

**E U R O P E A N   E C O N O M I C   A R E A**  
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**O F   T H E   E F T A   S T A T E S**

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**WORKING GROUP ON ENERGY MATTERS**

**EFTA COMMENTS ON  
THE COMMISSION PROPOSAL FOR A DIRECTIVE AMENDING DIRECTIVES  
96/92/EC AND 98/30/EC AND THE COMMISSION PROPOSAL FOR A  
REGULATION ON CONDITIONS FOR ACCESS TO THE NETWORK FOR CROSS-  
BORDER EXCHANGES IN ELECTRICITY (COM(2001) 125 FINAL)**

**EXECUTIVE SUMMARY**

It is the opinion of the EEA EFTA States that the draft amendments to the two energy market Directives and the draft Regulation on cross-border exchanges in electricity constitute important measures for developing the internal energy markets further. The EEA EFTA States would like to underline the following important issues:

- A national regulatory authority is important for the further development of the electricity market, and should have an active ex-ante function. The EEA EFTA States find that a general requirement of advance approval of the tariffs by the national regulatory authority may be unsuitable for the purpose and difficult to comply with. A system of advance approval should therefore be up to each State's regulation. Furthermore, the EEA EFTA States emphasise the importance of creating tariffs that provide efficient locational signals to both generators and consumers.
- The EEA EFTA States accept that a mechanism for the compensation of costs for countries that are hosting transit flows is necessary in order to establish a real integrated internal electricity market. Such a mechanism is, however, strictly speaking, no prerequisite for establishing an efficient market. The EEA EFTA States will underline that the mechanism must not lead to export, or import charges, i.e., cross-border charges. The mechanism must not interfere with the market.
- The EEA EFTA States take note of the proposal to establish a regulatory and an advisory committee. There is, however, still a need to clarify the competence of these committees and how they will impact on the roles of the Commission and individual governments in decisions under the scope of the regulation. The EEA EFTA States wish to participate in the proposed committees, according to the general rules of the EEA Agreement (reference is made to Articles 99-101 EEA).

## **1 INTRODUCTION**

1. The EEA EFTA States support the overall direction of the Commission proposal of 13 March 2001 to amend the electricity and gas market directives (96/92/EC and 98/30/EC) and the regulation on conditions for access to the network for cross-border exchanges in electricity. The proposals constitute important measures for further developing the internal market for electricity and gas.

2. The EEA EFTA States have taken note of the main amendments made in directives 96/92 and 98/30. The amendments represent important steps forward in the work to further harmonise the EU/EEA rules in the internal market for electricity and gas. The EEA EFTA States have some preliminary comments on the different parts of the new energy market package drawn up by the Commission. Since the whole “energy market package” is currently being negotiated in the EU Council, we strongly underline that positions could change due to developments in these negotiations.

## **2 COMMENTS ON THE PROPOSAL FOR A DIRECTIVE AMENDING DIRECTIVE 98/30/EC**

3. The EEA EFTA States note that the intention of the proposal is to ensure the completion of the internal gas market through further measures, such as forced market opening, stricter rules for access to transmission and distribution pipelines, and further rules on legal unbundling. We also note that there are no direct proposals for amendments to Article 23 of the directive on upstream pipelines. However, the Commission states that it will closely monitor the situation on the upstream sector to see whether further measures are also needed in that respect.

4. The EEA EFTA States have very marginal downstream gas sectors at present. Norway and Liechtenstein are in the preliminary stages of developing a legal framework for this sector. The amendments proposed by the Commission will be considered for inclusion in such legal framework in due time. Consequently, the EEA EFTA States will follow closely the process that is now going on between the Commission and the Member States on further developing the proposal.

## **3 COMMENTS ON THE ARTICLES IN THE PROPOSAL FOR A DIRECTIVE AMENDING DIRECTIVE 96/92/EC**

### **3.1 Article 7, paragraph 6**

5. Independence of the transmission system operator is important. Requirements to ensure common minimum standards of unbundling are necessary to achieve a fully functional internal market. The proposals in Article 7 in particular, but also in Article 10, regarding such standards are therefore very important.

### **3.2 Article 10, paragraph 4**

6. Article 7, paragraph 6 demands that the transmission system operator should be independent. Article 10, paragraph 4 makes a corresponding demand for distribution system

operators. A problem interpreting these articles is how the terms "distribution system operator" and "transmission system operator" should be understood.

7. The term "transmission system operator" is generally used for the company that is responsible for operating the transmission system in a country, or a defined area. It should be made clear that these are the only companies covered by Article 7. The term "distribution system operator" is not so well known and should also be given a clear definition.

### **3.3 Article 16**

8. According to the proposal in Article 16, tariffs must be approved prior to their entry into force by a national regulatory authority. The EEA EFTA States find a general requirement for advance approval in principle unsuitable and difficult to go along with. As an illustration, there are approximately 200 network companies in Norway, each one having several different tariffs. An advance approval would thus be a very demanding task for the regulator. The regulators should be able to decide on whether to implement a system of advance approval or not.

9. The Commission emphasises that the regulatory authority should have an active ex-ante function. The EEA EFTA States support this view. The EEA EFTA States are of the opinion that this can be carried out by establishing an efficient regulation, and not only through advance approval.

10. As an illustration, the tariffs in Norway are regulated through regulations laid down in advance by the regulatory authority. The network companies are responsible for designing the tariffs within the regulations. The customers may complain about the tariffs to the regulatory authority and the regulatory authority decisions may be appealed to the Ministry of Petroleum and Energy. Past experience of this system is positive.

11. Furthermore, the term "third party access" should be replaced by "access to the market". It is not only third parties that should be given access to the transmission and distribution system. There should be open access for all parties under equal conditions and discrimination between grid customers should not be permitted.

12. The proposed Article 16 (2), which is equal to Article 17 (5) in the existing directive, states that the operator of the transmission, or distribution system, may be refused access to the system where he lacks the necessary capacity. Duly substantiated reasons must be given for such refusals, in particular with regard to Article 3.

13. The EEA EFTA States refer to the Norwegian Amendment to the Energy Act of 2000 (Ot.prp.nr. 56 (2000-01)) that will become operative on 1 January 2002. According to the Energy Act, the grid owners are obliged to give all customers access to network services and offer non-discriminating and objective point tariffs and conditions. Equivalent provisions have also earlier been set down in more detailed regulations.

14. Pursuant to the regulations, the system operator has the right to set the necessary physical transmission limits as required by relevant system operation criteria. These limits are set and made public to the market in advance and mean that all capacity not reserved due to relevant system criteria is made available to the market for trade.

15. The regulation secures that all network capacity will be available and can be utilised by the market, thus facilitating an efficient market.



### **3.4 Article 22**

16. To achieve a fully functional internal market, the proposal that all Member States shall establish an independent national regulatory authority is a suitable contribution. Norway has had good experience over a long time with a regulatory authority (Norwegian Water Resources and Energy Directorate), which is wholly independent of interests of the electricity industry. Active regulation is important for the development of a complicated market such as the electricity market.

17. Article 22 par.1 lit. b) should be expanded by also adding cross-border distribution and not only cross-border transmission.

### **3.5 Annex to article 3, letter d**

18. The composition of the fuel mix used to generate electricity, the relative cost of different fuels used to generate a unit of electricity, and the relative importance of each energy source with respect to the production of greenhouse gases should be deleted from the requirements that suppliers shall specify on the invoice. This is an extremely demanding regulation to comply with.

19. In a liberalised and international market where electricity is traded on a marketplace and customers are free to choose their electricity supplier, such a requirement is not a suitable instrument. For example, all electricity traded at a spot-market has to be specified. The physical flow of electricity follows physical laws, not contractual obligations. Such a regulation would also require extensive control from the authorities and regulation. Green electricity should be encouraged in other ways than through enforced specifications on invoices.

## **4 COMMENTS ON THE ARTICLES IN THE PROPOSAL FOR A REGULATION ON CONDITIONS FOR ACCESS TO THE NETWORK FOR CROSS-BORDER EXCHANGES IN ELECTRICITY**

### **4.1 Article 1 – Subject matter and scope**

20. It is of great importance to facilitate cross-border exchanges and competition within the internal electricity market. The EEA EFTA States are of the opinion that there is a need for a common regulation in this area.

21. The main aim is to create an efficient electricity market. Physical trade between countries is not necessarily a good measure of how efficiently a market works. Cross-border trade may, however, be important to obtain efficient use of the total electricity system. The physical exchange should be based on market prices.

22. The proposed article focuses inter alia on the setting of harmonised principles on cross-border transmission charges. The objective of the regulation is to inter alia facilitate the harmonisation of charges in general. "Cross-border transmission charges" should therefore be replaced by "charges for access to networks". This article must not facilitate cross-border charges.

## **4.2 Article 2 - Definitions**

### *4.2.1 Article 2(a)*

23. The definition of “transit” should comprise physical flows of electricity, i.e., feeding into and tapping from the network determine these flows. In many cases, it will be impossible to determine which country the produced electricity comes from, or it’s destination. Feeding into, or tapping from the grid is more general.

24. On this basis, the EEA EFTA States suggest: "Transit of electricity means a physical flow of electricity hosted on the transmission system of a Member State, which was neither produced nor consumed in the country, including transit flows which are commonly denominated as "loop-flows" or "parallel-flows".

### *4.2.2 Article 2(b)*

25. The EEA EFTA States suggest that the word "transactions" in the definition be replaced by "physical flows":

26. "Congestion" means a situation in which an interconnection linking national transmission networks cannot accommodate the physical flows resulting from international trade by market operators due to lack of capacity.

27. The EEA EFTA States also suggest that it is not necessary to restrict the definition of congestion to the connections between countries. Congestion will also occur in the internal network in a country, and could be managed using the same principles as those between countries.

## **4.3 Article 3 - Inter transmission system operator compensation mechanism**

28. It is not stated explicitly in the regulation, but the EEA EFTA States assume that the idea of a compensation mechanism is the result of the acknowledgement that elimination of all export or import charges (cross-border charges) is a way to achieve an efficient internal market.

29. The EEA EFTA States accept that a mechanism for the compensation of costs for countries that are hosting transit flows is necessary in order to establish a truly integrated internal electricity market. Such a mechanism is, however, strictly speaking, no prerequisite for establishing an efficient market.

30. The EEA EFTA States would like to underline that the mechanism must not lead to export or import charges, i.e., cross-border charges. The mechanism must not interfere with the market. In this context, the EEA EFTA States refer to the ETSO’s proposal for a temporary mechanism for cross-border trade, which in fact implies cross-border charges. Any mechanism that disrupts trade will lead to an inefficient market. For instance, it could be mentioned that for the Norwegian interconnections, there are no cross-border charges to Sweden, Finland and Denmark. The costs related to the interconnections are included in the basis for the general charges of the Norwegian central grid.

31. The EEA EFTA States agree that the TSOs in the countries exporting or importing electricity have to pay in accordance with the compensation mechanism. The payments should go into a fund. Mechanisms where one TSO pays directly to another may be very complicated to figure out.

32. Whether exports or imports shall pay for the transit flows is a question linked to the allocation of costs in the network. This has to be seen in connection with the general rules for the allocation of the costs between generation and load.

33. The amounts of transit hosted and the amounts of transit fed into or tapped from the network should be determined on the basis of the physical flows of electricity actually measured in a given period of time.

34. The definition of transit and the definition of costs incurred by transit flows are not simple. If transit flows are determined as the minimum sum of either export or import in an hour, this could imply that countries where the network system is actually relieved by "transit" flows also get paid for hosting transit flows. The effects on a TSO of transit might differ due to operational and physical conditions in the TSO's network, for example in a situation with a bottleneck inside a country. If the country imports electricity in the south, where it has a deficit of generation and exports the same amount in the north, where it has a surplus of generation, the "transit" through the country will in fact relieve (less losses) the national network. The EEA EFTA States suggest that either the definition of transit flows or the definition of the costs connected with transit flows take this fact into account.

35. The definition of the costs connected with transit flows is not very clear. The definition of the forward-looking long run average incremental cost and how to measure the difference between the costs and benefits that a network bears from hosting transit flows and the costs it would bear in the absence of such flows has to be clearly defined. Even if these costs and benefits are clearly defined, the EEA EFTA States are not sure that it will be possible to create a general mechanism that will allocate the costs and the payments in a reasonable way. In Norway, several research programmes were carried out to find out if it was possible to allocate the costs in the transmission system depending on whether an area had a surplus or a deficit. The conclusions of the research programmes gave no basis for creating a general model that would give acceptable results.

36. The regulation stresses the need for TSOs to recover specific costs incurred by transit. The EEA EFTA States are not sure that it will be possible to find a general mechanism that would ensure adequate return on investment for new installations needed to host transits. Neither do the EEA EFTA States believe that an objective of this mechanism should be to give the right incentives to invest in constructing new network capacity and interconnections. The question of how the building of new network capacity is to be financed, i.e., if there are large systematic bottlenecks in a third country or on the border between TSOs is difficult and could probably not be done through a general mechanism. However, the mechanism could contribute to finance investments in interconnectors.

37. Regarding the proposal from the ETSO about cross-border trade and a transit mechanism from 2002, the EEA EFTA States underline that the existing proposal might imply cross-border tariffs. The EEA EFTA States will not reintroduce cross border tariffs on their interconnections. The EEA EFTA States understand the importance of the proposal made by the ETSO, but also underline that the proposed system should not last for more than one year.

The work towards establishing better systems in accordance with the proposed regulation should be intensified and finished.

#### **4.4 Article 4 - Charges for access to networks**

38. Regarding charges for access to networks, the proposal focuses on important characteristics that should be taken into account. Point tariffs that are independent of trade with electricity and based on non-discriminating conditions are a prerequisite in order to establish an efficient market. Therefore, the EEA EFTA States fully support that there shall be no specific charge in addition to the general point tariff (general charge) for operators with exporting or importing contracts. The EEA EFTA States believe that this is of crucial importance when it comes to creating an efficient integrated internal market.

39. The basic principles for the charges should be to achieve efficient use of the network and thus give efficient locational signals that also will give the right incentives for the location of generation and load. The proposal might be improved if this principle were more binding, or stressed. Therefore, the EEA EFTA States emphasise the importance of creating tariffs that provide efficient locational signals to both generators and consumers.

40. For example, the Norwegian regulations state that the transmission charge (the charge in the central grid) should have one variable component and one or two fixed components. There is also a capacity charge if there are bottlenecks in the transmission system.

41. The energy component is, as a general rule, intended to reflect the marginal losses in transmission. The energy charge also depends on the amount of energy that is fed into, or tapped from the grid, and on the spot price.

42. The energy component in the central grid, which is operated by the TSO Statnett, is based on the percentage marginal loss in each node and on the spot price of Nord Pool.

43. The percentage marginal loss is calculated eight times a year and there are different day-time, night-time and week-end rates. The marginal loss varies with the load on the system and according to where the nodes are situated in relation to each other. In general, feeding into the grid in a surplus area will incur a positive energy charge and tapping out in the same area will incur a negative energy charge. Through tapping and feeding in the same node, the marginal losses should be around zero. The marginal loss rate in the central grid varies by +/- 10%. These energy components facilitate an efficient use of the Norwegian central grid and gives valuable locational signals to the customers of the central grid. A process has now been started to also implement energy components with equivalent characteristics in the regional networks.

44. The fixed components do not vary with the amount of electricity that is fed into, or tapped from, the grid. The fixed component of the charge for the central grid has a connection component and a power component. Both components are based on capacity, measured in MW. All network companies are mainly obliged to charge the same fixed components in the input charge as the central grid.

45. When it comes to the harmonisation of the national network tariffs, the EEA EFTA States support the harmonisation of either the ratio, or the absolute level of the network charges applied to ensure competitive neutrality for generation. The EEA EFTA States nonetheless emphasise that it is not necessary that the level be absolutely the same in every

country. It might also be more convenient for the future work in the harmonisation of tariffs if the basis had a broader economic perspective than only G and L, i.e. not only a discussion on the sharing of costs between producers and consumers. In addition, structural issues are important in the harmonisation.

#### **4.5 Article 5 - Provision of information on interconnection capacities**

46. The EEA EFTA States fully support the necessity of public information regarding the capacity on interconnectors. Information exchange mechanisms between TSOs is of utmost importance when it comes to achieving efficient use of the network and the interconnectors, and also when it comes to questions about the security of the systems.

47. The EEA EFTA States would suggest that the TSOs be obliged to create information exchange mechanisms in order to inform about the net flow that will go over one interconnector. If the TSOs do not know, or have no mechanisms to reveal the net flow, the allocation and use of the interconnectors could be inefficient. In addition, the EEA EFTA States propose that TSOs should be obliged to offer the capacity that they have announced as being available to the market, i.e. the TSOs should not only be responsible for giving indications.

#### **4.6 Article 6 - General principles on congestion management**

48. The EEA EFTA States support that congestion problems shall be addressed with non-discriminatory market-based solutions, which give efficient economic signals to the market participants.

49. Although the EEA EFTA States would like to stress the point that the method of market splitting gives appropriate signals to the market participants, it give revenues to the TSO.

50. In Norway, there exists a system of income caps that ensures that revenues from congestion do not constitute a source of extra profit for the TSO, nor do they give the TSO incentives to keep large bottlenecks. In Norway, the revenues from congestion reduce the general charges.

51. The EEA EFTA States support that curtailment procedures shall only be used in emergency situations where the transmission system operator must act in an expeditious manner and that re-dispatching, or counter-trading is not possible.

52. It is very important that any allocated capacity that will not be used shall be reattributed to the market. This implies that the allocation of capacity has to be done according to the physical flows and not according to the transactions that are made. The "use it or lose it" principle is good, but sanctions for market participants who do not use their reserved capacity must also be put in place. It is crucial that market participants do not have the possibility to prevent usage of the capacity. In addition, the TSOs must always have the possibility to alter the use of the interconnectors when running the system.

53. The EEA EFTA States would like to underline that the system operators have to net the capacity requirements of any power flows in the opposite direction over the congested

interconnection line, in order to secure a usage of this line up to its maximum capacity. This is important in order to achieve efficient use of the interconnections.

#### **4.7 Article 7 – Guidelines**

54. The guidelines should not be more detailed than is absolutely necessary. Parts of the specific details should be left to subsidiary, i.e., to the national regulators.

#### **4.8 Article 13 - Regulatory committee**

55. EEA EFTA States take note of the proposal to establish a regulatory committee. There is, however, still a need to clarify the competence of such a committee and how it impacts the roles of the Commission and individual governments in decisions under the scope of the regulation. In addition, the EEA EFTA States would like to add that the regulatory committee should be composed of members representing the national regulatory authorities. The regulatory committee might work more efficiently if it were composed of homogenous members. The EEA EFTA States wish to participate on equal footing as EU Member States in the committee according to the provisions in the EEA Agreement (reference is made to Articles 99-101 EEA).

#### **4.9 Article 14 - Advisory committee**

56. The EEA EFTA States have further noted the proposal to establish an advisory committee. The role and competence of this committee in the decision-making process related to the further development of the regulation still need clarification. The EEA EFTA States' support for such an advisory committee will be pending on how the role of the advisory committee will be explained more in detail. The recommendation is to make the advisory committee as homogenous in its composition as possible. The EEA EFTA States also wish to participate on equal footing in this committee according to the provisions in the EEA Agreement (reference is made to Articles 99-101 EEA).

#### **4.10 ANNEX - Guidelines on the management and allocation of available transfer capacity of interconnections between national systems**

57. It is of utmost importance that the TSOs do not differentiate between different types of cross-border transactions, whether they are physical bilateral contracts, or bids into foreign organised markets. The method for allocating scarce transmission capacity must be transparent and not related to the different types of contracts, but to the physical flows.

58. It is unclear what is meant by directional price signals as a result of the congestion management.

59. It is also important that the explicit auctions are organised in such a way that they do not lead to problems related to any dominant position of market participants, and that the pricing of the capacity and the auction facilitate an efficient power exchange.

60. According to the proposed regulation regarding the position of long-term contracts, priority access rights to an interconnection capacity cannot be assigned to those contracts, which violate Articles 81 and 82 of the EC Treaty. Provided that the long-term contracts are not in defiance of the relevant provisions in the EEA framework, the EEA EFTA countries assume that the parties in a long-term power exchange agreement can go through with the agreement. It should therefore be clarified that general principles such as "use it or lose it",

and general provisions regarding congestion management and transparency will not be applied on interconnections based on such long-term contracts.

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