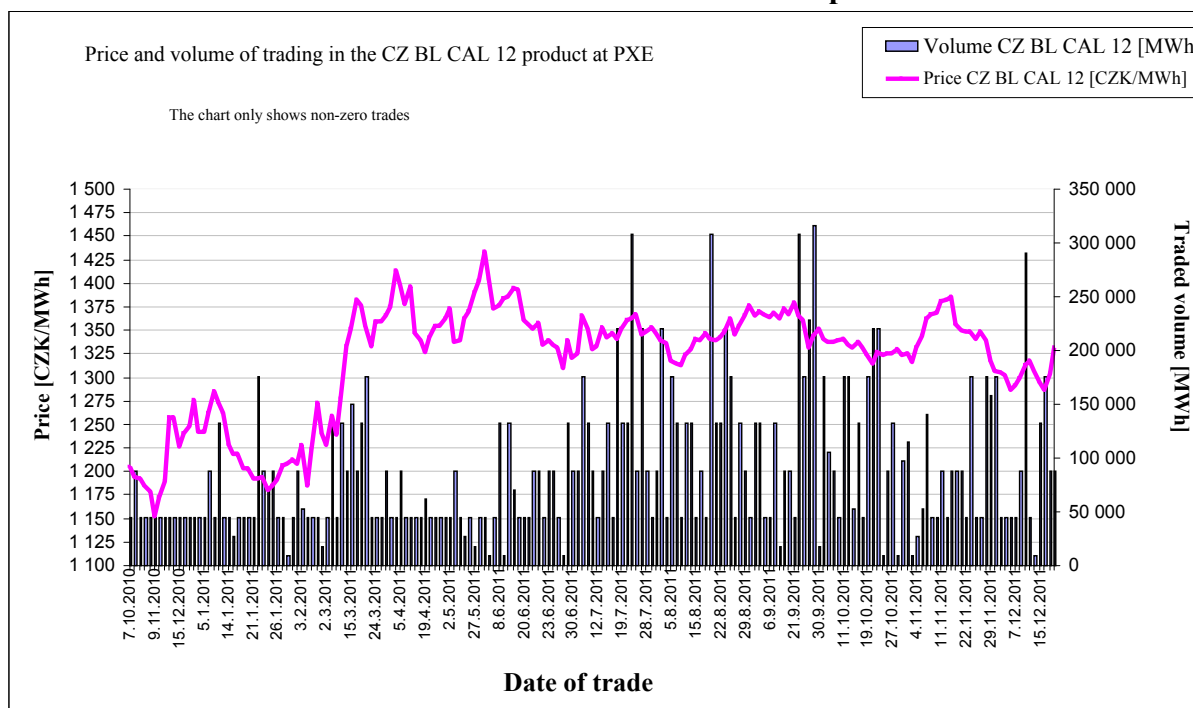
Table 5 Trading in Czech financial products at PXE in 2011

Number of trading sessions			253
Czech financial futures market			
Volume traded		[MWh]	20,061,968
of which	BASE LOAD	[MWh]	19,707,428
	PEAK LOAD	[MWh]	354,540
Volume traded		[EURm]	1,095.992
of which	BASE LOAD	[EURm]	1,071.698
	PEAK LOAD	[EURm]	24.294
Traded contracts		[MW]	7,092
of which	BASE LOAD	[MW]	6,302
	PEAK LOAD	[MW]	790

Source for tables 3, 4, and 5: PXE

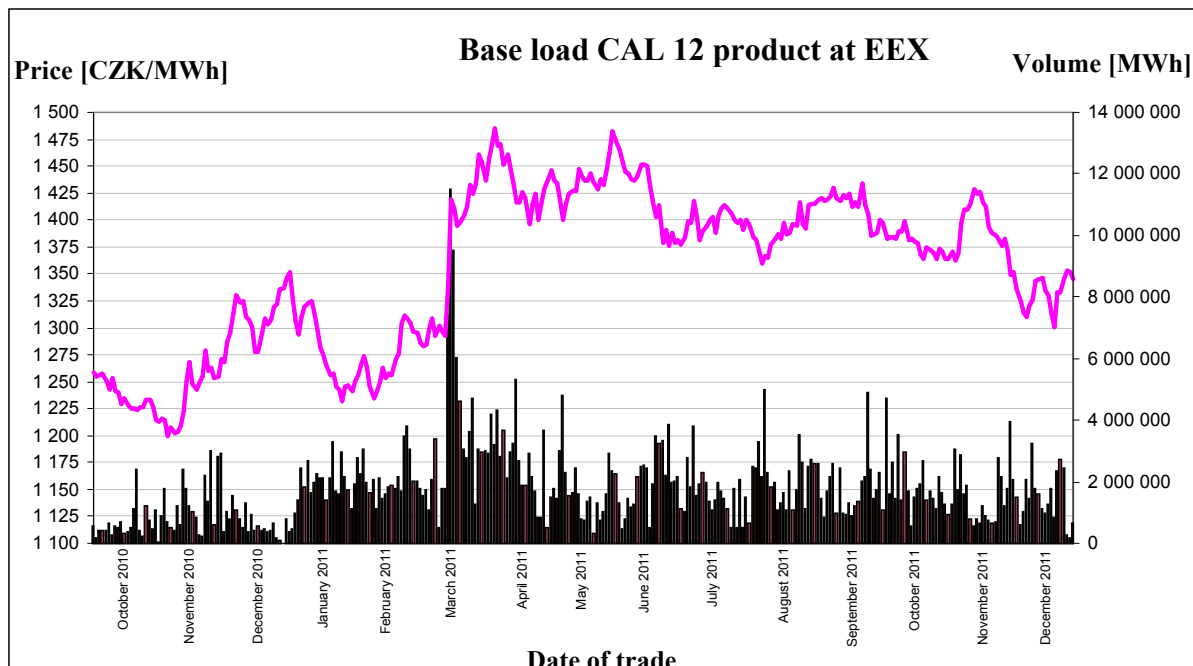
The prices of the products traded at PXE (or the spot market organised by OTE) are closely correlated with those at the Leipzig energy exchange, EEX, for products to be delivered to the German and Austrian electricity grids (see Chart 3).

Chart 2 Prices of annual base load for 2012 for the Czech Republic at PXE in 2011



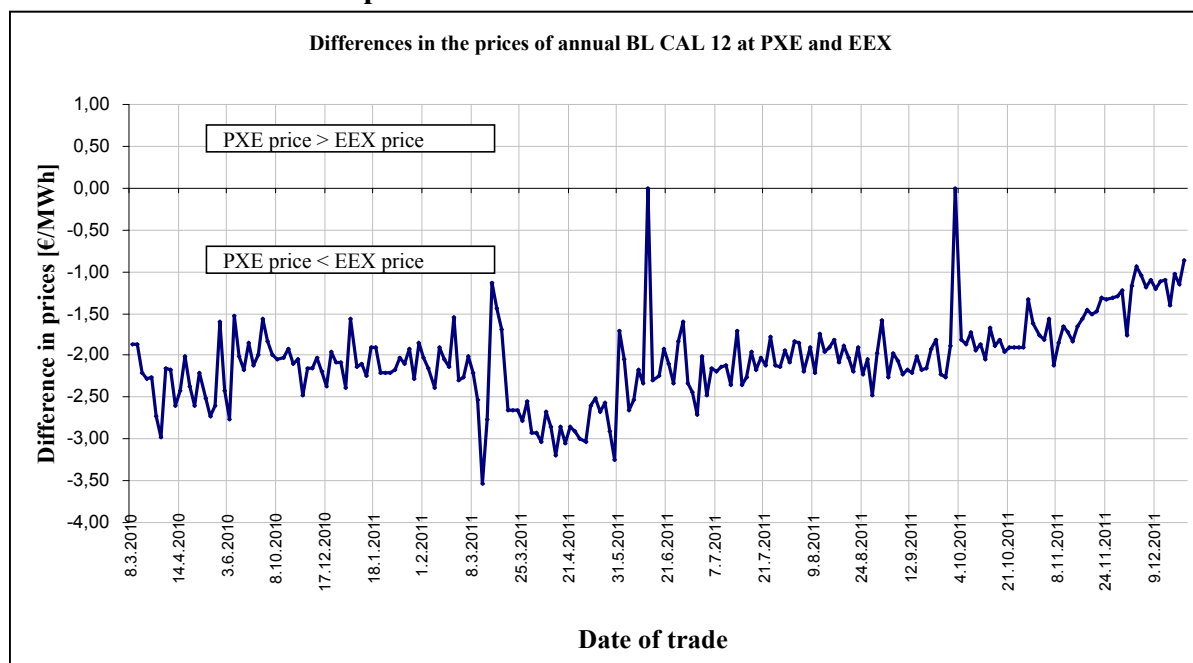
Source: PXE

Chart 3 Prices of annual base loads for 2012 at EEX in 2011



Source: EEX

Chart 4 Differences in the prices of annual BL CAL 12 at PXE and EEX in 2011



Source: PXE, EEX

The remaining volume of electricity is traded under OTC bilateral contracts and also on the spot markets (day-ahead and intra-day markets) organised exclusively by the market operator since February 2009. All cleared entities, i.e., not only traders and producers but also the customers who are responsible for imbalances (the so-called entities subject to clearing), can go to the spot market to procure electricity.

3.2.1.2. Monitoring the level of transparency, including compliance with transparency obligations, and the level and effectiveness of market opening and competition

In this respect, the ERO did not report any activity in 2011.

3.2.2 Retail markets

As regards electricity traders' market position, this market is fully liberalised in the Czech Republic at both the wholesale and retail levels. Electricity traders are therefore not legally constrained at all in buying electricity directly from producers (generators) or at exchanges or on spot markets in the Czech Republic and in other countries. At the same time they have the right to sell electricity to market participants to other countries. The scope of the stored data on the performance of agreements on the supply of electricity, or derivatives thereof, has been laid down by the ERO in an implementing legal regulation.

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, a.s.

In connection with consumer protection, the transposition amendment to the Energy Act has further empowered customers through the provisions of Section 11a of the Energy Act, which now requires electricity generation and electricity trading licence holders to publish, in a manner allowing remote access, their terms and conditions of electricity supply and electricity supply prices for households and natural persons who carry on a business taking electricity from the LV level. Licence holders shall also publish any changes to electricity supply prices or changes to other conditions of electricity supply no later than 30 days before the day of effect of such changes.

3.2.2.1. Price monitoring

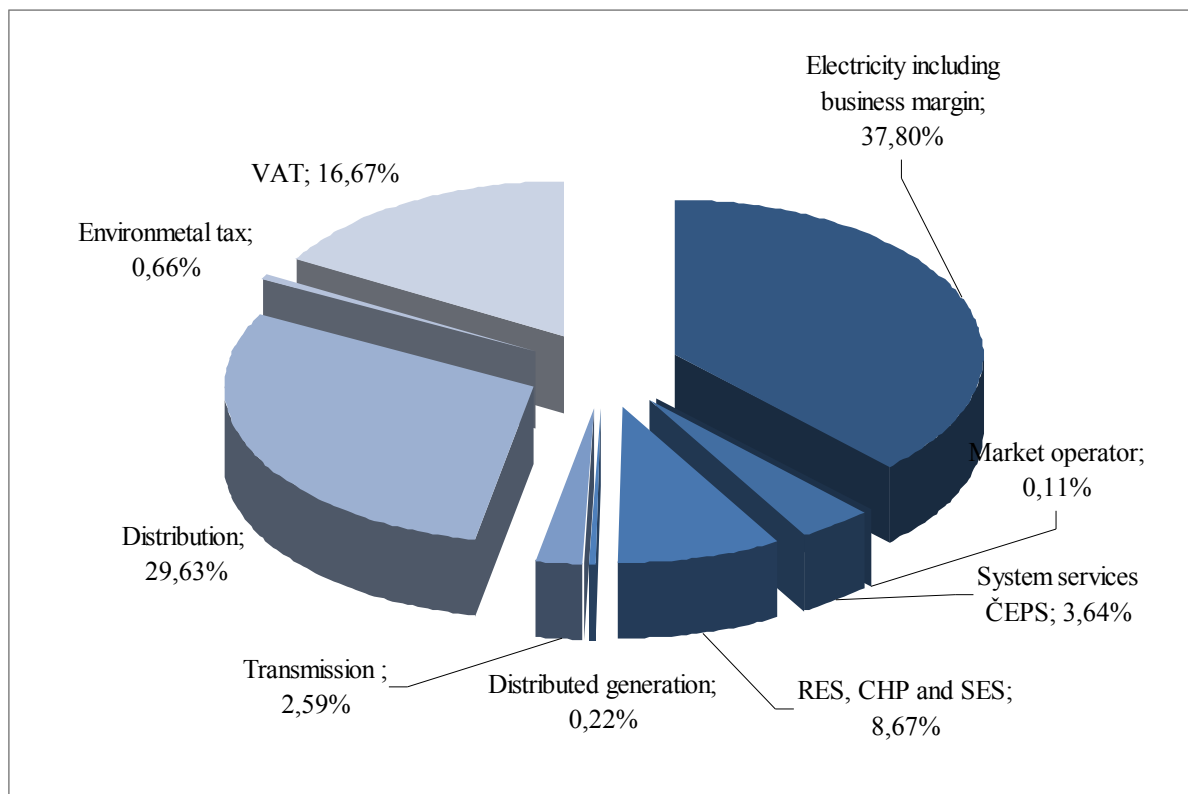
The overall price of electricity supply for customers at the LV level is made up of the regulated items of charges for distribution and related services and the unregulated prices of electrical energy products, which are determined by the supplier selected by the customers.

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 supported clean sources, line losses, the development of the size and structure of consumption, and the rate of inflation).

For 2011, the average increase in the overall price of electricity supply for households was 4.6 percent and for low-demand business customers it was 4.5 percent (net of tax items). The change in electricity price for each individual customer could differ from the above values due to the selected tariff, rated current of the main circuit breaker upstream of the electricity meter, nature and size of consumption and, last but not least, in relation to the supplier of the energy.

Chart 5 shows the percentage shares (including VAT and electricity tax) of the various components in the resulting price of electricity supply for households for 2011.

Chart 5 Percentage shares taken by each of the components of the price of electricity supply at the LV level in 2011



Source: ERO

3.2.2.2. Monitoring the level of transparency, including compliance with transparency obligations, and the level and effectiveness of market opening and competition

In this respect, the ERO did not report any activity in 2011.

3.2.3 Recommendations on supply prices

Eligible 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 consumption.

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 circuit breaker they can influence the fixed components of the regulated charge. 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, 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.

Customers are able to proactively influence a part of the costs of electricity at the LV level by selecting their supplier of energy; the rest 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 consumption; on average, regulated items account for less than 50 percent of the resulting price of supply for household customers (but only 20 percent for some tariffs).

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.

3.2.4 Carrying out investigations and imposing measures to promote effective competition

The transposition amendment has markedly broadened the ERO's competences and Section 17c of the Energy Act has remodelled the ERO's co-operation with 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 as the disclosing side guarantees.

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

In 2011, the ERO did not conduct any investigations within the meaning of the respective requirements of the above Articles of Directive 2009/72/EC.

3.3 Consumer protection

Act No 211/2011 has, among other things, further empowered consumers/customers in the energy industries, and broadened their rights and enhanced their protection, in line with Annex 1 to Directive 2009/72/EC, mainly by amending Section 11a of the Energy Act through which the provisions of Article 3 of Directive 2009/72/EC and Annex I to the Directive have been transposed into the national law.

Section 11a of the Energy Act lays down, *inter alia*, that traders shall publish, in a manner allowing remote access, their terms and conditions and electricity supply prices for households and natural persons who carry on a business, no later than 30 days before the day of effect of any change to these prices or other terms and conditions. Section 11a of the Energy Act also establishes customers' right to withdraw from the contract free of charge in the case of their disagreement with a change to the contract terms and conditions, or a price hike, and sets out the time limits for exercising the right to withdraw from the contract and the effect of such withdrawal. The law also contains provisions on the customers' right to select the method of payment for electricity supply, and stipulates that the system of advance payments shall be fair and reasonable.

In its valid and effective wording, the Energy Act does not define 'vulnerable customer'; as regards customers who can be regarded as 'socially disadvantaged', certain measures for their protection or support are provided for at the level of generally applicable legal regulations in the domain of social security law.

Further, under Section 17(7)(l) and (q) of the Energy Act, the ERO shall publish recommendations on electricity pricing for households and shall cooperate with civic

associations and other juristic persons established for the purpose of protecting consumer rights in the energy sector.

Under Section 17(7)(e) of the Energy Act, the ERO 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 electricity supply/distribution, disputes seeking a declaration of whether or not a legal relationship between the customer and licence holder has come into existence, continues to exist, or has ceased to exist, and also disputes over compensation for failure to keep the set standards of quality and services in the electricity industry.

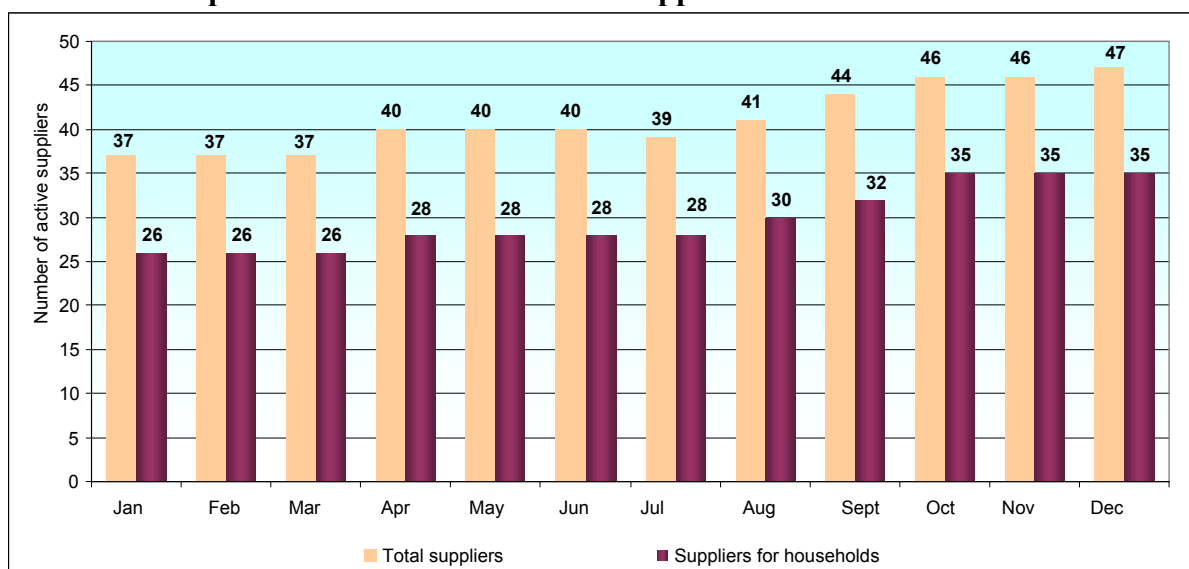
Under Section 17(7)(f) of the Energy Act, the ERO is also competent to perform inspections in the energy industries and to perform supervision over the performance of the duties laid down by the law on consumer protection in respect of business in energy industries (use of unfair business practices,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

In connection with the extension of the statutory provisions related to consumer protection, the ERO has set up a Consumer Protection Unit tasked with receiving and addressing submissions, questions, suggestions and complaints from customers.

4 The gas market

Several new gas traders entered the market in 2011, although the growth in their number was not as steep as in the previous years. Not all of the suppliers offered gas supply to all gas customer categories; some traders specialise only in the high and medium-sized demand segments. The following chart indicates the development of the number of active gas traders. A trader who actually delivered gas to customers in the respective month is regarded as an active trader.

Chart 6 Development of the number of active suppliers in 2011

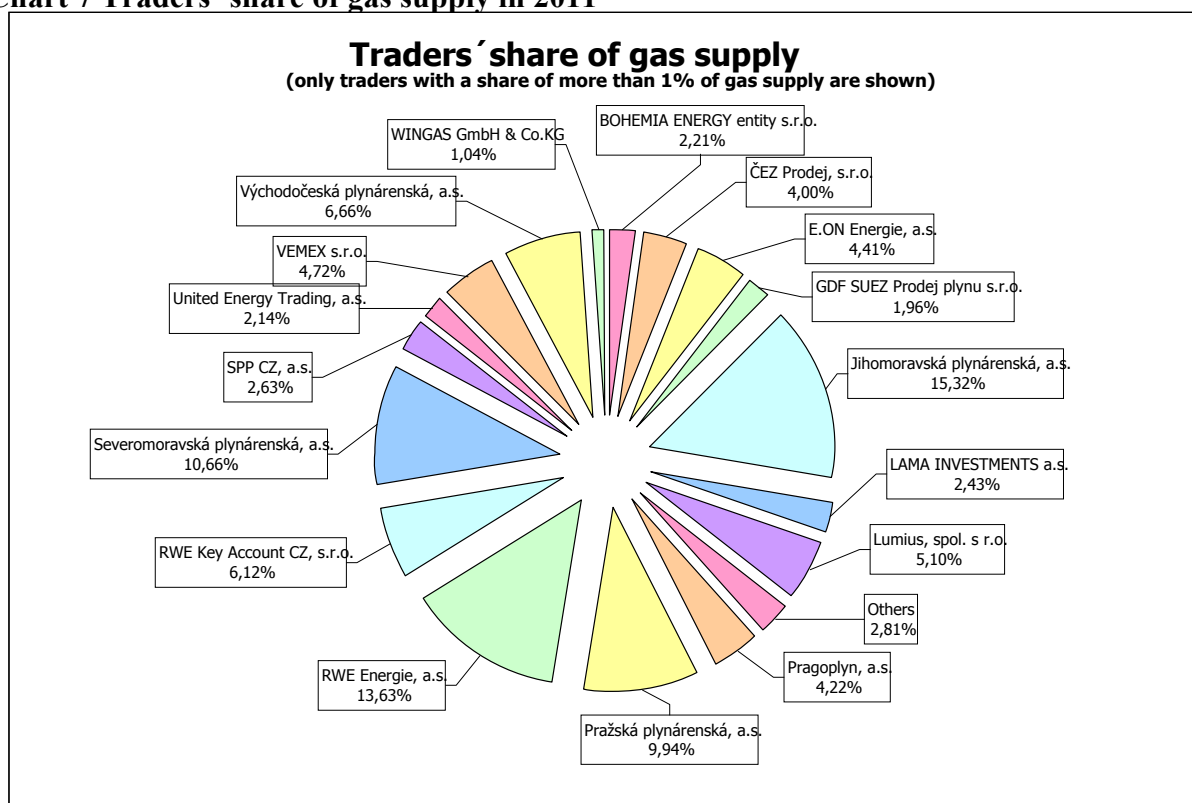


Source: ERO

The RWE Group's traders held the largest market share; between them, they sold 52.4 percent of the gas consumed. Pražská plynárenská, a.s. followed with its 9.9% share of the gas quantity supplied. The other gas suppliers with appreciable shares of the gas sold to customers included Lumius, s.r.o., VEMEX, s.r.o., and E.ON Energie, a.s. in 2011.

For 2011, the procedure for supplier switching was modified by an amendment to the Gas Market Rules. The modifications were based on gas market participants' suggestions and the experience with the practical working of the rules that had been set for the preceding period. The purpose of the new settings related to timing and procedures was to ensure a quicker and easier exercise of the customers' statutory right to gas supplier switching.

Chart 7 Traders' share of gas supply in 2011



Source: OTE

On the fully liberalised gas market, dynamic development related to the significant differences between prices charged by the various suppliers was registered. Almost 13 percent of all customers used the possibility to switch their supplier, while 3 percent of customers changed their supplier in 2010.

The strongest migration was registered in the segment of small businesses and households, namely 360,262 supplier switches accounting for 99.5 percent of the total number of switches.

In the medium-sized demand category, 1,142 customers decided to change their gas supplier in 2011, up by 69 percent over 2010.

In the high-demand customer category, 537 gas supplier switches took place in 2011. More than 31 percent of all high-demand gas customers changed their supplier.

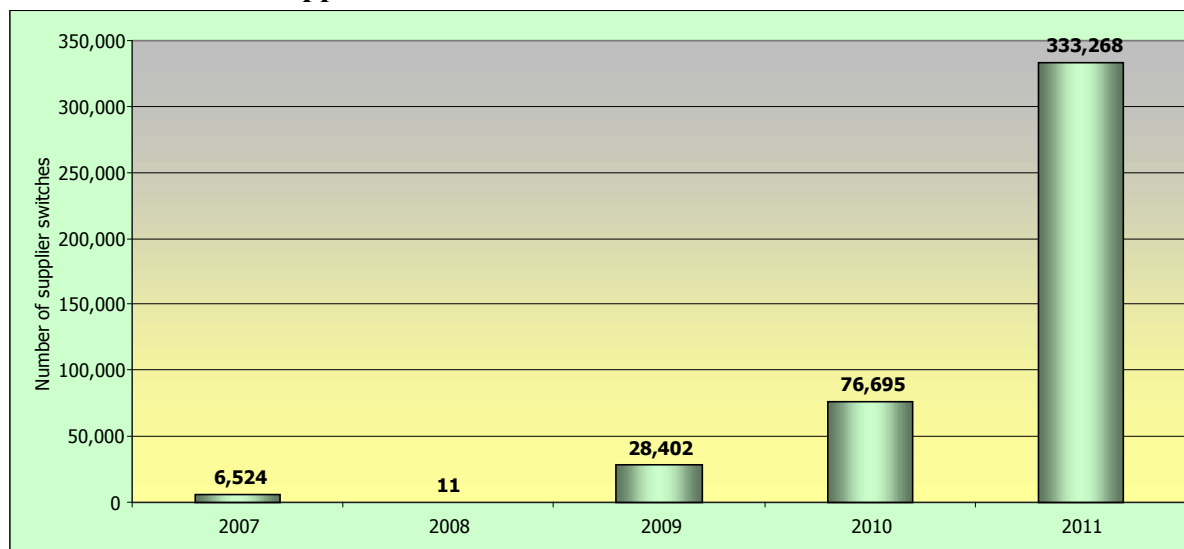
The single largest number of supplier switches in the high and medium-sized demand categories took place in January, when three-fifths of all the changes made in 2011 took place. The reason is the usual one-year term of supply agreements, which provide for termination as of the end of a calendar year.

More and more customers are increasingly realising, and actually using, their statutory opportunity to change their supplier.

Table 6 Customers' gas supplier switches

Type of demand	2010	2011	2011	2011
	Number of supplier switches	Number of supplier switches	Total number of supply points	Switching [%]
Large offtake	213	537	1,707	31.46
Medium-sized	674	1,142	7,033	16.24
Low offtake	6,842	26,994	200,496	13.46
Households	76,695	333,268	2,659,787	12.53
Large offtake	84,424	361,941	2,869,023	12.62

Source: ERO

Chart 8 Number of supplier switches between 2007 and 2011

Source: ERO

4.1 Network regulation

4.1.1 Unbundling of the owners of the gas transmission system

In respect of the gas industry, the transposition amendment to the Energy Act mainly focuses on the method of the TSO's unbundling and certification and the related new duties for state administration authorities.

In the gas industry, pursuant to Article 9(8) of Directive 2009/73/EC the option of an independent system operator was selected, because on 3 September 2009 the gas transmission system operator, RWE Transgas, s.r.o. (today NET4GAS, s.r.o.) belonged to a vertically integrated undertaking, a part of which was also RWE Transgas, a.s. as a gas importer and supplier.

An assessment of the viable alternative options for effective unbundling indicated that in terms of costs, interference 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 establishment of an independent transmission operator, ITO, would be the best approach. NET4GAS s.r.o. started to gradually unbundle shared activities from the rest of the business group. In this connection, representatives of the gas transmission system applied for the recognition of demonstrable unbundling costs in regulated prices. Because of the extent of the costs requested for recognition and the complexity of assessing whether or not the costs were expended reasonably, this analysis was not completed in 2011. The ERO

also made the recognition of any unbundling costs conditional on the award of the certificate of independence.

In respect of the unbundling of distribution system operators, Article 26 of Directive 2009/73/EC maintains the concept of legal and functional unbundling of distribution system operators, with some formal changes concerning the position of the person responsible for monitoring the compliance programme of the distribution system operator. Implementation of these formal modifications is the subject of Section 59a(3) and (4) of the Energy Act. The new Section 59a(5) requires the operators to prepare and submit for approval annual reports on the measures adopted for the performance of the equal-treatment programme for the past year.

Under Article 26(2)(c) of Directive 2009/73/EC, in the gas industry the distribution system operator shall have at its disposal the necessary resources including human, technical, physical and financial resources. Since such a requirement can also be applied to any system operator and other energy business entities, this provision of the Directive has been implemented through a new provision, Section 11(1)(m) of the Energy Act, which applies to all licence holders.

Directive 2009/73/EC also imposes a new obligation of the legal and functional unbundling of SSOs that are part of a vertically integrated undertaking together with a gas transmission system operator. Since the legislation on the legal and functional unbundling of SSOs under Article 15 of Directive 2009/73/EC is identical to the legislation on the legal and functional unbundling of distribution system operators under Article 26 of Directive 2009/73/EC, it matches the provisions of Sections 25a and 59a of the Energy Act. In terms of content, the unbundling of SSOs is laid down in Section 60a of the Energy Act on the unbundling of SSOs. Both unbundled and bundled SSOs currently operate on the Czech gas market, and the Energy Act therefore provides enough time to meet the unbundling requirement for all SSOs in its transitory provisions.

4.1.2 Technical functioning

The gas transmission system

The Czech gas transmission system is comprised of gas pipelines having a total length of 3,640 km, and it includes five compression stations with a total installed capacity of 297 MW that help to maintain the required pressure in the pipelines. Part of the gas transmission system is also six border transfer stations (at Lanžhot, Hora Sv. Kateřiny–Olbernhau, Hora Sv. Kateřiny–Sayda, Waidhaus, Český Těšín and Brandov) and 81 inland transfer stations delivering gas from transit pipelines to the distribution network. Gas flows from the transit pipeline to direct customers via six delivery points, while the remaining 75 delivery points deliver gas from the national network into distribution networks and other direct customers. In line with the applicable legislation, all delivery points are equipped with commercial metering.

The national pipeline system has a length of 1,180 km, while the transit network includes pipelines with a total length of 2,460 km.

The gas transmission system facilitates international gas transport across the Czech Republic through transit gas pipelines with nominal diameters ranging from DN 800 to DN 1400, while the national system, with pipelines having diameters ranging from DN 80 to DN 700, is intended for smooth and safe gas supply for the needs of the Czech Republic.

In 2011, six regional distribution companies with a total length of pipelines of 73,452 km distributed gas.

In addition to the regional distribution companies, gas was also distributed within delineated areas by local distribution system operators; the systems that they operate are connected via entry delivery points to the regional distribution systems. In the Czech Republic, 68 local distribution system operators were active at the end of 2011.

In relation to the plans to enhance the flexibility and diversification of the gas flows in the gas transmission system, several investment projects were completed in 2011. Some parts of the transmission system have also been modified to facilitate 'reverse flow' of gas from the west to the southeast of the Czech Republic in the direction of Slovakia, Hungary, Austria and southern Germany. The purpose of these adjustments was to reinforce the system's transmission capacity from the German/Czech national border to the Czech/Slovak national border, thereby ensuring a safe and flexible distribution of gas flows in Europe.

Civil work that would make it possible to connect the Počerady gas power station to the transmission system was completed in 2011. This power station is to be put into operation in 2013. Another three gas power stations are to be commissioned in 2015 and 2016. The transmission system operator has taken preparatory steps for the future connection of these capacities.

Gas storage facilities

Three companies, RWE Gas Storage, s.r.o., MND Gas Storage, a.s. and SPP Storage s.r.o., operated in the Czech storage capacity market in 2011.

RWE Gas Storage, s.r.o. owns six underground gas storage (UGS) facilities (at Háje, Tvrdonice, Lobodice, Třanovice, Štramberk and Dolní Dunajovice) with an aggregate capacity of 2,601 million m³. MND Gas Storage a.s. owns and operates the Uhřice UGS facility, the technical capacity of which was 160 million m³ in 2011. The owner and operator of the Dolní Bojanovice UGS facility, with a capacity of 576 million m³, is SPP Bohemia, a.s. This facility is not used for customers in the Czech Republic for technical reasons of connection to the Czech transmission system. It is only used for the Slovak Republic's needs under contracts.

Compared with 2010, the storage capacity was increased in the Háje UGS facility, by 7 million m³. The capacities in the other storage facilities remained unchanged. At the Třanovice UGS facility, 2011 saw the running of the EEPR project; following completion, its storage capacity will be up by 150 million m³.

Requirements for quality of service

The requirement for the quality of services and, in this respect, the standards of gas supply laid down in legislation, is currently an important attribute. Given the current market environment and the business entities' strong pressure on customers, unfair practices and/or discriminatory conduct on the part of business entities are likely to occur in this environment. Suppliers resort to such unfair practices not only by way of price hikes but also by reducing the quality of the gas they supply. The required values of the physical and chemical parameters that determine gas quality specifications are laid down in Schedule 5 to public notice no. 108/2011.

To eliminate these negative developments, on 1 January 2007 public notice no. 545/2006 on the quality of gas supply and related services in the gas industry came into force; it was amended by no. 396/2011 with effect from 1 January 2012. This statutory instrument is applicable not only to gas traders but also to distribution system operators, the gas transmission system operator, and SSOs. It lays down the minimum rules and procedures that

the regulated entities must follow with a view to the customers receiving the required reliable and safe quality for the price that they pay for gas supply.

It also lays down certain standards of the required quality of supply and services related to the regulated activities in the gas industry and the amount of compensation for non-compliance, the time limits for claiming compensation for sustained damage and for shortcomings, and it imposes on the holders of the relevant licences to keep the required parameters and to publish, by 31 March of every year, summary reports on their observance of all the standards for the preceding calendar year.

In 2011, standards were not violated by holders of licences for gas transmission, distribution or storage or major holders of gas trade licences.

4.1.3 Charges for gas transmission and distribution, storage capacity, and the market operator's services

Charges for gas transmission and distribution and the market operator's services, which are set out in an ERO price decision, are applicable throughout the term of effect of the price decision. The practice so far has been to issue a price decision every year no later than by 30 November, with the prices set out therein taking effect on 1 January of the following calendar year. Part of the pricing process is responding to the development of the Czech gas market and checking whether all components match the market conditions.

Price decisions are published in the *Energy Regulation Gazette* and are also available on the ERO's official website. The revenue cap method is employed for regulating the prices for gas transmission and distribution and the market operator's services.

The parameters for calculating the prices are based on the configuration of the specific transmission or distribution system, the required efficiency of system operators' operations, the development of the Czech economy, and the data reported by gas distribution licence holders pursuant to secondary legislation on energy. This ensures the transparency of the criteria for the regulation of charges for distribution. Parameters determining the level of the transmission/distribution charge ensure that the transmission/distribution system operator will meet the costs of system repair and maintenance in accordance with energy legislation and generate enough money for the required investments. The annually set rate of return on the regulatory asset base (RAB) also ensures reasonable support for improving the operating effectiveness and efficiency of the regulated activity. The same criteria are also applied for calculating the charges for the market operator's services. Almost 100 percent of the gas supplied to customers in the Czech Republic is imported. Gas is imported into and transported and distributed inside the country in the gaseous state.

Gas transmission

Since 1 January 2011, the ERO has been applying a single regulatory principle to each of the entry and exit points of the transmission system, while respecting the cap on the revenues allowed to the transmission system operator. Thus, all of the gas transmission agreements that have been entered into since 1 January 2011 for the various entry and exit points of the transmission system (the entry/exit model) are subject to regulation. In this respect, an important issue is the amount of the adjusted allowed revenues from gas transmission, which is set by the ERO every year. On the basis of the expected use of each of the entry and exit points of the transmission system, total adjusted allowed revenues are allocated to these entry and exit points of the transmission system, which include the border transfer stations, gas storage facilities, and the interface between the transmission and distribution system serving for supplying gas to the customer's supply point in the Czech Republic, which is referred to as

‘the domestic point’. The double-component charges are comprised of a fixed component for booked capacity and a variable component for the transported gas quantity and are based on the allocation of allowed revenues. Costs related to transmission depend on the size of the booked transmission capacity, i.e., the gas quantity that the transmission system operator agrees to transport over one day, and the gas quantity actually transported during the term of the gas transmission agreement. The fixed component of the charge reflects the above costs related to the transmission capacity booked at each of the entry and exit points and the expected values of the capacities booked for the respective calendar year. The variable component of the charge defrays the costs of the gas required for driving compression stations in the transmission system (fuel gas). These costs are calculated as the product of the planned quantity of gas energy to be transported over the respective year, the planned purchase price of the gas energy for valuing the fuel gas, and a coefficient that expresses, in percentage terms, compression stations’ consumption out of the gas actually transported at each of the exit points. Beginning in 2011, the variable part of the charge for the exit border points is calculated with the help of the above coefficient and the current price on the German exchange at which gas is traded, so that it meets the transmission system operator’s actual costs of the fuel gas required for transport through the exit border points of the transmission system on the principle of well-working market mechanisms. For customers in the Czech Republic the transmission system operator’s revenues related to gas supply are included in the charge for gas distribution. The transmission system operator’s allowed revenues for 2011 dropped by almost 13 percent. The main reason is the significant correction factor, which represents the difference between the expected and actual revenues from gas transmission in the period under review, in this case for 2009 when due to a significant increase in new gas suppliers’ gas imports the transmission system was used more than previously. The other factors include a decrease in the transmission system operator’s profit and lower costs incurred in the procurement of the services required for ensuring the system’s stability.

In setting the charges for the use of the transmission system’s entry points on the national border, the Office proceeded in line with its objective, stated earlier, of supporting gas imports into the Czech Republic, and therefore kept them at the same level as in the preceding year. The charges at the exit points to gas storage facilities also stayed at the level of 2010 for 2011. At the exit points on the national border, the fixed components of the charge slightly decreased by approximately 3 percent. The variable parts of prices are calculated, with the help of coefficients, so as to cover the transmission system operator’s fuel gas consumption at compression stations, which are needed for controlling pressure in the network and smooth supply to customers. The above decrease was therefore mainly reflected in prices of gas transport for customers in the Czech Republic.

Gas distribution

In 2011, six regional distribution companies with a total length of pipelines of 73,452 km as at 31 December 2011, distributed gas in the Czech Republic.

In addition to the regional distribution companies, gas was also distributed within delineated areas by local distribution system operators; the systems that they operate are connected via entry delivery points to the regional distribution systems. In the Czech Republic, 68 local distribution system operators were active at the end of 2011.

Regulated prices are set as fixed prices, and it is therefore not possible to increase these prices or to grant discounts. The pricing methodology is laid down in the ERO’s public notice and it is the same for all regional distribution system operators, the market operator and the transmission system operator. 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 pursuant to secondary legislation on energy. This ensures the transparency of the criteria for the regulation of distribution charges. Parameters determining the level of the distribution charge ensure that the distribution system operator will meet the costs of system repair and maintenance in accordance with energy legislation and generate enough money for the required investments. The annually set rate of return on the regulatory asset base (RAB) also ensures reasonable support for improving the operating effectiveness and efficiency of the regulated activity.

Table 7 shows average gas distribution charges for 2011 for selected customer categories using Eurostat categorisation, ranging from the least to the most expensive distribution system with 90,000 or more customers. The charges are in CZK/MWh and without VAT. Average charges contain both the fixed and the variable component. Charges also include gas transmission within the Czech Republic

Table 7 Average distribution charges in 2011

Eurostat category	Distribution charge	
	min CZK	max CZK
I1	158.43	306.23
D3	169.78	294.28

Source: ERO

In 2011, there was no need to interrupt supply in the Czech Republic due to a shortage of distribution capacity.

Gas storage facilities

Public notice no. 365/2009 on the Gas Market Rules responded to the situation on the Czech gas market, where the supply of storage capacities exceeded demand and in addition, projects for the construction of storage capacities were being prepared. The modification of the Rules has simplified and relaxed the rules for capacity booking with a view to enabling SSOs to freely offer their storage capacity to the market. SSOs can offer the market such storage capacity products which reflect the market's needs. However, the Rules maintain the duty to publish the auction conditions well in advance to give all potential bidders for storage capacity enough time to prepare for the auction.

Charges for storage capacities are not regulated and in 2011 they were again completely derived from market mechanisms on the basis of multi-round online auctions. In 2011, SSOs called 12 auctions for the sale of storage capacity for subsequent storage years. The influence of extremely low gas prices on spot markets in Germany throughout the year was reflected, and positively from the gas traders' perspective, in the much lower reserve price and the results of these auctions. RWE Gas Storage, s.r.o. called four auctions for annual storage capacity booking, one auction for free storage capacity for monthly agreements. The purpose of the last auction was to sell a new storage capacity of 50 million m³. This auction ended with the result CZK 1.10/m³ per storage volume unit. In 2011, MND Gas Storage, a.s. called two auctions for new storage capacity booking, offering storage capacities of 10 million m³ and 3.5 million m³. The auction called for the 10 million m³ free storage capacity was intended for a monthly agreement. Four auctions were called for storage capacity booking for annual agreements.

Forecasts of further development need to take into account the developments on spot markets, where the unusually low prices can probably be expected to come to an end and traders will therefore be compelled to use more the traditional method of security, i.e., gas storage, for providing flexibility. A new factor which can be expected to influence the prices of storage capacities is the introduction of the duty to adopt measures to ensure supply to protected customers, known as 'the security standard' (Energy Act, Section 73a), under which traders shall keep the security standard of supply between 30 September and 1 April. On the other hand, the expected tendency towards rising prices for storage capacity booking will be countered by SSOs' projects for the expansion of the existing and preparation of new storage capacities.

4.1.4 Cross-border issues

Central, Eastern and in part Western Europe is supplied with gas mainly from Russia and Norway; facilitating new flows and reverse flows in the transmission system, and building new gas storage capacities in the Czech Republic, is therefore desirable from the perspective of transport route diversification.

The Czech-Polish interconnector, the STORK gas pipeline, is a joint project of the Polish pipeline operator GAZ-SYSTEM S.A. and the Czech gas transmission system operator NET4GAS, s.r.o.

The new interconnector (approximately 10 km of pipeline on the Czech side, and 22 km of pipeline and a border transfer station on the Polish side) facilitates gas transport, so far non-existent, between the Czech Republic and Poland, thereby enhancing energy market integration in this region. The operation of this interconnector has also helped to reinforce transmission capacity in the cross-border areas and improve security of supply. The project contributes to the required increase in transport capacity, but it also has a strategic importance in terms of energy security and diversification of energy sources.

In view of the key role that the Czech-Polish interconnector can play in the process of gas market integration and liberalisation in this part of Europe, the two parties are planning further development of this interconnection. The companies expect that at the next stage, they will take steps that will make it possible to optimise the transport capacity of the completed pipeline by reinforcing its capacity to about 2.5 bcm/year and by provisions for gas flow in both directions.

On the Czech and Polish sides the project was co-financed under the European Commission's European Economic Programme for Recovery (EEPR). The entire system of gas pipelines, including the transfer station, is being developed as a single technological system with the option of reverse flow. The Polish part of the project has received a subsidy of EUR 10.5 million, while the Czech side received EUR 3.5 million, which accounts for 50 percent of the planned costs.

For this gas pipeline, capacity was allocated in an Open Season process; all of the long-term capacity on offer was booked, and at the same time 10 percent of total capacity was left available for short-term contracts.

The Gazelle gas pipeline was also a major investment project in 2011. In order to enable this investment, in 2010 NET4GAS, s.r.o. applied for an exemption from the obligation of allowing third party access for regulated prices subject to the conditions laid down by the Energy Act and for an exemption from the ownerships unbundling of the gas transmission system operator within the meaning of Article 9 of Directive 2009/73/ES.

Under the ERO's decision of 28 July 2011, the interconnecting "Brandov Border Transit Station – Rozvadov DN 1400 High-pressure Gas Pipeline" (Gazelle) was exempted from the obligation to allow third party access for regulated prices subject to the conditions laid down by the Energy Act. The granted exemption applies subject to the conditions set out in the above decision. A favourable decision concerning ownership unbundling was issued on 2 August 2011.

The two decisions have been upheld by the European Commission (Commission Decision of 1 December 2011).

This pipeline will connect the Czech Republic to Russian gas transported to Europe via the Northern Route. In late 2011, the Brandov border transfer station was put into operation; at this station Gazelle will connect to the German OPAL pipeline. The whole Gazelle, having a length of 166 km, is expected to be put into operation in late 2012. Its completion will enhance the flexibility of the currently existing system. The gas pipeline is being built subject to the conditions set out in the exemptions granted to this pipeline.

Monitoring investment plans and assessment of consistency with Community-wide network development plan

NET4GAS, s.r.o. submitted, in accordance with the requirements of the Energy Act, its ten-year development plan to the ERO by the required date. The ERO posted the plan on its website and invited market participants to provide comments. The ERO also evaluated the compatibility of the national ten-year plan with the Community-wide network development plan.

The ten-year plan for the development of the gas transmission system in the Czech Republic which was submitted in 2011 analyses the development of gas demand and the adequacy of the entry/exit capacity of the domestic zone in the Czech Republic for 2012-2021. The TSO based the preparation of this plan on historical and predictable gas supply and demand.

On the basis of the data and contexts contained in the document, full 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 consumption in the Czech Republic for the ten-year period covered by the plan.

4.1.5 Compliance

The transposition amendment to the Energy Act has harmonised the Czech Republic's national legislation with the legislation of the EU's third package; in the case of the gas industry, Directive 2009/73/EC, Regulation No 715/2009 and Regulation No 713/2009.

In 2011, the ERO promulgated some new implementing legal regulations, or amendments to earlier implementing regulations, necessitated by the experience with their application on the liberalised energy markets and also by the passing of the transposition amendment, which substantively amended the Energy Act. They included: a new public notice no. 210/2011 on the scope, essentials and dates of the billing of electricity, gas and thermal energy supply and related services, and no. 62/2011 on the conditions of connection to the gas system and on changes to Ministry of Industry and Trade public notice no. 251/2001, which lays down the Operating Rules for the Gas Transmission and Distribution Systems.

Further, in 2011 the ERO amended the following implementing regulations: public notice no. 392/2011, amending no. 426/2005 on the details of licensing for business in energy industries, as amended; public notice no. 393/2011, amending no. 140/2009, on regulatory methods in the energy industries and procedures for price control, as amended by no. 264/2010; public

notice no. 396/2011, amending no. 545/2006 on the quality of gas supplies and related services in the gas industry; public notice no. 442/2011, amending no. 365/2009 on Gas Market Rules, as amended by no. 370/2010. In that same year the ERO also drafted a new public notice on regulatory reporting and a public notice on the required particulars of applications for the approval of the appointment, election and other installation in office and dismissal of the bodies of the independent gas transmission system operator.

The ERO exercised its power to request any information from undertakings in the gas industry several times in various contexts, in particular for the purpose of initiating *ex post* checks of compliance with the Energy Act and/or the law on consumer protection, or the law on prices; see Section 15a of the Energy Act.

The ERO supervises the performance of the obligations imposed by the Energy Act on licence holders in general; for this purpose, in 2011 it carried out a number of inspections, despite the fact that the inspection competences were only transferred to the ERO as of 18 August 2011.

4.1.6 Dispute settlement

The ERO did not adjudicate any dispute falling under Article 41(11) and Article 41(4)(e) of Directive 2009/73/EC in the gas industry in 2011.

4.2 Promoting competition

4.2.1 Wholesale markets

4.2.1.1 Price monitoring

In 2011, gas was imported into the Czech Republic from Russia, Norway, and the EU; these imports met more than 98 percent of demand. The remaining less than 2 percent were supplied from indigenous resources, which included drained gas (from surface layers) and indigenous gas production.

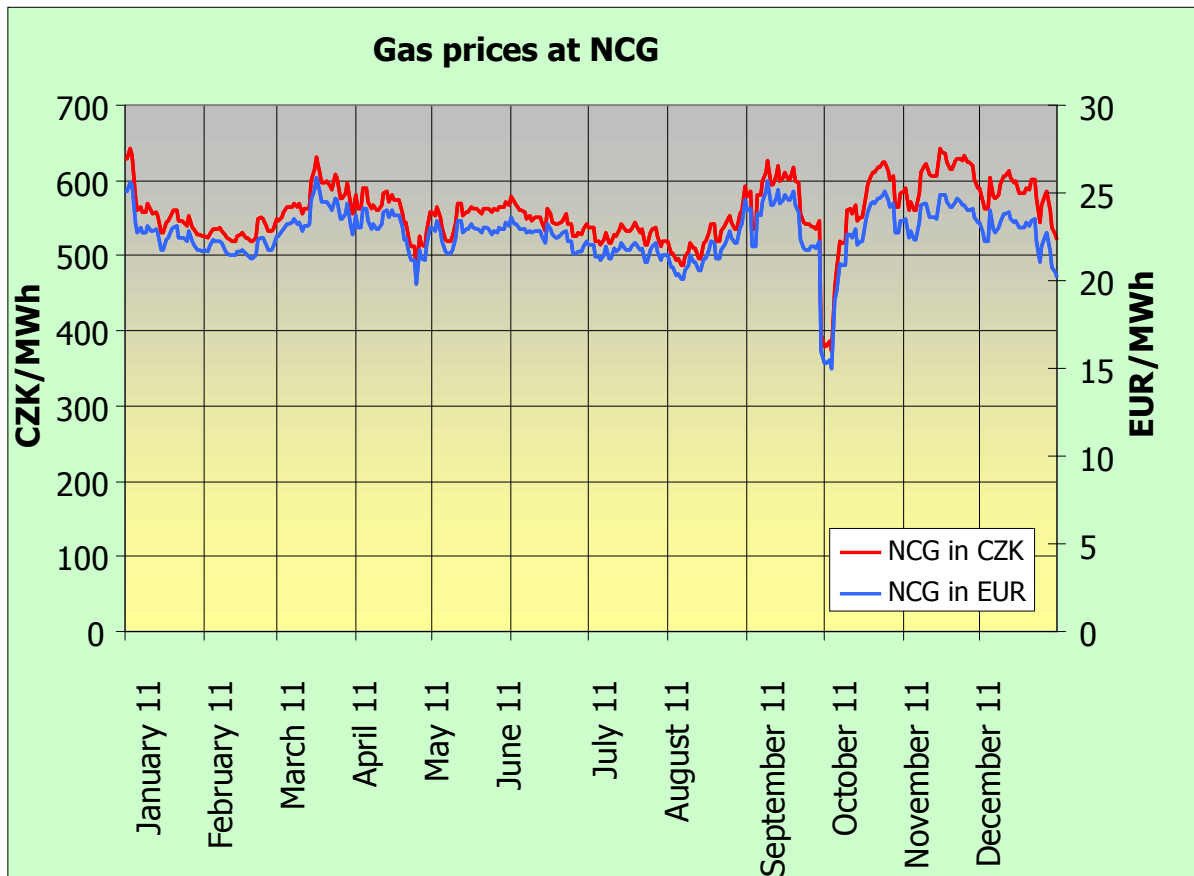
Traders can procure gas imported into the Czech Republic in two ways for their customers. One is entering into a long-term contract directly with gas exporters in Russia or Norway. The other option is to buy gas at an energy exchange in Europe. While purchase prices on spot markets depend primarily on market mechanisms, supply and demand, for long-term contracts the decisive factor is the prices of competing fuels, first of all gas oil, fuel oil and coal.

Each of these pricing approaches has its pros and cons and responds to different economic factors.

Compared with the NCG energy exchange in Leipzig, which is relevant for the Central European region, the purchase price under long-term contracts was more than 30 percent higher on average in 2011. The main reason for this difference was the rising prices of oil and, in turn, oil products. This difference caused a disadvantage for dominant gas suppliers who have in place long-term contracts and were compelled to offer gas to customers for a higher price than alternative suppliers who bought gas on spot markets.

Gas prices on spot markets did not register any dramatic developments, with the only fluctuation occurring in October due to the increased gas quantity offered on spot markets, and grew only slightly over the whole year, specifically in the last quarter. The price per MWh of gas ranged between EUR 20 and 25.

Chart 9 Gas purchase prices at NCG in 2011



Source: NCG

Spot markets in continental Europe developed very differently from the global trend. Globally, gas prices decreased in 2011, thereby following up the continuous price decline observed in previous years. This decline is attributable to the opening of new gas fields, mainly in North America and to available and tradable gas quantities increasing on the energy markets there. However, the Central European gas market responds to these impetuses very little because it is not physically connected with North America.

4.2.1.2 Monitoring the level of transparency, including compliance with transparency obligations, and the level and effectiveness of market opening and competition

In this respect, the ERO did not report any activity in 2011.

4.2.2 Retail markets

As regards gas traders’ market position, this market is fully liberalised in the Czech Republic at both the wholesale and retail levels. Gas traders are therefore not legally constrained at all in buying gas directly from producers or at exchanges or on spot markets in the Czech Republic and in other countries. At the same time they have the right to sell gas to market participants in other countries. The scope of the stored data on the performance of agreements on the supply of gas, or derivatives thereof, has been laid down by the ERO in an implementing regulation.

Furthermore, unlike electricity traders gas traders have the duty to keep the security standard for the required gas supply, i.e., ensure safe and reliable gas supply during gas supply disruptions for 8 weeks at a level of 20 percent for customers whose annual consumption is less than 400,000 cubic metres.

Traders must provide distribution system operators with identification details of the customers whom they supply with gas under agreements on bundled supply services. Traders must also provide gas transmission and distribution system operators with information required for the safe and reliable operation and development of these systems. Gas traders' obligation is to promote energy services and offers thereof. Gas traders have the right to receive from the market operator, the information that they need for billing their gas supply to customers whose supply point is registered with OTE, a.s.

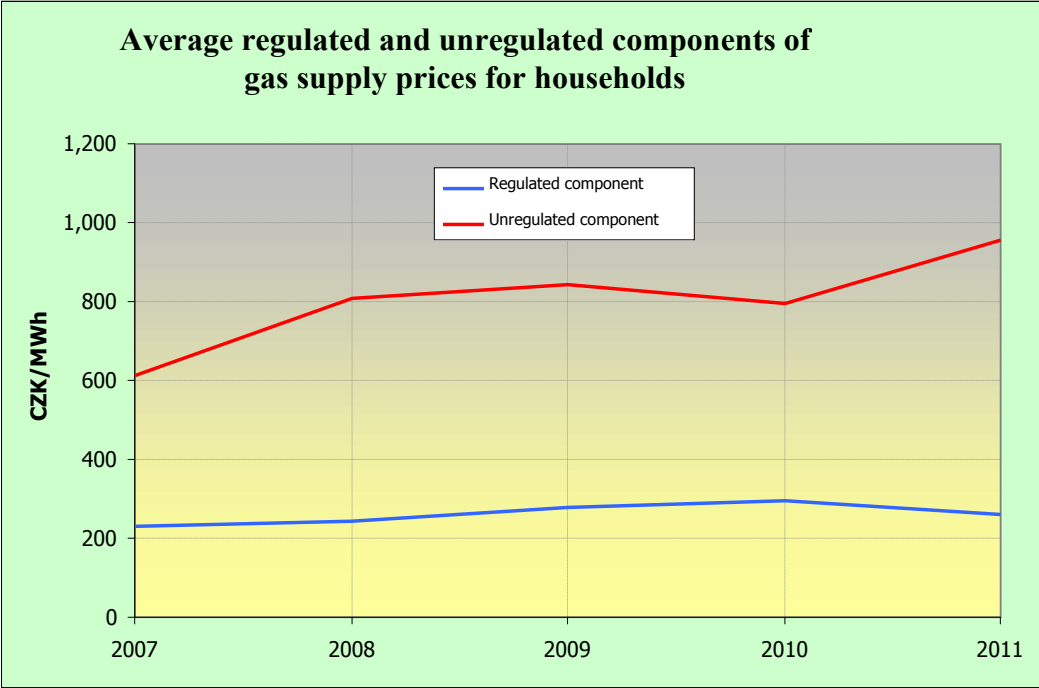
In relation to customer protection, the transposition amendment has enhanced customers' position through the provisions of Section 11a of the Energy Act, which now requires gas production and gas trading licence holders to publish, in a manner allowing remote access, their terms and conditions of gas supply and gas supply prices for households and natural persons who carry on a business with an annual gas consumption of up to 630 MWh. Licence holders shall also publish any changes to gas supply prices or changes to other conditions of gas supply no later than 30 days before the day of effect of such changes.

As regards implementing (secondary) legislation, in 2011 the ERO promulgated a public notice on the scope, particulars and dates of electricity, gas and heat supply billing and related services.

4.2.2.1 Price monitoring

Compared with previous years, the development of gas prices for final customers was quite unusual. Some energy suppliers responded to the unexpected increase in the gas procurement costs by diverging from their customary changes of prices lists on a quarterly basis. During 2011, some of the gas traders therefore updated their price lists several times and on different dates. In the first half of 2011 gas prices for final customers were constant. The second half of the year progressively saw several price hikes caused by the unfavourable development of the CZK/USD rate, growing prices of competing fuels, and the gas quantities offered on spot markets.

Chart 10 Average regulated and unregulated components of gas supply prices for households



Source: ERO

The total price for gas supply for final customers is comprised of regulated and unregulated items. In 2011, regulated items accounted for approximately one-fifth of the total gas supply price, and decreased by about 2 percent over the preceding year.

The remaining four-fifths of the gas supply price comprise unregulated items, which include the charge for commodity and trade and the charge for flexibility, i.e., the balancing of imbalances in gas consumption during the course of a year. This part of the price is determined by the gas traders themselves in the well-developed competitive environment on the gas market.

The Czech Statistical Office's following table shows the development of prices for various Eurostat customer categories. The table also clearly indicates the differences in the prices for these consumer groups. Households and small business customers (categories D3 and I1) buy gas and related services for public prices set out in traders' price lists for a certain period of time. On the other hand, medium-sized and large gas customers usually have a price individually determined for them using price formulae that change every month during a year.

In all customer categories, gas prices increased due to the rising prices of oil products and the development, unfavourable for imports, of the USD/CZK rate in late 2011.

Table 8 Prices of gas supply to customers by Eurostat categories as at the first day of a quarter in the Czech Republic in 2011, in CZK/MWh

Period	Standard consumer, Eurostat					
	D3		I1		I4	
	w/o VAT	with VAT	w/o VAT	with VAT	w/o VAT	with VAT
First quarter of 2011	1,033.13	1,239.76	1,025.75	1,230.90	672.68	807.22
Second quarter of 2011	1,053.14	1,263.77	1,083.42	1,300.10	696.68	836.02
Third quarter of 2011	1,133.31	1,359.97	1,156.19	1,387.43	759.31	911.17
Fourth quarter of 2011	1,204.10	1,444.92	1,209.27	1,451.12	806.67	968.00

Source: Czech Statistical Office

4.2.2.2 Monitoring the level of transparency, including compliance with transparency obligations, and the level and effectiveness of market opening and competition

In this respect, the ERO did not report any activity in 2011.

4.2.3 Recommendations on supply prices

All gas customers in the Czech Republic have the right to change their supplier. In this process, they are only limited by applicable legal regulations and obligations under contracts with their existing suppliers. Suppliers' quotations for the various customer categories and offtake bands differ, and a good selection of the supplier can therefore help to achieve significant savings related to gas supply.

Customers are not in a position to change their gas distributor who operates the gas distribution system in the delineated area. For household and small business customer categories, bands of consumption (demand) are defined, and the fixed and variable components of the regulated gas distribution charge differ for each of the bands. Customers are automatically categorised on the basis of their consumption, and inclusion in an offtake band therefore cannot be influenced.

For all customers, the regulated charge for the market operator's services is also fixed. This item is related to the gas quantity consumed.

In some of the offtake bands, the unregulated part of the price accounts for almost 80 percent of the overall price for gas supply. Customers can therefore influence a significant portion of their annual gas bills.

Under Article 41(1)(p) of Directive 2009/73/EC, the ERO publishes, in accordance with Section 17(7)(l) of the Energy Act, recommendations in relation to gas supply prices for households.

4.2.4 Carrying out investigations and imposing measures to promote effective competition

The transposition amendment to the Energy Act lays down that the ERO shall inform ÚOHS of market participants' practices which there exist good reasons to regard as distorting or restricting competition, or as resulting in such distortion or restriction, of the use of constraining or unreasonable terms and conditions in contracts on the gas market, and of the methods of gas pricing for households.

In 2011, the ERO did not conduct any investigations within the meaning of the respective requirements of the above Articles of Directive 2009/73/EC.

4.3 Consumer protection

Among other things, Act No 211/2011 supports the position of consumers, or customers, in the energy industries, broadens their rights, and reinforces their protection in accordance with Annex 1 to Directive 2009/73/EC, primarily through Section 11a of the Energy Act, which transposes the provisions of Article 3 of Directive 2009/73/EC and Annex I thereto into the national law.

Under Section 11a of the Energy Act, it applies, *inter alia*, that traders shall publish, in a manner allowing remote access, their terms and conditions and gas supply prices for households and natural persons who carry on a business, no later than 30 days before the day of effect of any change to these prices or other terms and conditions. Section 11a of the Energy Act also establishes customers' right to withdraw from the contract free of charge in the case of their disagreement with a change to the contract terms and conditions, or a price hike, and sets out the time limits for exercising the right to withdrawal from the contract and the effect of such withdrawal. The law also contains provisions on the customers' right to select the method of payments for gas supplies, and stipulates that the system of advance payments shall be fair and reasonable.

In its valid and effective wording, the Energy Act does not define 'vulnerable customer'; as regards customers who can be regarded as 'socially disadvantaged', certain measures for their protection or support are provided for at the level of generally applicable legal regulations in the domain of social security law.

Further, under Section 17(7)(l) and (q) of the Energy Act, the ERO shall publish recommendations on gas pricing for households and shall cooperate with civic associations and other juristic persons established for the purpose of protecting consumer rights in the energy sector.

Under Section 17(7)(e) of the Energy Act, the ERO 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 licence holder has come into existence, continues to exist, or has ceased to exist, and also disputes

over compensation for failure to keep the set standards of quality and services in the gas industry.

Under Section 17(7)(f) of the Energy Act the ERO is also competent to perform inspections in the energy industries and to perform 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).

In connection with the extension of the statutory provisions related to consumer protection, the ERO has set up a Consumer Protection Unit tasked with receiving and addressing submissions, questions, suggestions and complaints from customers.