



## **COMMENTS ON THE PROPOSAL FOR A DIRECTIVE TO SAFEGUARD SECURITY OF SUPPLY OF ELECTRICITY AND INFRASTRUCTURE INVESTMENT**

27 May 2004

### **General Comments**

- 1.** ETSO welcomes the opportunity to comment on the proposed directive concerning security of supply and infrastructure investment. ETSO, as the organisation representing transmission system operators throughout the European Community, is deeply involved in both these issues. Our members are responsible for the minute by minute balancing of demand and generation across the transmission systems of the Community. We are also responsible for ensuring that the transmission systems themselves are maintained and developed in such a way as to contribute to secure supplies of electricity through the provision of transmission capacity and its reliability.
- 2.** ETSO members are particularly supportive of initiatives and policy proposals that contribute to the provision of secure electricity supplies in the context of a liberalised and open energy market. As such, we contributed to the development of the Internal Electricity Market Directive (Directive 2003/54/EC) and its associated Regulation through commenting fully on the draft Directives as they became available.
- 3.** The IEM directive, which only comes fully into force in July 2004, covers many of the issues that are also dealt with in the current proposal. Indeed, one of our concerns with the current draft is that on a number of issues the proposed Directive extends, qualifies and partly contradicts the existing IEM Directive.
- 4.** A second major concern is that in a number of instances we do not see how the proposals actually contribute to security of supply in general or the contribution that network investment can make to it. Indeed, in some instances, the proposals could be counter-productive compared with the position as set out in the existing directive.
- 5.** Our final concern is that in a number of instances the proposed directive is not clear in what its intention is and, potentially, misconstrues the responsibilities of certain industry participants, including TSOs. As a consequence, it is in danger of developing inappropriate policy instruments.
- 6.** The following comments, first, illustrate each of these points by reference to individual articles in the proposed directive and then proposes areas that should be positively included in a revised Directive.

## Detailed Comments

**7. Article 3 General Provisions:** Clause 1 of this Article refers to the need for Member States to define and publish the role and responsibilities of transmission system operators and suppliers in respect of ensuring high levels of security of supply. All parties in the supply chain contribute to security of supply. TSOs contribute to security of supply through the minute by minute balancing of generation and load and control of flows on their systems, jointly with their provision of transmission infrastructure. This includes their responsibility to determine the requirements for additional transmission capacity and to invest accordingly. The statement, however, should be expanded to include generators, and distributors, as well as suppliers and TSOs. Furthermore, given the regulated nature of most markets and the fact that Governments set the regulators' responsibilities, it is also appropriate to include Government and Regulatory Authorities in this list. The list as currently specified implies, wrongly, that only TSOs and suppliers have the responsibility for security of supply.

**8. Article 4 Network Security:** It is in our view appropriate that TSOs should establish operational standards for the power systems, both in terms of operation of the power system and the provision of the physical capacity of the transmission system. Compliance with these standards can then be monitored by the Regulatory Authorities. The wording of this clause, as currently drafted, confuses the responsibilities of Governments, Regulatory Authorities, TSOs and distributors. To be effective, clear responsibilities have to be recognised, as is the case in the IEM Directive, where in Article 9, the responsibility of the TSO to provide adequate transmission capacity and a reliable system is quite clear. TSOs should also establish technical standards for generators and distributors in order to maintain consistent operational rules for the power system. Compliance with these standards should also be monitored by the Regulatory Authorities.

**9. Article 5 Maintaining the Balance between Demand and Supply:** This Article as currently drafted is capable of a number of interpretations. The uncertainty revolves around the statement that "Member states shall require transmission system operators to ensure an appropriate level of reserve capacity.....". One interpretation of this statement is that the TSO is responsible for ensuring that sufficient generating (and demand management capability) is available to meet peak demands securely. Such an interpretation would place duties on the TSO that would seriously prejudice a market-orientated approach to the provision of generating capacity to the market and would run counter to the fundamental principles espoused in the IEM Directive and indeed to the Explanatory Memorandum to this proposed Directive. It would also run counter to the principles that generation capacity should be subject to market forces and that TSOs should not be actively engaged in the generation market. An alternative interpretation is that TSOs, in operating the system, should use all reasonable efforts to enable sufficient short-term operational reserve is available to it to be able to deal with credible faults on the system and uncertainties in forecasting demand. Such credible faults would include losses of transmission lines and instantaneous losses of generator in-feed. The levels of such losses and uncertainties to be covered should be established in the operational standards referred to in the comments on Article 4 above, to which TSOs have to operate.

This latter interpretation is current industry practice and is an entirely appropriate responsibility to place on a TSO. On the basis that the latter interpretation is what the Commission envisages then the drafting needs to be clarified to reflect this. If, in the unlikely event that the Commission intends to reflect the former interpretation, the majority of ETSO members fundamentally disagree with this Article.

**10. Article 6 Network Investment:** This Article adds little to what is already included in other Directives, except to require investment plans of distributors and TSOs to take into account in their investment decisions the effects of demand side management. As a comment, not directly related to TSO matters, it is difficult to see how Member States, where the amount of generation is determined by market forces, can ensure that demand side management is taken into account in investment decisions by generators, who are themselves making investment decisions based on their individual interpretations of market trends and developments.

**11. Article 7 Interconnector Construction:** Clause 1 of this article implies that TSOs are the sole body responsible for the provision of cross border interconnection capability. This clearly does not represent the position in many Member States. This clause and clause 2, which sets out the parameters to be taken into account in such decisions, explicitly places a new duty on TSOs “to assess an adequate level of cross border capacity”. However, the clause does not set out on what basis an “adequate level” should be assessed. In this respect, considerable further work is required if this Article is to be put in place. In particular: -

- To amend it to reflect the fact that TSOs do not have sole rights to build interconnectors.
- To make explicit, if this is the Commission’s intention, that TSOs have an obligation to build interconnectors, where existing capacity is seen as not being “adequate”.
- To define “adequate”. In this respect ETSO has commented on a number of occasions on previous Commission documents on the importance of establishing the economic viability of investment in interconnectors before the investment decision is taken. We would hope that the definition of “adequate” would involve, primarily, an economic test.

12. This article also envisages a process where regulatory authorities can intervene in and, indeed, potentially determine the investment plans of TSOs. Furthermore, it suggests a two-stage process for such interventions, involving both the national Regulatory Authorities and the European Commission itself. While ETSO supports the initiative of the Commission to attribute a high level of priority through a Declaration of European Interest to priority projects and recognizes that there should be regulatory involvement in the consideration of planned cross border interconnection capacity, ETSO believes that the need for possible sanctioning should be confined to the relevant National Regulatory Authorities. There may be justification for Commission involvement in the sanctioning

process of interconnection projects that are identified as being Priority Projects of European Interest and which qualify for EU financial support, it would be inappropriate to follow the suggested route in the case of entrepreneurial interconnector construction. ETSO considers that the requirement for the Member States' Regulatory Authorities to consult with the Commission on all proposed interconnection investments, which in turn consults with the European Regulators Group, will introduce unnecessary and inefficient bureaucratic delays to investments. In any event, the reference to financial penalties on TSOs and the issuing of instructions to TSOs in clause 6 of this Article is inappropriate in the event of delays occurring as a consequence of the TSO being unable to gain the necessary approvals for the routing of cables or lines or the construction of sub-stations.

13. ETSO also believes that it is not appropriate for Regulators to be directly involved in infrastructure investment decisions by TSOs. As already commented upon, and as is explicit in the IEM Directive, it is the responsibility of the TSO to determine the need for investment in transmission capacity and to invest accordingly. A process by which this responsibility is weakened through involvement of the Regulator is not helpful to the provision of a secure and efficient network. Furthermore, responsibilities will be made even more unclear if a two-stage process involving national regulators and the Commission is put in place.

14. Overall in respect of Article 7, it is ETSO's view that the current draft should be deleted and that any replacement Article dealing with interconnectors should concentrate on aiding the processes by which TSOs or others can gain the necessary approvals for such projects in a timely manner.

15. **Article 8 Penalties:** This article requires Member States to put in place penalties, including presumably on TSOs, for infringements of the proposed Directive. Given the above comments, it is essential that the roles and responsibilities of the various participants, including Governments and Regulatory Authorities, are accurately and fully set out before any such regime is introduced. Furthermore, any such penalties require duties and obligations to be placed on Governments and Regulatory Authorities to provide:

- A stable and feasible regulatory framework.
- Appropriate levels of risk and reward for regulated industry parties.
- Exclusions where non-performance is outside the control of the party concerned. For example, where TSOs are unable to expand transmission capacity as a consequence of being unable to gain approvals for new lines.

## **ETSO Proposals for Inclusion in Revised Directive**

16. As set out above, ETSO is of the view that a Directive on Security of Supply could enhance the security of the electricity market in Europe and could provide additional reinforcement to the IEM Directive. To do so, in our view, it would need to include the following:

- A recognition of the roles and responsibilities of Member States, Regulatory Authorities, Generators, Suppliers, Transmission System Operators and Distribution Network Operators in contributing to the overall security of supply.
- A clear statement that the provision of sufficient generating capacity to meet demand will be via market forces operating in a stable statutory and regulatory environment and that, through this process, adequate incentives will be provided to generators and suppliers.
- A requirement on TSOs to assess the adequacy of generation in its area and to report on this to the Regulatory Authorities.
- The role of TSOs in matching generation to demand in most member states is limited, currently and for the foreseeable future, to the real time balancing of the market and the procurement of emergency reserves, as laid down in the security standards under which they operate.
- In respect of network investment by TSOs and Distribution Network Operators, a recognition that it is the sole responsibility of the network operator to invest adequately to meet prescribed standards of security;
- The responsibility of the regulatory authorities to set, in conjunction with the network operators, these standards, to ensure that adequate financial resources are available to the network operators to fulfil this obligation by way of the regulated revenues of the operators and to monitor the network operators' performance in doing so.
- In respect of investment in interconnection between countries the Directive should recognise that:
  - No technical standards currently exist to determine the appropriate level of capacity for interconnections between countries.
  - In a number of Member States the TSO has no statutory or licence obligation to invest in interconnection capacity nor is it required to be the owner of such investment.
  - The IEM Directive and Regulation allows for the existence of entrepreneurial interconnectors.
  - ETSO has previously put forward the view that interconnector capacity should be determined on the basis of its economic merits, including within this assessment, the potential contribution to security of supply. The Directive should, in ETSO's view, reflect this position.
  - That a major issue with the development of new interconnectors or with proposals to increase the capacity of existing interconnectors is the gaining of the required approvals for the siting of lines, cables and substations.

## **Conclusions**

17. ETSO and its members have key roles to play in contributing to the security of supply of electricity throughout the Community. As such, we support all initiatives that help to make supplies more secure. Whilst we accept that the existing IEM Directive may need to be supplemented in certain respects in the context of security of supply, the current proposal has a number of shortcomings and errors. Considerable further work is required to overcome these. ETSO and its individual members will, of course, be happy to collaborate with the appropriate authorities in such work