
CEER comments on the Proposal for a Directive concerning measures to safeguard security of electricity supply and infrastructure investment

Introduction

1. The CEER fully supports the principle that security of supply, underpinned by appropriate investment in infrastructure, is a key objective for the successful operation of the internal market. Consumers' interests will be best served where electricity supplies are secure and reliable. The completion of the internal market will be facilitated by appropriate investment in interconnectors. Therefore the CEER supports the broad aims of the December 2003 Commission Proposal concerning measures to safeguard security of electricity supply and infrastructure development.
2. However, the CEER has a number of comments and proposals regarding the approach and potential effect of the Proposal. These particularly concern the development of interconnector infrastructures.

Basis of Proposal

3. The Proposal is based on a number of premises:
 - further interconnection between Member States is required to deliver effective competition;
 - investment in networks and/or interconnectors is required to accommodate the advent of new generation technologies such as renewable generation and CHP;
 - electricity demand is growing and this coincides with the expected closure of existing plant; and
 - a stable, consistent and adequate regulatory framework which allows for a reasonable return is needed to provide investors (e.g. TSOs) with a stable environment for long term investment.

Some of these basic premises are broad. The aims of the Directive would be more easily understood if it were to concentrate on the key issues. This focus could be a subject of discussion involving Commission, CEER and stakeholders.

Context

4. A basic framework for the establishment of a competitive single electricity market has now been set out in Directive 2003/54/EC and Regulation 1228/2003, including regulated Third Party Access to networks, the establishment of independent regulatory authorities, and market opening. The Directive also includes an explicit obligation on Member States to ensure the possibility, in the interests of security of supply, to provide for new generation capacity through a tendering procedure or other equivalent procedure. The Regulation establishes some binding rules regarding the construction, the operation and the use of revenues of interconnections and specifies the conditions under which new interconnectors can be exempted from these rules.
5. In this framework, once it is transposed into the national law of each Member State, a stable regulatory environment shall be established for all market participants. Such an environment should facilitate investment decisions at all levels of the market, which will be important contributors to the long term development of the market. Any new items of legislation should be carefully appraised to ensure that they increase certainty and confidence in the regulatory environment.
6. Although a basic framework has now been set, it is clear that effective competition has not yet been established across the EU. The potential for competition can be enhanced in a number of ways:
 - through effective separation of network from competitive activities (required by the Directive but not yet achieved in all Member States);
 - through the implementation of appropriate market designs;
 - through a minimization of barriers to market entry and by addressing market structure issues;
 - and, through appropriate and efficient development of further interconnections between Member States which can be particularly relevant for systems with few market players.

The CEER would wish to stress however that, taking the EU as a whole, increased interconnection can only deliver effective competition if accompanied by both market design and market structure reforms.

7. Regarding security of supply, this will be given where there is sufficient generation delivered over reliable and secure transmission and distribution networks. The CEER believes that, where markets have been liberalized, such security of supply can be achieved within properly designed and regulated network activities and competitive markets. In liberalised markets these are the primary mechanism for ensuring the balance between demand and supply. These mechanisms can also accommodate contributions from demand side measures and renewable generation technologies in a non-discriminatory and market based manner.
8. Security of supply at all levels of the supply chain will also be enhanced where the roles and responsibilities of all stakeholders and market participants are defined clearly and transparently.
9. Regarding networks, as the Commission notes, generation capacity is beginning to include more renewable and CHP production sources. These developments may pose new challenges to network operators regarding for example investment. However, if networks are

to be developed in an efficient manner, network pricing must reflect the costs of network investment associated with any generation expansion and siting, regardless of generation technology.

10. Network security as a whole will be facilitated where operational and technical standards for power systems are established by TSOs and enforced by Regulators, and where roles and responsibilities of regulators, government, TSOs and DSOs are made clear. The CEER therefore agrees with the Commission that there is merit in rationalising and co-ordinating some network security and reliability standards across the EU.
11. The CEER believes that any further proposals for security of supply and infrastructure investment, including the present Proposal, must be coherent and consistent with this basic approach to market liberalisation, the established supporting legislative framework, and the basic aim of introducing efficient and effectively competitive markets.

Article 6 : Network investment

CEER comments on Commission Proposal

12. The measures proposed in Article 6 add little to the scope of requirements on Member States and powers for regulators already given in the Directive. The call for investment decisions to be taken such that increased demand side management measures are prioritised is at odds with the aspiration to create efficient and effectively competitive generation markets, where the generation mix (including any contribution from the demand side) will be market determined.
13. The CEER's view is that this Article, if implemented, would at best repeat elements already in the Directive, and at worst, increase uncertainty surrounding the aims of TSOs and regulators, and the promotion of non-discriminatory provision of network access, investment, and generation markets.

Article 7 : Investment in cross border interconnector infrastructure

CEER comments on Commission Proposal: Article 7

14. The CEER notes the Commission's approach set out in paragraph 7(1) of the proposed Directive, which places on the TSOs a duty to assess an adequate level of cross-border interconnection. However, this assessment should:
 - take into account the possibility of merchant interconnectors, provided they are subject to a regulatory framework dealing notably with their possible external effects,
 - evaluate if and how to encourage the provision of new cross border transmission infrastructure in ways that meet all requirements of a market comprising many upstream and downstream agents independent of TSOs, and,
 - clarify the concept of 'adequate' as it is imprecise and should, if it remains, be linked to the economic viability of any proposed interconnection.
15. The prescriptions in paragraph 7(2) of the need to promote certain technologies are inconsistent with the need to be non-discriminatory. The need to promote renewable

generation for example is not a grid issue but an environmental and political issue that cannot be handled by the TSO. In addition the TSO might not have the required information about planned generation, distribution and supply.

16. The CEER sees a role for concerned regulators acting together in overseeing investments that span TSO borders. Such co-ordination can take into account the reality that actions by TSOs and market actors in one market or Member State can induce costs and benefits in neighbouring markets or Member States, and that planning and operational standards either side of an interconnector need to be sufficiently coherent. Given that these effects are usually specific to the local situation, and the need to allow TSOs to develop their own investment plans in response to local needs, it appears that there is no need for a statutory consultation between regulatory authorities and the Commission on planned investments, as anticipated by paragraph 7(3). Given this, the provisions of paragraph 7(4) are not required.
17. The CEER believes that:
 - given the present regulatory conditions and level of implementation of the Internal Electricity Market, the TSOs should be responsible to pursue cross-border investments as they have to do for internal investments after they have considered the available market signals and the inputs and requests from the market agents;
 - merchant cross-border lines are also possible subject to the Electricity Regulation;
 - investments shall be overseen by regulators acting locally and where appropriate together, willing to sanction appropriate remuneration;
 - grid investments, if they are to be efficient, must be made on a non-discriminatory basis and without emphasising one generation technology over any other;
 - such investment can already be delivered within the existing national competences of regulators, in those Member States where regulatory authorities have been established; and
 - Article 7 of the Proposal has the potential to increase regulatory uncertainty rather than diminish it, because for example it introduces new criteria which the TSOs are to take account of in making new investments, and uncertainties through the role of the Commission.

CEER detailed view

18. The CEER discusses in its May 2004 Position Paper "*Regulatory control and financial reward for electricity cross-border transmission infrastructure*", what immediate steps might be taken to encourage efficient interconnector investment. The CEER noted that one current major obstacle to such investment is the uncertainty of investors obtaining an adequate remuneration.
19. The CEER therefore issued two sets of Guidelines which provide regulatory authorities with an immediate and pragmatic toolkit with which to promote such infrastructures.
20. Broadly speaking, the first set of Guidelines envisages that the initiative to pursue new cross-border investments will mostly remain the responsibility of the TSOs, after they have considered the available market signals and the inputs and requests from the market agents, since the TSOs have the technical knowledge, as well as the expertise, to evaluate cross-

border transmission investments. Indeed the accuracy and the limitations of the methods for evaluation of these investments are quite similar to those used for purely national transmission investments. Such proposals are then subject to the normal regulatory and legal oversight, by relevant authorities acting together to reach a common position on an appropriate remuneration scheme. The CEER anticipates being informed about any new cross border regulated investments by the corresponding national regulatory authorities and may have a consultative role regarding these new investments. The CEER would offer to mediate in the case of disagreement between regulators regarding proposed new facilities if the parties felt it would be helpful.

21. Remuneration for regulated assets approved by regulators can be based on regulated transmission revenues. Hence remuneration should be based on returns consistent with other similar risk investments. The CEER suggests the use of public tender as an adequate means to allocate competitively the construction of new regulated lines and to allow the determination of the regulated asset value. The major advantage of the proposed approach is to provide the means of minimizing the risk for the investors in these cross-border facilities and to facilitate the determination of the network cost to be taken into account in the calculation of the inter-TSO compensation.
22. Alternatively, according to the second set of Guidelines, private parties can also contribute to the enhancement of interconnections. Remuneration for 'Merchant lines' will come from user revenues, and in principle the level of such remuneration will be unregulated.
23. The CEER notes that an important barrier to cross border electricity transmission infrastructure development comprises the delays and diverse difficulties in obtaining construction and operation authorizations for such development. Attention could be paid to this issue.
24. In addition, the CEER suggests that in order for investors to make rational economic decisions about investments in new cross-border transmission facilities, they should have access to information on the drivers for the market and how these evolve. This information should include e.g. data on electricity prices, network topology, and usage of the cross-border transmission facilities.
25. Finally, the CEER proposes, in its May 2004 Position Paper "Regulatory control and financial reward for electricity cross-border transmission infrastructure", to analyse in detail the opportunity of the introduction of a more comprehensive investment framework, with a key focus on assessing the ability of signals emerging from trade to highlight the need for new investment.

Article 5: Maintaining the balance between Demand and Supply

26. Concerning the Proposal content about generation adequacy the CEER has the following view:
27. The development of deep and liquid organised energy markets should provide the primary mechanism to enable and produce the necessary short term production responses from generators. Under appropriate regulatory supervision, the establishment of balancing markets will provide strong incentives for markets to match demand with supply in the short term, as well as co-ordination of TSOs and appropriate pricing such as locational pricing.

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28. Small isolated systems where the introduction of wholesale electricity markets may not be feasible require specific solutions (e.g. Cyprus and Malta).
 29. Efficient investment in new generation capacity will be facilitated where price data is also supplemented by the full transparent and non-discriminatory availability of information concerning wholesale market characteristics and network developments since investors need to take this information into account in their decision-making process. Price signals alone cannot be used for deciding investment in transmission grids and/or power plants. Indeed, forward investment decisions concerning transmission and/or generation capacity shall also include consideration of demand and supply forecasts, interconnection projects, assessment of risks for various fuels. Demand side response shall also be properly incorporated. Inappropriate intervention in the market to achieve generation adequacy might well have the effect of reducing the willingness of market parties to invest if they know that 'adequate' capacity will always be procured through non-market methods.
 30. These elements also need to be provided in a clear framework of roles and responsibilities of all stakeholders, including governments, regulators, TSOs and investors. Any limits of the signals delivered by the market designs applied must be carefully assessed. It is important also that security of supply issues are continuously monitored and assessed.

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