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National
Association of
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Universal service obligations in liberalised markets

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Center for
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Plan of the lecture

- Private versus public company
- Universal service obligations
- EU Directives on the public service obligations
- Supplier of last resort
- Service quality

Public vs. private company: different goals

- private company's goal is profit seeking
- public company may have different goals set by the Government
- public company may take care about welfare of its customers, without abusing its monopoly power
- but public company may take care about welfare of the politicians
- public company may keep unnecessary workforce, unneeded facilities, etc.

Need for universal service requirements

- Private utility, if unregulated, will pursue higher profits by increasing tariffs and reducing quality, it may also refuse to serve remote and vulnerable customers
- Therefore, not only prices but also quality should be regulated and, more general, universal service requirements must be set

Universal service – a definition

- Universal service means a defined “adequate” set of services of specified quality available to all users independently of their geographical location, and at affordable price

As a rule, users expect:

- **Access** (physical and geographical) and
- **Affordability** (affordable price);
- **Choice** (widest possible choice of services, full choice of payment methods);
- **Transparency** and full information (clear information about prices, bills and suppliers);
- **Quality** (reliability and continuity of services; payment options; complaints handling; dispute resolution, monitoring of performance);
- **Safety** (safe and reliable services);
- **Security** and reliability (continuous and reliable services, including protection against disconnection);
- **Fairness** (fair and genuine competition);

Directive 2003/54/EC states

- “Member States shall ensure that all household customers, and, where Member States deem it appropriate, small enterprises...enjoy universal service, that is the right to be supplied with electricity of a specified quality within territory at reasonable, easily and clearly comparable and transparent prices.”

- Member States may impose on undertakings operating in the electricity sector, in the general economic interest, public service obligations which may relate to
 - security, including security of supply
 - regularity, quality and price of supplies
 - environmental protection, including energy efficiency and climate protection
 - » Directive 2003/54/EC, Article 3

PSO should be

- clearly defined
- transparent
- non-discriminatory
- verifiable
- guarantee equality of access for EU electricity companies to national consumers
 - Directive 2003/54/EC, Article 3

- require Member States to take appropriate measures
 - to protect vulnerable customers (including to help them to avoid disconnection)
 - to protect final customers in remote areas
 - ensure high levels of consumer protection, particularly with respect to transparency regarding contractual terms and conditions, general information and dispute settlement mechanisms
- Member states may appoint supplier of last resort to ensure provision of the universal service
 - Directive 2003/54/EC, Article 3

- Member States shall, upon implementation of this Directive, inform the Commission of all measures adopted to fulfill universal service and public service obligations, including
 - consumer protection and environmental protection,
 - and their possible effect on national and international competition,
 - whether or not such measures require a derogation from this Directive.
- They shall inform the Commission subsequently every two years of any changes to such measures,
 - whether or not they require a derogation from this Directive.
 - » Directive 2003/54/EC, Article 3

Tension between 2 objectives

- Ensuring universal service for all citizens
 - with safe and secure supply
- In as competitive environment as possible
 - with level playing field for all suppliers

Implementation of Electricity and Gas directives in the EU MS

- Under both directives all customers (including residential ones) from the July 1, 2007 are eligible, i.e. may chose a supplier
- Does it mean that 100% opening of the retail market marks the end of regulated tariffs?
- ERGEG found that (as of June 2007) 17 of the EU-27 Member States (concerning electricity) and 9 EU Member States (concerning gas) with partially or totally open markets, had end-user energy price regulation in at least one open market segment

ERGEG has stated, that

- End-user price regulation in electricity and gas markets distorts the functioning of the market
- although in theory the market is open, in practice there may still be only one supplier and a consequent lack of choice for consumers
- ERGEG calls on all countries which are in a transition period to publish (by 1 July 2008) an individual road map towards competitive markets to remove regulated prices

EU directives allow protection of certain consumer categories

- EU directives allow even after a transition period for the removal of regulated end-user energy prices to protect certain vulnerable and remote customers, if necessary
- However protecting “vulnerable customers’ should not be confused with maintaining regulated energy prices for all (or certain categories of) customers
- If there is no competition among suppliers or some suppliers dominate in the market prices to the final consumers could be regulated (perhaps temporarily)

Supplier of last resort in the EU

- Supplier of last resort (SLR) is a tool which protects those customers who might otherwise be unable to obtain energy with reasonable terms and conditions
- A Supplier of Last Resort is obliged to provide energy to final customers in emergency situations according to national legislation when the chosen supplier does not serve or cannot serve

- By the *American approach* SLR supplies:
 - Captive customers before they become eligible
 - Vulnerable customers who suppliers do not want to serve without security of regulated compensation
 - Remote customers not cost effective to serve without subsidy
 - Default customers – Eligible customers who never choose
 - Abandoned customers - Eligible customers who choose, but something happens to their suppliers

Under the EU requirements

- SLR is not mandatory
- It is a mechanism by which universal service is met
- Universal service applied vis-à-vis small electricity consumers
- SLR safeguards cannot impede development of borderless competitive market
- Compensation and rights must be assigned in non-discriminatory and transparent way

Example: SLR in Romania

- SLR applies where a supplier has left the market (unplanned or planned exit, license revocation)
- SLR selected by an auction before the exit event
- Regulator sets up an Auction Committee
- Regulator maintains list of potential SLRs, arranged by service area and class (residential, small commercial, large consumers)
- Bids evaluated on the price proposals, if no bids, regulator appoints

Quality of supply

- quality of supply regulation is becoming an important issue for the regulators
- CEER in 2006 has published a comparative study of quality of supply in the EU Member States
- similar survey has been recently accomplished by ERRA

- *Commercial quality* includes such issues as the timing of a new connection (before the supply contract comes into force), as well as meter reading, billing, handling of customer queries and claims, speed and accuracy in checking the supply voltage and keeping appointments (during the validity of the contract)
- *Continuity of supply* in relation to the interruption of service to consumers connected to the distribution grid; in other words, events during which the voltage at a customer connection drops to zero
- *Voltage quality*, including a subset of the possible deviations of the voltage characteristics from the desired values

Regulatory instruments

to improve quality of supply

- key regulatory instruments are
 - performance standards
 - license conditions
- performance standards
 - guaranteed standards - service levels must be met, otherwise penalty
 - overall standards - customers may expect pre-determined level of service - no penalty

- In liberalized electricity markets vulnerable customers (residential and small commercial) should be guaranteed to enjoy universal service
- Directive 2003/54/EC defined a wide range of compulsory and optional PSO
- for the regulators it is very important that PSOs are clearly defined, transparent, non-discriminatory and do not distort the market

THANK YOU FOR YOUR ATTENTION!

REKK was established at the Corvinus University of Budapest in December, 2003. The mission of REKK is to contribute to the creation of working energy markets and the establishment of efficient regulation by carrying out applied research, training and quality consultancy activities for all those interested persons and organizations that are active in the field.

We think that the experiences that Hungary and some other Central and Eastern European countries have gained through the restructuring and re-regulation of their energy markets are valuable and relevant for all transition economies. This is why the Centre intends to put a special emphasis on the research and dissemination of the regional experience and intends to become a regional research and training centre.

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