European Regulation Forum on Electricity Reforms

Bergen SESSA Conference "Harmonising Effective Regulation"

Press Release

SESSA, a programme financed by the European Commission, is a European forum on electricity reforms involving researchers and stakeholders (www.sessa.eu.com). The first SESSA Conference, *Refining Market Design*, was held in Cambridge in July 2004, followed by conferences in Stockholm in October on *Addressing Market Power and Industry Restructuring for Consumer Benefits*, and in Berlin in December on *Perspectives and Challenges of EU Electricity Enlargement*, respectively.

The fourth SESSA Conference, *Harmonising effective regulation*, was held in Bergen, Norway, on 3-4 March 2005. The conference gathered some 100 participants from research institutions, regulatory bodies, and the electricity industry. The first day of the conference was devoted to academic papers describing regulatory experience and discussing regulatory issues, mainly in a European context, and drawing policy implications for the discussion by stakeholders, on the second day.

The objective of WP 6 is to examine the status of and the mechanisms for harmonising electricity sector-specific and general competition regulation at the national and European levels. What obstacles are there for regulatory harmonisation, what are the benefits to be gained, and how should a harmonised regulatory policy be designed and implemented?

The main motivation for harmonisation of regulation at the national and European levels is to assist in the transition of electricity sector from the traditional centrally planned framework to a decentralised framework that promotes economically efficient, secure and environmentally sustainable supply of electricity to European consumers. This calls for an establishment of competitive, market-driven generation and regulated transmission and distribution networks characterised by open and non-discriminatory access that promotes least-cost, reliable, secure and environmentally responsible operations and future development of the electricity industry across Europe.

A prerequisite for the establishment of competitive markets and efficient network regulation is the presence of independent, competent regulators that enjoy exclusive

decision making powers within their defined areas, and arm's length relationships with government and stakeholders. The actual situation in this regard varies across European countries, as documented in the paper by *Larsen et al*. The main objective should be to assure minimum regulation that is harmonised with respect to competence requirements and independence from government and interest groups intervention.

Most countries apply some form of an incentive regulatory mechanism in their network regulation. Measurement of the efficiency of firms is an integral part of such mechanisms. A lot of data and information exist on various approaches to the benchmarking of the performance of electric utilities in European countries, as documented and discussed in the papers by *Filippini et al* and *Bjørndal et al*. The general conclusion is that irrespective of the methods used for benchmarking, the results of such exercises should be used with care. The emphasis should be on using the empirical results to support rather than dictate the parameterisation of the chosen regime. Regulatory discretion and commitment are important in this process.

Reliability and security of supply is a necessary condition for continued political support for the transition of the electricity sector from the traditional centrally planned framework to a decentralised market driven sector, as discussed by *Singh* in his paper. A major hurdle in handling of reliability and security issues in Europe is the multiplicity of definitions and goals in this context, and, consequently, lack of agreement both with respect to problem definition and not the least, if, and in what manner the regulatory interventions should be designed.

Regulation of network activities can take various forms and be approached from various angles. Some alternatives to conduct regulation include regulation by exposure to competition for example through auctioning of monopoly rights, and regulation by contracts where establishment and enforcement of rights and responsibilities of the individual market participants are of crucial importance. Clearly defined rights and responsibilities reduce the traditional inefficiency and market failure reasons for regulation. For example, much of the current cross-border harmonisation between the transmission networks in the Nordic market is based on voluntary contracts between the transmission operators in the region. Regulation by contracts, as discussed by *von der Fehr et al* and *Baldurson*, provides an interesting option for regulation of network monopolies in the European electricity market.

An important issue that remains is related to the harmonisation between general competition policy regulation and sector-specific regulation. This is discussed by *Hope* in his paper. Convergence of network activities and increased application of competition-like instruments in sector-specific incentive regulation make the division of labour and responsibility between competition and sector-specific regulation an important policy issue. Various alternative organisational forms are in use in different countries; however, in most cases there are considerable overlaps wrt regulatory responsibilities between the competition and sector- specific authorities. An interesting institutional reform has been implemented in the Netherlands, where some areas of sector-specific regulation are integrated as divisions within the Competition Authority. Some relevant questions in this context are: What is the "proper" division of labour and responsibility between sector-specific and competition policy regulation? Should this be considered differently for energy markets under deregulation than for "mature" liberalised energy markets? It is too early to answer these questions on the basis of the experience so far; however, the performance of the Dutch model may provide important lessons for other countries.