



Association of Mediterranean Regulators for Electricity and Natural Gas

MEDREG Institutional AdHoc Group

Recommendations on the Minimum Requirements considered as necessary to ensure Independent Regulatory Authorities in the Mediterranean Area

FINAL REPORT

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INTRODUCTION

The MEDREG AdHoc Group on Institutional issues launched in August 2007 a questionnaire with the aim of referencing the state of the art of regulation in the different Mediterranean countries, regarding the structure, organization and competences of the Regulatory Authorities.

The benchmarking study analysis has been prepared and approved by INS AG in April 2008 with the data provided by regulators from 18 Mediterranean countries. The document has been approved during the 5th MEDREG General Assembly Meeting on May, 26th in Madrid.

On the basis of the benchmarking assessment report, the present document aims at identifying the minimum requirements considered as necessary to ensure independent Regulatory Authorities, which could be shared and implemented throughout the Mediterranean region.

The recommendations can be organized in 7 chapters, covering the various organizational and functional aspects of regulation:

1. Legal status
2. Independence
3. Competencies
4. Procedures for core regulation
5. Transparency
6. Enforcement
7. Accountability

1 MAIN CONCLUSIONS OF THE BENCHMARKING ASSESSMENT (REMINDER)

Analyzing the answers to the 187 items of the Regulatory Benchmarking Questionnaire, **some essential principles can be identified as already shared characteristics** for a significant number of Mediterranean regulators. These common principles cover a broad range of issues directly related to the very definition and role of regulators (see table below).

However, diverging issues remain as regards organizational and functional criteria. The main points are related to differences in the level of autonomy devoted to regulators, especially regarding the sharing of the missions and competencies with governmental bodies.

As promoting closer cooperation between Mediterranean regulators starts with building a common approach of regulation, this benchmarking study is a first step in the identification of shared values and best practice elements for independent and strong regulatory authorities.

Shared characteristics	Diverging points
<p>Independence of regulators from industrial interests</p> <ul style="list-style-type: none"> – setting up of a code of ethics, professional incompatibilities, ownership restrictions, and period of time before employment by the industry. <p>Regulators ability to decide</p> <ul style="list-style-type: none"> – decisions do not have to be approved formally by the government; cannot be rejected, at least without detailed motivation, and cannot be changed by the government. <p>Appeal of regulators decisions before civil and / or administrative Courts</p> <p>Setting up of a settlement of disputes mechanism, with authority on third party access and cross-border disputes</p> <p>Core elements of regulation</p> <ul style="list-style-type: none"> – principles for the elaboration of access tariffs to the transmission and distribution networks – quality of network monitoring – ability to elaborate and enforce rules and standards – supply / demand balance competencies – monitoring of future demand / capacities <p>Investigation powers with full access to information from sector participants</p> <p>Enforcement powers, with the ability to sanction failure to comply with standards and codes</p> <p>Ability to be actively involved in international institutions / projects</p> <p>Accountability procedures</p> <ul style="list-style-type: none"> – publicity and transparency of regulatory activities, issuance of annual reports, cooperation with other bodies (competition authorities) 	<p>Legal autonomy</p> <ul style="list-style-type: none"> – governmental structures – independent bodies <p>Financial autonomy</p> <ul style="list-style-type: none"> – part of State budget – sector based revenues (licenses or contributions from regulated companies through a levy on turnover) – significant constraints in practice in the use of the budget <p>Functional autonomy</p> <ul style="list-style-type: none"> – fixed terms for regulators, renewable or not – possibility to remove regulators <p>Core elements of regulation</p> <ul style="list-style-type: none"> – final decision on access tariff to the transmission and distribution networks – responsibilities as regards utility unbundling <p>Scope of regulators competencies</p> <ul style="list-style-type: none"> – electricity, oil, natural gas, LPG, heat... – impact on the environment

2 RECOMMENDATIONS

2.1 Legal status

Throughout the Mediterranean area, National Regulatory Authorities (NRAs) are set up on a specific legal basis, either through primary or secondary legislation.

Energy regulators are therefore clearly legally separated from their government's administration.

Besides, one single Regulatory Authority should be in charge of the regulation of at least both electricity and gas sectors in each country.

2.2 Independence

The international model of independent NRAs is based on **organizational, financial as well as management independence**, targeted towards having an independent discretion in every aspect of their decision-making process.

2.2.1 Appointment and mandate of members of the Board

Members of the Board are appointed for a fixed term that is non renewable or renewable only once.

Members of the Board are non dismissible. In case of one of the Members being incapable of carrying out its duty, the Board shall decide internally on the appropriate measures to take.

NRAs governance follows a “code of conduct” or “internal rules” including the following obligations for the Members of the Board:

- Incompatibilities with other professional activities or charges when in office;
- Ownership restrictions with regards to interested parties in energy companies;

As regards the appointment process of NRA members, appropriate technical skills as well as a valuable academic background are the main elements to be taken into consideration.

2.2.2 Functional independence

NRAs are fully independent from the interests of the energy industry as well as of State interests, all the more so in case of State-owned incumbents.

NRAs have independent discretion in issuing their decisions in the field of their own competencies, which:

- Do not have to be approved by the government;
- Cannot be rejected or overruled by the government;
- Cannot be modified by the government.

2.2.3 Legal and financial independence

Accordingly to their legal status, **NRAs benefit from a clearly established budget process**, including:

- An at least separate and preferably autonomous budget;
- A significant proportion of the revenues preferably funded by the energy sector and / or tax revenues paid by final consumers, compared to the share provided by State budget.

2.2.4 Organizational independence

NRAs benefit from full autonomy in terms of human resource, having the power to select, hire and remunerate their own staff upon specific criteria.

2.3 Competencies

NRAs are responsible for ensuring non-discrimination regarding access to the transmission and distribution networks, effective competition and efficient functioning of the market.

The minimum requirements for effective regulation include, inter alia, the ability for each NRA to:

- Determine tariff setting principles for the elaboration of access tariffs to the networks;
- Issue and modify licenses;
- Elaborate and enforce networks rules and standards;
- Monitor the market;
- Ensure consumer protection;
- Review effective utility unbundling;
- Investigate on the activity of operators and sanction failure to comply with standards and codes.

2.3.1 Tariff setting

NRAs are responsible for fixing, prior to their entry into force, tariff setting methodologies used to calculate or establish the terms and conditions for:

- Connection and access to national networks, including transmission and distribution tariffs that allow the necessary investments in the networks to ensure their viability;
- The provision of balancing services.

In accordance with the very meaning of regulation, NRAs have the ability to set connection fees.

Moreover and following the same logics, NRAs have the power to:

- Impose proportionate and non discriminatory conditions of access to the networks;
- Ensure that charges applied by network operators are transparent and cost reflective;
- Require performance based components within tariff methodologies (incentive regulation).

NRAs shall also cooperate to harmonize progressively tariff setting methodologies at regional level between neighboring countries.

2.3.2 Licenses

In the countries where licenses are granted to energy operators, **NRAs are responsible to issue and modify licenses and / or to determine the terms and conditions of licenses.**

Moreover, NRAs have the responsibility to review and monitor licenses and the compliance of the actors with licenses dispositions. NRAs also have the possibility to impose a fine on licensees for infraction and / or report infractions for violations of terms and conditions of licenses to another body.

2.3.3 Networks rules and standards

The minimum powers and competencies of NRAs with regard to the elaboration and enforcement of rules and standards include the ability to:

- Set or approve rules / grid code regarding the management and allocation of the interconnection capacity;
- Require that transmission and distribution system operators correct any congestion;
- Monitor the time taken by sector participants to make connections and repairs, to intervene when necessary, and even impose sanctions;
- Set or approve the terms, conditions and tariffs for connecting new producers to guarantee that these are objective, transparent and non-discriminatory;
- Monitor the way transmission and distribution system operators fulfill their tasks and obligations (security of the networks, quality of service standards), with a power to sanction in case of violation of these standards.

2.3.4 Market monitoring

NRAs monitor the wholesale and retail market activities to avoid any abuse of a dominant position, in particular to the detriment of consumers, as well as predatory and anti-competitive behaviour. NRAs shall work in close cooperation with, report to and shall be consulted by the national antitrust / competition authorities which are entitled to take decisions in this matter.

Besides, NRAs review the practical measures taken to ensure a sufficient variety of market actors and to enhance interconnection and competition.

2.3.5 Consumer protection

NRAs monitor the measures taken to ensure a high level of consumer protection and to provide universal service to all household customers and, if considered appropriate, to small enterprises. This includes the right to be supplied with energy of a specified quality at reasonable, easily and clearly comparable and transparent prices.

In this framework, NRAs may set up retail tariffs designed to ensure universal service.

NRAs act complementarily to other authorities and bodies in charge of protection of vulnerable customers, competition and fight against fraud.

2.3.6 Utility unbundling

NRAs have the responsibility to monitor the effective legal separation and accounts unbundling between competitive and monopolistic activities, to ensure that there are no cross-subsidies between generation, transmission, distribution and supply activities.

In this respect, NRAs have substantial competencies, such as:

- Establishing rules regarding the allocation of costs resulting from the unbundling process;
- Mandating changes in accounting practices when NRAs determine that sector participants are not sufficiently unbundled;
- Setting up rules for promoting separation (functional unbundling) between competitive and network activities.

Moreover, NRAs have the power to draw up guidelines for compliance review and reporting of the unbundling process, in order to assess the level of independence of the networks.

2.3.7 Investigation powers

In order to complete their duties and obligations properly, **NRAs are granted full access to the appropriate financial as well as technical information of all players** regarding regulated activities and market monitoring.

2.3.8 Cooperation with other public authorities

NRAs should have the responsibility for compiling information on market dominance, predatory and anti-competitive behaviour.

Besides, NRAs shall work in close cooperation with the national antitrust / competition authorities.

2.3.9 Environmental dimension

NRAs may have authority regarding the impact of the energy sector on the environment (e.g. promotion of renewables sources and of energy efficiency, carbon-dioxide emissions trading...).

2.3.10 International activities

NRAs have the legal and financial ability to participate in international energy cooperation processes and to become member of international institutions.

2.4 Procedures for core regulation

2.4.1 Decision making

Wherever decisions are taken by board members, they follow structured voting procedures (majority/unanimity, quorum, etc.).

In order to avoid deadlock in the decision-making process, the President / Chairman is given a deciding vote in case of even votes.

2.4.2 Appeal

Appeal of the decisions of NRAs is possible before national Civil and / or Administrative Courts.

2.4.3 Settlement of disputes mechanism

Each NRA includes a dispute settlement body among market participants, which powers extend to access issues, including third party access to the networks and cross-border disputes.

Any interested party can refer a complaint to the NRA against a transmission or distribution system operator on issues related to non-discrimination, effective competition, efficient functioning of the market, transmission and distribution tariffs and provision of balancing services.

The NRA then conducts public hearings on such complaints. Specific rules must be set up to protect confidential information.

2.5 Transparency

NRAs can conduct public consultations while elaborating their decisions. Besides, they seek and receive continuous input from sector participants through formal as well as informal ways (letters, e-mails, web portal).

NRAs shall encourage the implementation of compatible IT systems. NRAs shall also facilitate access to each other's information.

Transparency requirements also include the implementation of a communication strategy (press releases, periodical external letter..).

2.6 Enforcement

National Regulatory Authorities have the power to sanction sector participants through different means:

- Publication of comparative performance reports;
- Recommendation or imposition of fines for failure to comply (licenses, secondary legislation...);
- Revocation, suspension or modification of licenses;
- Revision of access tariffs to the transmission and distribution networks.

2.7 Accountability

NRAs should implement the following elements:

- **Issue an annual activity report** received by government and Parliament;
- **Cooperate** regularly with other public bodies;
- Have their **decisions officially published** (including on their website);
- **Motivate their decisions** upon reasoned conclusions;
- Have the ability to **appear before parliamentary committees.**