



**REPUBLIC OF ALBANIA**  
**-THE COMPETITION AUTHORITY-**  
**-THE COMPETITION COMMISSION-**

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**D E C I S I O N**

**Nr.90, Dated 07. 10. 2008**

**On**

**“On some recommendations for the liberalization and enhancement of competition in the electric energy sector”**

The Competition Commission, on its meeting held on 07.10.2008, with the participation of:

- |                            |                 |
|----------------------------|-----------------|
| ▪ Mrs. Lindita Milo (Lati) | Chairwoman      |
| ▪ Mr. Lush Përpali         | Deputy chairman |
| ▪ Mrs. Servete Gruda       | Member          |
| ▪ Mr. Koço Broka           | Member          |

Discussed the following issue:

**Subject:** Recommendations to public institutions on the liberalization of the electric energy sector.

**Legal basis:** Law No. 9121, dated 28.07.2003 “On Protection of Competition”, as amended, Article 24, letter “f” and Article 70, and also Article 5, paragraph 1 of the Regulation “On the functioning of the Competition Authority”.

**The Competition Commission**, upon reviewing the following documents:

- The report of the working group for the general investigation into the energy sector, the section(s) regarding the electric energy sector, presented by the Secretariat; and
- The organization of the consultative session with the interested institutions, i.e. the Ministry of Economy, Trade and Energy, the Energy Regulatory Entity, the Albanian Energy Corporation (KESH), the Operator of the Transmission System.

## **NOTED THAT:**

### **I. Field of application of Law No. 9121, dated 28.07.2003 “On Protection of Competition**

1. Law No. 9121, dated 28.07.2003 “On Protection of Competition” , as amended, (hereinafter called the “Law”) is applied in cases when undertakings or groups of undertakings, either directly or indirectly, affect, or can affect the market.
2. The Albanian Energy Corporation (KESH), the Operator of the Transmission System, the Operator of the Distribution System and other operators in the energy market exercise their activity as commercial companies and, by consequence, their activity is subject to the Law.
3. Cooperation with the institutions and market players:
  - Pursuant to Article 70 of the Law, and the Memorandum of Understanding, the Competition Authority has cooperated closely with the Energy Regulatory Entity concerning the measures to be undertaken for the liberalization of the energy market, with a view of making it more efficient and open to new entries.
  - The Competition Authority has cooperated with the Ministry of Economy, Trade and Energy, in order to identify the effectiveness of the legislative reform and its impact in the creation of a real market for the electrical energy. This was done in the framework of the work done by the Secretariat on energy issues.

### **II. Purpose of the general investigation**

4. The purpose of the general investigation launched by the Competition Authority into the energy market is the assesment of the level of competition in the market, which indicates what is the market efficiency.

### **III. General investigation followed procedures**

5. The procedures followed during the general investigation were in compliance with Law No. 9121, dated 28.07.2003 “On Protection of Competition”, as amended, and Law No. 8485, dated 11.11.1999, titled “On the Code of Administrative Procedures”. Upon proposal by the Secretary General, and pursuant to Article 24, letter “d” and Article 41 of Law No. 9121, dated 28.07.2003 “On Protection of Competition” the Competition Commission adopted Decision No. 60 dated 12.11.2007 that resolved the launching of a general investigation into the energy market and its submarkets: hydrocarbures, liquid gas and electrical energy markets with the purpose of verifying whether the market competition was being limited or distorted.
6. The report on the general investigation into the energy sector is divided into two parts: one concerns the electrical energy, the other hydrocarbures. This is due to the fact that hese markets have different characteristics and different degrees of liberalization.

7. The report “On the general investigation into the energy sector:, drafted by the working group, was delivered for comments to various institutions, to include the Ministry of Economy, Trade and Energy (METE), the Energy Regulatory Entity (ERE), as well as to the market operators: The Albanian Energy Corporation (KESH), the Operator of the Transmission System (OST), the Operator of the Distribution System and the Association of Independent Producers of Electrical Energy.
8. On 15 September 2008, all the parties mentioned under paragraph 7 above, were invited to participate in a hearing session. The session was held with the participation of METE, ERE, KESH-Gen and the OST. The opinions expressed by the participants were reflected in the final report “On the general investigation into the energy sector”, more specifically, under its first part concerning the electrical energy.
9. The Competition Authority has noted that the Operator of the Distribution System has not been responsive neither during the consultation phase, nor during the process of the general investigation.

#### **V. Legal framework of the electrical energy sector**

10. The activity of the production, distribution and supply with electrical energy in Albania is regulated by Law No. 9072, dated 22.05.2003 “On the electrical energy sector”. The law defines the conditions for the supply with electrical energy, in compliance with the standards, through the effective functioning of the energy market, the promotion of competition in the market, and with regard of the preservation of customers’ interests and the protection of the environment.
11. The legal framework in the sector is further completed by Law No. 9379, dated 28.04.2005 “On the energy efficiency”, which objective is to enhance the efficient use of all types of energy, as well as Law No. 8937, dated 12.09.2002 “On the preservation of heat in the buildings”. The legal framework is further completed by a number of bylaws.

#### **VI. The characteristics of electrical energy market**

12. In spite of some specific characteristics, the electrical energy supply is a service similar to many other public services. One characteristic is that the demand for electrical energy is fluctuating and varies at different periods (within a day, a year, or a business cycle), and these fluctuations are both casual and non-casual. In addition, at least until the present time, can not be deposited in an economically efficient way, which implies that it must be produced and consumed at the same time, and in order to preserve the network stability, there must be a perpetual equilibrium between production and consumption. Another characteristic of the electrical energy is that it can be produced by using a number of technologies, which implies the existence of many cost structures for the electrical energy (e.g. through hydropower, thermopower, (with coal or gas), nuclear power, renewable energy, etc.) The cost structure has important implications on the price mechanism.

12. During the study period was observed the fact that this market is dominated by public property (KESH). In the year 2007, production from the private sector represented only 1.03% of total electrical energy production. The sector included 14 companies engaged in the production of electrical energy.

**VII. The assesment of the degree of liberalization of electrical energy sector and of competition**

14. The market of the electrical energy in Albania is going through a liberalization process. The completion of this process requires significant investments mainly in new energy resources, the transmission and distribution systems, to ensure a real market efficiency and the servicing of all the consumers.
15. The electrical energy sector is regulated by the Energy Regulatory Entity (ERE). The sector regulation has already a completed legal framework and ERE is responsible for its implementation. The ERE has aimed to approve tariffs according to consumer categories, in order to make sure that the tariffs reflect the real costs of electrical energy. In addition, one objective has been the liberalization of production licensing, in order to attract private investors.
16. The electrical energy sector in Albania is in a difficult situation because of the lack of new energy resources and import lines, facing, at the same time, an increasing demand.
17. The reform underway in the sector is synthetized into the Albanian Market Model, adopted by Decision No. 68, dated 23.06.2008 of the Energy Regulatory Entity. In the model are defined all market participants and the relations between them. The main purpose of the Model is the promotion of competition in the wholesale and retail market for the qualified clients. In this context, is aimed at the liberalization of the licensing of production by creating a sufficient number of producers. The Operator of the Transmission System shall perform the activities of transmitter and operator of the system. While the distribution shall be carried on by the Operator of the Distribution System, which is at the final phase of privatization. It has been concocted that the competition in the wholesale market may be increased if more market players are introduced.
18. The reform in the sector has achieved, {from the legal standpoint, at least), the separation of the activities. In addition, the privatization of the Operator of the Distribution System would create the necessary economic motivations in the sector. However, the current status and market structure do not promote the development of competition and this is true both for the wholesale trade, and the qualified clients.
19. In the wholesale energy market are applied, rather unnecessary, two different sale prices by small and independent electrical energy producers.

Given the current tariffs in the market, and at a time when the price of energy is below cost, no company would find the necessary motivation to require the status of *qualified client*. Therefore, under

the current conditions, it can not be discussed on the issue of market opening. The obtaining of the status of *qualified client* requires the covering of administrative costs related with the granting of such status, in accordance with the bylaws enacted by ERE. All these costs make difficult to apply for the the status of *qualified client*, and therefore a clear and comprehensive policy must be applied to ensure that the selected strategy, i.e. the promotion of competition in the wholesale and qualified clients market result in thecreation of better options for the consumers.

20. The privatisation of the Operator of the Distribution System is expected to improve the financial performance because of the expected increase of foreign investments. Nevertheless, the real challenge remains the creation of an elastic demand and supply through the creation of market intermediaries and the increase of choices for qualified clients, in a first phase, and later of the tariff clients.
21. The wholesale supplier and the Operator of the Distribution System must undertake all the necessary measures to fulfill the obligations of the electrical energy sale contracts entered into with small producers. At present, the sale contracts have one-year validity (with the right of rennovation) and the buyers do not have any payment obligation to pay/compensate in the cases when he interrupts the connection with the network. The Energy Regulatory Entity must support a 15 years long-term electrical energy sale contracts, as it is required in the Law on Concessions (December 2006 and two respective DCM fro the granting of concessions, respectively on January 2007 and January 2008) of the type “take or pay”. Such approach would avoid the existing difficulty arising from the fact that the small producers may produce, but may not be able to sell because the distribution is unable to absorb all production. Also, this approach would create better investment conditions for investors, to include the banks.
22. The Law “On Electrical Energy Sector” foresees the obligation for the provision of public service. However, based on the dispositions of the Law, it appears that all the services in this sector are public services, failing to make a clear a detailed definition of the public service and the enterprises that are obligated to fulfill it. The specification of this obligation becomes indispensable for the fulfillment of the obligations stemming from the Law “On state subsidies”, because the imposition of such obligation would, in many cases, require the provision of state subsidies to the enterprise that has the obligation to fulfill the public service.

**FOR THE ABOVE REASONS:**

Pursuant to Article 24, letter “f”, and Article 70 of Law No. 9121, dated 28.07.2003 “On Protection of Competition”, as amended, and upon proposal by its Secretariat, the Competition Commission,

**DECIDED:**

To recommend the Ministry of Economy, Trade and Energy, as well as the Energy Regulatory Entity to undertake the necessary steps for the

consolidation and the real opening of electrical energy market, in accordance with the European Directives (especially 2003/54/EC), and the requirements of the Secretariat for Energy for SouthEastern Europe, with the objective to ensure a functional energy market, with better service and the lowest possible prices.

With regard to the liberalization of electrical energy market, a number of steps must be undertaken, such as follows:

1. To recommend the Ministry of Economy, Trade and Energy that, in cases when natural monopolies are administered by the public sector (KESH-Gen and OST), it must be ensured that they function as commercial companies, thus eliminating financial support from the state budget (both direct and indirect subsidies).
2. To recommend the Ministry of Economy, Trade and Energy, as well as the Energy Regulatory Entity to undertake the following:
  - 2.1 Besides the Operator of the Distribution System, in the market must be introduced the Operator of Wholesale Supply, possibly separated from the former operator, and that in conjunction with the energy market intermediaries and the establishment of a Functional Dispatch Center would enable the creation of a functional energy market. In this manner would improve the competition on the production side, as well as on the wholesale and retail supply.
  - 2.2 To observe the Article 69 Law No. 9121, dated 28.07.2003 "On Protection of Competition", that stipulates that prior to adopting the legal acts, the ERE must obtain from the Competition Authority the assessment [of such acts] regarding restriction, distortion or limitation of competition. This procedure increases the transparency of the process of privatization and liberalization of the electrical energy market.
3. To recommend the Energy Regulatory Entity to undertake the following:
  - 3.1 To increase access to qualified businesses, in order to improve elasticity of demand and opening of the market. The market liberalization in paper must become a reality in practice, to ensure the choice of more than one source of supply, initially for non-tariff customers and latter for tariff customers. The creation of the option to be supplied by multiple energy sources and the use of transmission and distribution networks, the wholesale and /or retail supply, in accordance with the prices regulated by ERE.
  - 3.2 Besides the privatization of the Operator of the Distribution System, the ERE must undertake the necessary steps to further liberalize the market through the licensing of market intermediaries. The transmission and operation of the system shall continue to be monopolies. While regarding the services of supply, production and distribution at the retail market, they are offered by many market players. The news concerning competition in the retail market is the introduction of market intermediaries into the structure, to create the wholesale market.

3.3 The approval of the electrical energy tariffs must be done in a balanced way and undiscriminately. The tariffs must be oriented towards a weighted average cost of the energy bid, and by including there both the average cost of imported energy and the average production cost.

3.4 To merge the two existing methodologies for the trading of electrical energy between small producers and the Public Retail Supplier (the Operator of the Distribution System), into one intergrated methodology that is based in the investment costs.

3.5 To monitor both the Wholesale Suppliers and the Operator of the Distribution System in order to verify whether they are taking all the necessary measures to fulfill the obligations stemming from the electrical energy purchasing contracts, entered between them and the smaller producers.

4. To recommend both the Operator of the Transmission System and the Operator of the Distribution System to ensure access to the network to all consumers, in any case, and in compliance with the rules of conduct of the Operators with Significant Market Power.

This decision enters into effect immediately.

## **THE COMPETITION COMMISSION**

**Lush Përpali**

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**Deputy Chairman**

**Servete Gruda**

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**Member**

**Koço Broka**

(\_\_\_\_\_)

**Member**

**Lindita Milo (Lati)**

**CHAIRWOMAN**