Mutual Recognition of Licenses - Potential Simplification of Licensing Procedure of the Trading Activity

ERRA Licensing/Competition Committee

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ENERGY REGULATORS REGIONAL ASSOCIATION
LICENSING/COMPETITION COMMITTEE

ISSUE PAPER:
MUTUAL RECOGNITION OF LICENSES -
POTENTIAL SIMPLIFICATION OF LICENSING PROCEDURE OF THE TRADING ACTIVITY

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Preface

Dear Colleagues:

I am honored to present to you one of the results of our joint work and efforts during 2005 and 2006: an issue paper prepared by Pierce Atwood based on a request by the ERRA Licensing/Competition Committee. This paper is submitted to the 7th Annual Conference of ERRA.

The issue paper of Mutual Recognition of Licenses - Potential Simplification of Licensing Procedure of the Trading Activity examines and discusses the potential harmonization of licensing procedure and the mutual recognition of licenses in the energy sector as a mechanism for advancing regional markets. However, we need to emphasize two things. The first one is that this document was made by a consultant company, therefore all information and opinion is independent from any of the energy regulatory authorities. The second most important thing is that by the compilation of this paper, our task has not been finished yet. The ERRA Licensing/Competition Committee decided on continuation of this work; discussing the possible way of harmonization, simplification of licensing procedure.

The issue of mutual recognition of licenses in the trading activities is very complex. In the financial world there is one common EU directive which regulate the cooperation of financial authorities. Countries in the different regions could follow the same practice in the energy trading activities (agreements, directives, harmonizes legislation). It is evident that for this a basic harmonization of governmental, legal and regulatory issues would be necessary, which makes the progress more time-consuming.

A set of further steps for the future work will be presented by the ERRA Licensing/Competition members like:

- Defining the aim of the future work, as well as the necessary actions and timing for this
  - treat the trader with and without end-user separately (if possible)
  - simplified licensing treatment for trader without end-user
  - harmonized licensing procedure
  - harmonized licensing conditions
  - harmonized monitoring and enforcement policy, as well, in the regional basis,
  - mutual recognition of trading licenses (as future goal).

The ERRA Licensing/Competition’s suggestion is to publish this document by a press release and send it to CEER and ERRA members and to the EFET after May, 2007.

I would like to thank the continuous technical support received from the National Association of Regulatory Utility Commissioners (NARUC), U.S. Agency for International Development (USAID), the Council of European Energy Regulators (CEER) and the European Federation of Energy Traders (EFET). I look forward to our successful work in the next years.

Sincerely:

Dr. Gabor Szorenyi
Chairman, ERRA Licensing/Competition Committee
Director, Hungarian Energy Office
I. Introduction

A. Purpose and Content

The purpose of this Issue Paper is to discuss the mutual recognition of licenses in the energy sector as a mechanism for advancing regional markets.

Ideally, to avoid inconsistencies and unnecessary transactional costs, a participant in a regional market would only have to obtain one license, instead of a separate license from each jurisdiction participating in the market. A unitary, harmonized licensing regime would ensure license monitoring and the enforcement of regulatory action against license holders throughout the entire region.

As a practical matter, however, the sovereignty of each jurisdiction must be respected, and specific circumstances of each jurisdiction could support the application of differing criteria.

Section II, infra, of this Paper examines the balance between uniformity (harmonization) and subsidiarity, and includes an overview of the current status of efforts to coordinate or otherwise facilitate cross-border licensing and monitoring in the energy sector. Guidance in this area from the European Commission and other authorities, both with respect to the energy sector and analogous cross-border reciprocity efforts, is included.

In Section III, the Paper focuses on the treatment of this issue in three jurisdictions: Hungary, Romania and Ukraine, in order to provide representative case studies.

The last section of the Paper, Section IV, includes a summary and proposes conclusions and next steps.

B. Procedure

Development of this Paper has proceeded in accordance with the following schedule:

May 1: Project Commencement: consultation with the Energy Regulators Regional Association (ERRA) Licensing Committee regarding overall project goals and identification of preferred research areas/countries.

May 15: Identification and finalization with ERRA of the three candidate countries for comparative study.

May 15-July 17: Collection of materials from the regulators of the three candidate countries: the Hungarian Energy Office (HEO), Romanian Energy Regulatory Authority (ANRE), and National Electricity Regulatory Commission of Ukraine (NERC). The regulators were asked to provide
II. Executive Summary

The issue of multiple licensing arises with greatest frequency in the trader context. Opinions differ whether, as a legal matter, countries within the EU or signatories to the 25 October 2005 Energy Community Treaty can require a trader without a physical presence in a jurisdiction to obtain a license from the jurisdiction, even if the trader is doing business in (and can therefore affect) the market in that jurisdiction. Traders seek to limit or eliminate the number of licenses they must acquire, viewing them as unnecessary transactional costs. Regulators from individual countries, however, are concerned that, in the absence of licensing requirements imposed within their particular jurisdiction, they will be unable to obtain necessary data from traders and to enforce the laws and regulations enacted within their jurisdictions to maintain stable markets. This concern is particularly acute in jurisdictions with undeveloped or illiquid markets.

Whatever the ultimate legal conclusion on whether each country can legally demand that a trader obtain a license in order to do business, many ERRA countries currently impose this requirement. To balance trader concerns as to unnecessary costs, and regulatory concerns as to adequate monitoring and enforcement, this Paper recommends that efforts be made to harmonize individual licensing throughout the region and to minimize the cost of obtaining separate licenses. Toward that end, the Committee should develop a model license to use throughout the region, and, during a transitional phase, agree to general principles that will reduce traders’ costs in obtaining the separate licenses demanded of them, eyeing a goal of a unified regional licensing regime.

1 Copies of the questionnaires sent to the three regulatory bodies, with their responses, are attached hereto in Addendum 1, as 1-A (Hungary); 1-B (Romania) and 1-C (Ukraine). During this period, information was also collected regarding the position of the European Federation of Energy Traders (“EFET”) and the related communications from the Hungarian regulator. Copies of these communications are attached hereto in Addendum 2, as 2-A (EFET communications) and 2-B (Hungarian communications).
III. **The Current Status of Efforts to Provide Mutual Licensing Recognition, Reciprocity, or Otherwise to Streamline Licensing Requirements.**

A. **Overview**

Generally speaking, energy regulators issue licenses for each step in the energy chain after the initial extraction of natural resources: production, transmission, distribution and supply. Attention has focused on two of these four stepping stones in particular as requiring multi-jurisdictional coordination in order to facilitate regional markets: transmission and supply.²

Coordination of cross-border transmission is the subject of much discussion and effort, but takes place largely not in the context of licensing reciprocity, but rather in setting consistent system operation rules and developing regional least-cost planning initiatives.

Hence, most discussion with respect to cross-border licensing coordination and recognition has focused on supply, and, in particular, wholesale supply or trade.

B. **Positions Regarding Trader Licensing**

1. **The “Light Touch” View**

   a. **European Federation of Energy Traders (EFET)**

In an October 2005 paper, EFET identified the need to obtain a trading license as one practical problem to the development of regional markets:

“**3.2 Trading licenses**

Particularly eastern European countries require that traders obtain a license. These licenses are usually issued to local companies. Each country has its own licensing authority and fees. Licensing is processed in the local language. All these factors present problems for foreign firms.”

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² Certain aspects of production have been deemed appropriate subjects of regional uniformity, e.g., setting emission standards. A general interest in the building new capacity pursuant to a regional least cost plan has also been shared by donors and other interested parties. (See, e.g., South East Europe Generation Investment Study, financed by the EC and project-managed by the World Bank (April 2005), http://web.worldbank.org/WEBSITE/EXTERNAL/COUNTRIES/ECAEXT/EXTECAREGTOPPOWER/0,.contentMDK:20551083–pagePK:34004173–piPK:34003707–theSitePK:733229,00.html.) There has been a focus on the issue of licensing, however, and the need for an individual country to authorize production has not been the subject of significant debate. Concerns in the area of production licensing have focused more on the general streamlining of licensing new capacity within a country, than on the coordination of licensing requirements from country to country. Similarly, the localized impact of distribution regulation has minimized scrutiny of setting regional standards beyond those technical standards that could affect larger transmission lines.
Thus, EFET supports the elimination of licensing in this area, reducing the transactional costs of cross-border service.

In follow-up discussions with the Committee, EFET has confirmed its position that licensing of traders is unnecessary and that multiple licensing is prohibited under EU law and the Energy Community Treaty.\(^3\)

### b. Southeast European Electrical System Technical Support Project (SEETEC)

In a June 2006 report, SEETEC stated:

“\textit{Licensing}

In the last few years, the regulatory authorities have been busy licensing participants (GenCos, TSO, Suppliers, Traders, DisCos). Some have been issuing trade licenses, while others have been issuing supply licenses. There are wide differences in the region regarding the definition of traders and suppliers. Each regulatory agency must license suppliers, but a trader license should not necessarily be an obligation.”

(SEETEC further stated:

“Licensing has been identified by traders as one of the key concern \cite{sic}. The more common complaints are:

- Non-harmonized licensing regimes in Southeast European countries. The requirements to the potential traders differ from country to country;
- Complicated and long lasting procedure for application and issuing of licenses in some countries;
- Relatively high initial and annual fees to obtaining and keeping of licenses;
- Lack of information in some countries about the current or planned requirements and licensing regime in respect to the wholesale and retail trade.”

\cite{Id. at 3-21.}

With respect to definitions, SEETEC states that “trade” has been defined in the region to mean physical wholesale supply and elsewhere to mean a buyer and seller of financial products. It recommends that the latter definition be used, in which case the “trader” need not be licensed by the energy regulator, but perhaps by the authority in charge of financial services. SEETEC will

\(^3\) See also September 2006 EFET Comments on Obstacles to Trading, found at www.efet.org.
apparently use, as a touchstone for whether licensing should be required, whether or not the
service involves responsibility for balancing. (See id.)

c. Union of Electricity Industry (Eurelectric)

In a 2003 report that surveys various trading regulations in Europe, Eurelectric appears to
suggest the appropriateness of a “light touch” regulatory regime that could eliminate the need for
a specific license for trading. (See Regulatory Aspects of Electricity Trading in Europe,
Eurelectric Working Group Trading, at 11-12, 19.)

2. Proponents of More Comprehensive Regulation

The 2003 Eurelectric report described the scope of trader regulation (including licensing) in
Europe at that time. A more recent publication purports to set out the supply licensing situation
in 30 worldwide jurisdictions, including many in Europe. (Electricity Regulation 2006, Global
Competition Review, in association with Freshfields Bruckhaus Deringer, answer to question
#13: “What governmental or administrative authorizations are required for the sale of power to
customers and which are the responsible authorities to grant such approvals?”).

These resources suggest that, in general, “lighter touch” regimes are found in Western Europe.
One such example, Nordpool, requires a trading company to be a member of Nordpool, which in
turn requires a set of contractual commitments. Norway, one of the countries served by
Nordpool, requires physical traders to obtain trading licenses (Energy Act § 4-1), but they are
subject to few formal requirements.

In France, under the energy law adopted on 13 July 2005, traders supplying eligible customers
file declarations that provide certain information, including their compliance with other
requirements of French law such as contractual prerequisites. The Minister may then object, but
if s/he does not, then the undertaking may trade for a period of five years. As a practical matter,
this could also be viewed as licensing in a “light touch” form.

In contrast, some ERRA countries, those with less developed markets and which lack regional
trading platforms with robust trading volumes (as exemplified by Nordpool), are wary of
exempting traders from stricter governmental oversight and comprehensive review prior to being
authorized to service domestic customers. Various trader scandals have not reduced these
concerns. Some jurisdictions have not been eager to surrender the licensing avenue of regulatory
oversight over trade given that traders are often subsidiaries of generators or otherwise
associated with very large foreign energy undertakings; only approximately 16% of the
electricity in Europe is actually traded cross-border; and complaints have been lodged regarding
the lack of competition in the field.

Also, oftentimes the more undeveloped or illiquid a market is increases the potential for one or a
small number of participants to game or skew the market. The existence of long-term power
purchase agreements (PPAs), regulated prices between generators and the incumbent wholesaler,
export-import limitations, and other inhibiting factors presents a status quo in some ERRA
countries for their markets, which are less developed or liquid than in some areas of Western
Europe. This situation can militate in favor of more regulation, such as licensing requirements, at least in the short run. Later, with the emergence of better-functioning, transparent and more liquid wholesale markets, such a need for a strictly regulated licensing regime could dissipate significantly.

The attached letter from the Hungarian Energy Office (Add. 2-A) summarizes a more comprehensive regulatory perspective. The view of the HEO is that the licensing of traders does not create an artificial entry constraint, but rather is a rational mechanism for the regulator to fulfill its monitoring responsibilities, and ensure “sound financial background, the necessary supply of data and the fulfillment of such minimal professional conditions that the implementation of the activity requires. This is particularly necessary in the respect of security of supply, the protection of customers and the transparency of competition.” In this letter, the HEO notes that several foreign traders are registered in Hungary, indicating that its licensing regulations have not impeded the market entry of foreign market participants.

C. Relevant Legal Authority from the EU

The following section describes guidance from the European Commission (EC) regarding Member States’ ability to license energy sector participants, and the EC’s efforts to eliminate or otherwise reduce duplication in such licensing.

Care must be taken to parse both the letter and the spirit of these EC missives. As described below, these directions show a general desire to promote mutual recognition of licenses, but do not appear to compel this in the energy context, at least not in the near future.

1. General Services Limitations: the Principle of Mutual Recognition

   a. The Definition, Origin and Development of the Principle of Mutual Recognition and Application to Services in General

The principle of mutual recognition can be traced to the Court of Justice’s “Cassis de Dijon” ruling (120/78). Under the principle, a producer or service provider who has complied with the requirements of its country of origin essentially has the right to sell its products or provide its services in all the other Member States.

The principle of mutual recognition thus allows goods and services to move freely within the single European market without the need to harmonize each Member States’ national legislation. In general, the rules of the Member State of origin prevail. Each Member State must accept within its territory products that are legally produced and/or marketed and services that are legally provided in other Member States.

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4 In this ruling, the Court stated that any product lawfully produced and marketed in one Member State must, in principle, be admitted to the market of any other Member State.
However, Member States may challenge the application of this principle in certain limited cases. For example, when public safety, health or the protection of the environment is at stake, the measures they take must be compatible with the principles of necessity and proportionality.

In 1999, the Commission concluded that the principle of mutual recognition had been successfully implemented with respect to goods, but not yet for services, and the Commission defined a new strategy in 2000 with respect to services. In a 2002 Report on the State of the Internal Market for Services, the Commission repeated that “the Internal Market for services is far from being a reality”; and one year later, issued an Internal Market Strategy for the period of 2003-2006 specifying, *inter alia*, that

> “The Commission will make a proposal for a Directive on services in the Internal Market before the end of 2003. This Directive will establish a clear and balanced legal framework aiming to facilitate the conditions for establishment and cross-border service provision. It will be based on a mix of mutual recognition, administrative co-operation, harmonisation where strictly necessary and encouragement of European codes of conduct / professional rules.”

The European Parliament then endorsed the Commission’s Report, stating that it “insists that the Competitiveness Council reaffirm Member States’ commitment to the country of origin and mutual recognition principles as the essential basis for completing the internal market in goods and services.”

### b. The Services Directive

In 2004, following up on these efforts to promote mutual recognition in the services area, the Commission adopted a Proposal for the Directive of the Council and the European Parliament on

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services in the internal market and transmitted it to the Council and the Parliament. The Council reached political agreement on the Proposal as it was amended upon the suggestion of the European Parliament on 31 May 2006, and the Proposal was approved by the European Parliament on 15 November 15 2006. The Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market (hereinafter referred to as the “Services Directive”) came into force on the day following that of its publication and Member States have three years to implement it in their national laws.

The Services Directive applies to services “supplied by providers established in a Member State.” (Article 2 (1).) Under Article 4 (1), “service” is defined as “any self-employed economic activity, normally provided for remuneration, as referred to in the Article 50 of the Treaty,” but excludes sectors such as financial services, transport and telecommunications, which are already covered by other Community-instruments and where further Community initiatives are underway.

**DIRECTIVE 2006/123/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL**

**of 12 December 2006**

**on services in the internal market**

Under the Directive, Member States will examine and, where appropriate, simplify the procedures and formalities governing access to and the exercise of any service activity.

In particular, the Directive provides for:

- The establishment of single points of contact where a service provider could complete the initial formalities relating to its activity and the obligation to make it possible to complete these procedures by electronic means;
- Certain principles to be met by the authorisation schemes applicable to service activities, in particular the conditions and procedures for granting authorisation;
- The prohibition of certain restrictive legal requirements persisting in the laws of certain Member States; and
- The obligation to assess the compatibility of a number of other legal requirements with the conditions laid down in the Directive.

Complex, lengthy and costly authorisation procedures should decrease based on limits on the number of documents required and the development of electronic procedures.
The Services Directive addresses two main elements: 1) freedom to establish a business in another member state (see EC Treaty Articles 43\textsuperscript{11} and 48\textsuperscript{12}) and 2) free trade among Member States (see EC Treaty Article 49\textsuperscript{13}). The primary difference between these two principles is that freedom of services (free trade) covers temporary cross-border provision of services (\textit{i.e.}, the service provider does not have an established physical presence in the State where it provides the services) while freedom of establishment covers those situations where a business has a permanent presence in the territory of another Member State. If a business has an establishment (\textit{e.g.} branch) in the Member State where it provides its services, it should come under the scope of application of the freedom of establishment. If the business does not have an establishment in the Member State where the service is provided, its activities should be covered by the rules on the free movement of services. The Court of Justice has consistently held that the temporary nature of the activities in question should be determined in light not only of the duration of the provision of the service, but also of its regularity, periodical nature or continuity. The fact that the activity is temporary should not mean that the provider may not equip itself with some forms of infrastructure in the Member State where the service is provided, such as an office, chambers or consulting rooms, insofar as such infrastructure is necessary for the purposes of providing the service in question. But an office rented by the company can also be deemed as an establishment if the activity performed there is managed by a provider's own staff or by a person who is independent but authorised to act on a permanent basis for the business.

**Freedom of establishment:**

The primary principle of this concept is that businesses established in a Member State (other than its home country) for the purpose of providing services there, should not have to obtain a license in that host Member State unless: the licensing conditions are non-discriminatory; there is a public interest that justifies their existence; and the objective pursued cannot be attained by means of less restrictive measures. The Directive specifies the criteria that the authorisation scheme shall meet, the prohibited requirements, and those that can be evaluated by the Member States. Notably, the Directive introduces the requirement of non-duplication. This means that the Member State may apply its own conditions in its authorisation procedures, but must take into account equivalent conditions already satisfied by the provider in another Member State.

\textsuperscript{11} EC Treaty Article 43: ”… Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 48, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of the chapter relating to capital.”

\textsuperscript{12} EC Treaty Article 48: “…‘Companies or firms’ means companies or firms constituted under civil or commercial law, including cooperative societies, and other legal persons governed by public or private law, save for those which are non-profit-making.”

\textsuperscript{13} EC Treaty Article 49: “Within the framework of the provisions set out below, restrictions on freedom to provide services within the Community shall be prohibited in respect of nationals of Member States who are established in a State of the Community other than that of the person for whom the services are intended.”
Freedom to provide services:

The freedom to provide services confirms the right of the service provider to provide service in a Member State other than the one where it is established and obliges the Member State in which the service is provided to ensure free access to and free exercise of the service activity within its territory. Under the “country of origin” principle, the Member State where the service is provided cannot apply its own national requirements to service providers established in another Member State unless justified on grounds of public policy, public security, public health or the protection of the environment, and they are non-discriminatory, necessary and proportionate.

The provisions of the Directive concerning the freedom of establishment and the free movement of services apply only to the extent that the activities in question are open to competition.

Derogations:

The Services Directive derogates services covered by the Electricity and Gas Directives from the application of the principle of freedom to provide services (Article 16 of Services Directive). Consequently, only the provisions on the right to establishment in another Member State apply to electricity services (Art. 6, Services Directive) and not those relating to the temporary cross-border services provision. It is unclear whether this derogation covers all services relating to electricity and gas, including trade.

The EC has stated that services of general economic interest are services that public authorities consider should be provided in all cases, whether or not there is an incentive for the private sector to do so. It has also stated that EU Member States are free to determine those services that they consider to be in the general interest. When public authorities deem that such services will not be satisfactorily provided by the market, the EC has stated that public authorities are free to set specific service obligations on undertakings that are entrusted to operate the services of general interest. As the derogation contained in the Services Directive reflects, the Electricity Directive acknowledges that the electricity and gas sectors involve services of general economic interest. Article 3(2) of the Electricity Directive provides: “Having full regard to the relevant provisions of the Treaty, in particular Article 86 thereof, Member States may impose on undertakings operating in the electricity sector, in the general economic interest, public service

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14 Article 16 shall not apply to:
1) Services of general economic interest which are provided in another Member State, inter alia:…
   (b) in the electricity sector, services covered by Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity;”


obligations which may relate to security, including security of supply, regularity, quality and price of supplies and environmental protection, including energy efficiency and climate protection. Such obligations shall be clearly defined, transparent, non-discriminatory, verifiable and shall guarantee equality of access for EU electricity companies to national consumers” (emphasis supplied).

These provisions could be interpreted to mean that when, based on general economic interest, a Member State imposes public service obligations on electricity undertakings, and such undertakings intend to provide services of general economic interest in the territory of another Member State without having an establishment in that other Member State, Article 16 of the Service Directive on free movements of services will not apply to these undertakings -- the other Member State where the undertaking intends to provide its services is not required to provide free access to and free exercise of service activity within its territory. That undertaking shall, however, be entitled to the right of establishment in the other Member State based on Article 9 of the Services Directive, and where it has an establishment in the other Member State, that State may impose non-discriminatory public service obligations upon it.

Administrative simplification:

The Directive provides for significant administrative simplification. Under the proposed Directive, Member States will examine and, where appropriate, simplify the procedures and formalities governing access to and the exercise of any service activity.

In particular, the proposal provides for:

- The establishment of single points of contact where a service provider may complete the initial formalities relating to its activity and the obligation to make it possible to complete these procedures by electronic means;
- Certain principles to be met by the authorisation schemes applicable to service activities, in particular the conditions and procedures for granting authorisation;
- The prohibition of certain restrictive legal requirements persisting in the laws of certain Member States; and
- The obligation to assess the compatibility of a number of other legal requirements with the conditions laid down in the Directive.

Administrative cooperation among the regulatory authorities of the Member States:

To facilitate establishment and the free movement of services in the European Union, the Commission considers it vital to increase mutual trust between the Member States. With this in view, the proposed Directive seeks to:

- Increase mutual assistance between the national authorities to ensure effective control of service activities, based on a clear division of responsibilities between the Member

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States and on cooperation and control obligations vis-à-vis the service providers established in each country. A warning mechanism is established;

- **Develop incentives with regard to the quality of services**, such as voluntary certification of activities, the drawing up of quality charters or cooperation between chambers of commerce and craft associations; and
- Encourage the adoption of **codes of conduct**, in particular by professional bodies or associations, in order to facilitate the supply of services or the establishment of a service provider in another Member State.

**The supervisory rights of the Member State of establishment:**

The Member State of establishment shall ensure that compliance with its requirements is supervised in conformity with its national law, in particular through supervisory measures at the place of the establishment of the provider. In this context, "supervision" should cover activities such as monitoring and fact finding, problem solving, enforcement and imposition of sanctions and subsequent follow-up activities.

**The rights of the Member State where the service is provided:**

At the request of the Member State of establishment, the competent authorities of the Member State where the service is provided shall carry out any checks, inspections and investigations necessary for ensuring the effective supervision by the Member State of establishment. In so doing, the authorities shall act to the extent permitted by the powers vested in them in their Member State. The authorities may decide on the most appropriate measures to be taken in each individual case in order to meet the request by the Member State of establishment.

On their own initiative, the competent authorities of the Member State where the service is provided may conduct checks, inspections and investigations on the spot, provided that those checks, inspections or investigations are not discriminatory, are not motivated by the fact that the provider is established in another Member State and are proportionate.

The Member State where the service is provided may impose requirements on the service provider where they are justified for reasons of public policy, public security, public health or the protection of the environment. In these cases the Member State where the service is provided is responsible for the supervision of the activity of the provider in its territory and shall take all measures necessary to ensure the provider complies with those requirements as regards to the access to and the exercise of the activity and shall carry out the checks, inspections and investigations necessary to supervise the service provided.

To summarize, while the direct applicability of the Services Directive to trading activities is not certain; the Directive will only apply within the EU; Member States will have three years to bring their law into alignment; and issues of public security and other factors will support imposition of State-specific requirements, the Directive nonetheless provides a roadmap toward mutual recognition and regional cooperation. States must take concrete steps to facilitate cross-border provision of services, such as providing a “one-stop shopping” forum to obtain necessary
approvals, and generally speaking, the goal is to leave the primary responsibility for policing a service provider to the State in which the provider is physically centered.

2. Energy Sector EU legislation

Focusing on Electricity, the major applicable EC pronouncement is Directive 2003/54/EC of the European Parliament and of the Council (hereinafter the “Electricity Directive”) concerning common rules for the internal market in electricity and repealing Directive 96/92/EC.

a. The Goal of a Single Market

Among the measures required by the Directive are full market opening, legal unbundling, and the introduction of sector specific regulation in all Member States in order to ensure non-discriminatory access to networks.

Section (4) of the Preamble of the Electricity Directive states, “The freedoms which the Treaty guarantees European citizens – free movement of goods, freedom to provide services and freedom of establishment – are only possible in a fully open market, which enables all consumers freely to choose their suppliers and all suppliers freely to deliver to their customers.” In order to achieve these objectives, the Directive provides for full market opening for all customers effective July 1, 2007.

b. Reciprocity

Recognizing that the degree of market opening would vary State by State, the Directive incorporated the principle of reciprocity in Article 21(2)(a):

To avoid imbalance in the opening of electricity markets:

(a) contracts for the supply of electricity with an eligible customer in the system of another Member State shall not be prohibited if the customer is considered as eligible in both systems involved;….

This principle of reciprocity, whereby one State must open its borders only to the extent that its neighbour state does, is not consistent with the provisions of the EC Treaty on free movement of services requiring equal and open access throughout the one EU market. The Services Directive acknowledges the special features of national electricity markets in the EU, however, and while it generally prohibits Member States to apply reciprocity, it includes an exception with respect to energy.18

c. Harmonization and Development of Regulation

In Section (14) of the Preamble, the Directive provides: “In order to facilitate the conclusion of contracts by an electricity undertaking established in a Member State for the supply of electricity

18 See Article 14(3) of Services Directive.
to eligible customers in another Member State, Member States and, where appropriate, national regulatory authorities should work towards more homogenous conditions and the same degree of eligibility for the whole of the internal market.”

Towards this end, while the Electricity Directive itself does not regulate cross-border trade, Regulation (EC) No 1228/2003 of the European Parliament and of the Council on conditions for access to the network for cross-border exchanges in electricity (hereinafter “Regulation 1228/2003”) does. These Regulations currently cover primarily technical aspects of the cross-border trade, and do not speak to these regulatory issues. They do, however, reflect a process used to develop specific, substantive criteria applicable across borders.

d. EC Desire for Further Progress

Just as the Commission voiced dissatisfaction with the state of the market as to services in general, the Report of the EU Commission on progress in creating the internal gas and electricity market (hereinafter “Progress Report”) states that “… the internal energy market trade is currently underdeveloped.” The Progress Report lists several key factors of the failure to fully integrate the national energy supply into a wider European market, including limited cross-border capacities, market structures with few dominant companies, incomplete unbundling of network operators, regulated third party access, the continued existence of regulated end user prices for electricity, and long-term power purchase arrangements (PPAs).

The Council of the European Union, in its meeting 8-9 June, 2006 in Luxemburg, concluded that for the completion and functioning of the internal competitive energy market, “[t]he national regulatory authorities, relevant state administrative bodies and competition authorities have to play an increasingly important role in delivering liberalised energy market across the EU…. The relevant authorities should be able to carry out their tasks effectively and in a clearly defined manner, and cooperate and coordinate with each other, particularly on issues such as the regulation and monitoring of cross-border network access and trading in order to achieve adequate regulatory consistency across Member States and to avoid double regulation and the imposition of additional unnecessary costs” (emphasis supplied).

The European Energy Regulators’ Group for Gas and Electricity (ERGEG) also emphasizes the importance of a clear regulatory framework and the necessity of governmental support for regional initiatives that are, if necessary, mandated on the EU level through further legislative measures. Based on the Iberian and Southern European examples, ERGEG’s view is that treaties or further EU requirements could prove a useful legal basis for governance of regional markets.

21 10042/06 (Presse 167) Press Release 2735th Council Meeting.
23 The creation of regional energy markets – ERGEG discussion paper 08 June, 2005. Section 6.25.
ERGEG states, “It is necessary to recognise that each individual regulator has limited jurisdiction and authority (i.e. limited to its own national market area) and that it may be necessary to put in place clear and effective regulatory mechanisms to ensure that activity across the regional market can be effectively regulated. Important factors that need to be considered here by the regulators is the need to address any critical ‘regulatory gaps’ that may exist within the regional market, for example in terms of investment but also in terms of the monitoring of market activity at a regional, as well as national, level.”

The ERGEG discussion paper quoted above reported on the following significant regional market initiatives in Europe: Great Britain, the All-Island Market for Ireland and Northern Ireland, the Iberian market, and the Nordic market.

The case studies on the development of these regional markets are attached to the ERGEG discussion paper. As noted above, Nordpool uses, at most, a “light touch” approach: Norway uses a simple trading license; Sweden and Finland do not require authorization to sell power; and Denmark does not require energy licenses for trade; trading activities are regulated under Nordpool’s Competition Act. Hence, to trade in the market only one license (from Norway) is required (in addition to contractual arrangements). Great Britain has one regulator, OFGEM, so mutual recognition is not an issue. The regulators of the All-Island Market have promoted a single regulatory licensing regime to be achieved in interim steps. The intent for the Iberian market is to apply the mutual license recognition principle, so that recognition by one of the countries will automatically credit an agent to act in the other country. The Energy Community Treaty, promoting a South East Europe regional electricity market, and whose signatories consist both of EU and non-EU Members, provides in Article 34: “The Energy Community may take Measures concerning … mutual recognition of licenses…”

In sum, these developed and developing markets are moving toward no licensing or mutual recognition.

3. Financial Services

As noted above, trading in electricity can be either physical or through financial instruments. Particularly, with respect to the latter, it may be helpful to examine EU treatment of licensing in the financial sector.

Mutual license recognition for credit institutions within the EU is regulated in EU Directive 2000/12/EC relating to the establishment and permitting of credit institutions. The EU has moved to create a borderless market conducive to financial sector development, stating in the Preamble to Directive 2000/12: “The approach which has been adopted is to achieve only the essential harmonisation necessary and sufficient to secure the mutual recognition of authorisation and of prudential supervision systems, making possible the granting of a single license recognized throughout the Community and the application of the principle of home Member State prudential supervision. Therefore, the requirement that a programme of operations must be

produced should be seen merely as a factor enabling the competent authorities to decide on the basis of more precise information using objective criteria. A measure of flexibility may none the less be possible as regards the requirements on the legal form of credit institutions of the protection of banking names.”

Based on the provisions of Directive 2000/12/EC, a credit institution which is a legal person must be authorised in the Member State in which it has its registered office. A credit institution that is not a legal person must have its head office in the Member State in which it has been authorised. In addition, Member States can require that a credit institution’s head office always be situated in its home Member State and that it actually operates there. The Directive then permits credit institutions authorised in their home Member States to carry on, throughout the Community, any or all of the activities listed in the Directive by establishing branches or by providing services.

The principles of mutual recognition and home Member State supervision require that Member States’ competent authorities not grant or withdraw authorisation when certain factors indicate clearly that a credit institution has opted for the legal system of one Member State for the purpose of evading the stricter standards in force in another Member State within whose territory it carries on or intends to carry on on the greater part of its activities.

Credit institutions licensed in a Member State may establish a branch or provide cross-border service in another Member State without any further license issued by the host Member State. Consequently, the licensing authority of the home Member State will supervise the activity of this credit institution. A credit institution that intends to establish a branch within the territory of another Member State or intends to carry on its activities within the territory of another Member State must notify the competent authorities of its home Member State.

The competent authority of the home Member State then notifies the host Member State. The competent authority for the host Member State has two months to prepare for the supervision of the new branch or may set up conditions under which, in the interest of the general good, activities must be performed in the host Member State. When a credit institution intends to provide only services in the territory of another Member State, without establishing a branch, the institution notifies the competent authorities of the home Member State, who sends that notification to the competent authorities of the host Member State.

Responsibility for supervising the financial soundness of a credit institution, and in particular its solvency, rests with the competent authorities of its home Member State. The host Member State’s competent authorities retain responsibility for the supervision of liquidity and monetary policy. The supervision of market risk is the subject of close cooperation between the competent authorities of the home and host Member States. The basis of their cooperation is the regular exchange of information. The competent authority of the host Member State has direct power against the credit institution in case it is not complying with the laws of the host Member State and does not stop its non-compliance either upon the request of the authority of the host Member State or its home Member State. In such a situation, the competent authority of a host Member State may take appropriate measures to prevent or to punish further irregularities and, insofar as
is necessary, to prevent that institution from initiating further transactions within its territory.

4. Summary of the EU’s Position

The EU guidance described above contains few actual, clear and squarely applicable substantive requirements or prohibitions with respect to the licensing of energy providers. The EU guidance, along with somewhat parallel efforts in other service areas such as credit institutions, does, however, reflect the Commission’s general views and strong suggestions as to how to proceed, and can be used as predictors as to where the EC is going. Collectively, these materials can be read to suggest as follows:

- The Commission believes that the single European market is not succeeding with respect to services in general;
- While much of the electricity and gas sectors is excluded from the direct requirements of the Service Directive, the Commission has also voiced dissatisfaction with development of a single European electricity market, citing various factors that retard progress;
- The Commission would prefer, when possible, that an undertaking need only obtain one comprehensive license from its “home” State;
- When this broad mutual recognition principle is not fully appropriate, reciprocity may be an interim mechanism to achieve results; any deviation from the mutual recognition principle should be proportional to the reason for the exception; and any required individual State licensing in addition to the home state license should minimize the drawbacks of multiple regulatory regimes;
- Hence, if a Member State is going to require a license from an undertaking that has been licensed in another Member State, at least when the Member State in which the undertaking has been licensed has an open market with respect to the other Member State, the other Member State should attempt to avoid duplication, should reduce the cost of that additional licensing, and should implement one-stop shopping and other mechanisms to streamline the licensing regime and make it transparent.

IV. Case Studies: Hungary, Romania and Ukraine

A. Hungary

Under the provisions of the Hungarian Electricity Act, trade means the purchase and sale of electricity for other than the purchaser’s own use. Electricity trade activity is subject to license; a license is issued for 10 years and may be extended.

The law differentiates between trade activity on the regulated market and on the competitive market. A trader is entitled to act on the competitive market and may sell electricity to other traders, to eligible customers and, in cases specified by the law, to the public service wholesaler. The public service wholesaler operates on the regulated market and may sell electricity only to public service suppliers up to the amount of the electricity consumption of the captive customers. The trader may purchase electricity from generators, from other traders and from abroad (based on a separate license for cross-border transmission of electricity). A licensed trader is also
entitled by the law to trade electricity on the organized electricity market (electricity exchange) after it starts operation (the exchange has not yet been established).

Traders have to hold and maintain their registered capital in the amount of HUF 50 Million (approx. €180,000), and must provide a financial guarantee in the amount equal to one-twelfth of its annual electricity turnover, with a floor of not less than HUF 20 Million (approx. €71,000) and a cap of not more than HUF 500 million (approx. €1,800,000). The amount of the financial guarantee must be deposited in a sub-account separated for this purpose and kept there as transaction collateral. The financial guarantee can be provided in the form of an unconditional and irrevocable bank guarantee in the amount equal to the amount of the required deposit or in any other form of financial guarantee that provides the same level of security.

Foreign trade licenses are not recognized and accepted in Hungary. Foreigners must establish and register a Hungarian company to be able to apply for a trade license.

B. Romania

Under the provisions of the Electricity Law of Romania, supply includes trading electricity to customers, both eligible and captive, and covers supply activity performed on the regulated market and on the competitive market as well.

Supply activity is subject to license, based on conditions specified by the law. A license can be granted to a legal person with its headquarters in Romania. Foreign legal persons must establish a secondary location in Romania.

The supplier must hold and maintain financial guarantees that allow it to continue its activity and ensure the continuity of the service, specified as €100,000 at the time of application approval, with the maintenance of 30-days turnover on supply business during the licensed operation.

The supplier on the competitive market may purchase electricity from domestic producers, from import and on the electricity market (spot market bids) and may sell that power to eligible customers. Suppliers on the regulated market (i.e., distributors) may supply electricity to captive customers and to eligible customers not exercising their eligibility rights.

Foreign trade licenses are not recognized and accepted in Romania, and there is no reciprocity in place with any other country.

C. Ukraine

The Ukrainian Energy Law provides for three general types of licenses issued by NERC: generation, transmission and supply. Because Ukraine currently uses a single buyer market, wholesale trade is conducted by a state enterprise operator, acting as the system and market operator.

Focusing on supply, NERC issues three types of licenses: (1) wholesale, issued to the operator and only the operator; (2) supply at regulated prices; and (3) supply at unregulated prices. The
license for unregulated price supply is simpler than for supply at regulated prices (the suppliers at regulated prices are also the suppliers of last resort and the distribution companies, and they supply all household customers because the regulated price is currently below market price).

There are currently 43 suppliers at regulated tariffs and 556 suppliers (retailers) at unregulated tariffs. There are no eligible customers, but large industrial consumers can acquire a delivery license and supply themselves at non-regulated prices.

Foreign supply licenses are not recognized and accepted in Ukraine. Foreigners must establish and register a Ukrainian company to be able to apply for a supply license.

**D. The United States**

Finally, the federated U.S. system, while materially different from systems presented in, for example, the EU, may still be instructive.

Wholesale trading is regulated in the United States at the federal (i.e. not state) level. While states have some control over traders doing business in the state, they cannot condition wholesale trades on obtaining a state license.

Traders do not obtain licenses per se from FERC, the federal regulator, but do require a filing to obtain “market based rate” authority, i.e. permission to enter into contracts and sell power at competitive prices. See http://www.ferc.gov/industries/electric/gen-info/mbr/application.asp (showing the application for a pure trader, i.e. one that is not a public utility). The process is not complicated or difficult for pure traders; traders within or affiliated with public utilities are subject to greater regulatory scrutiny due to market power issues.

If a state regulatory body believes that a wholesale trader is misbehaving, it can ask FERC or the federal Department of Justice to pursue the trader, but they have no authority to act themselves under existing energy law. It is not entirely clear under existing antitrust law whether a state antimonopoly authority could pursue the trader. If the state antitrust law were not preempted by the Federal Power Act so that state authorities could punish anticompetitive behavior, whether the state authorities could assert jurisdiction over the trader would depend on the state’s longarm jurisdiction statute and, under the U.S. Constitution, on case-specific factors.

Traders who want to engage in the wholesale markets, such as PJM or the New England ISO, must sign membership agreements. These agreements require compliance with the market rules of the RTO/ISO and provide for certain remedies. RTO/ISO market monitors also have the authority to report to FERC suspicions of unlawful conduct or market manipulation (but cannot themselves enforce FERC rules). A new federal statute gives FERC greater authority to punish dishonest behavior.
V. Analysis and Recommendations

Each of the countries included in the case studies require licensing of supply/trade, and given the current status of the markets in the ERRA regions, this requirement is not likely to disappear soon. The question, therefore, is what steps, if any, make sense to facilitate the development of regional markets.

Under the mutual recognition approach, competent authorities need not directly concern themselves with harmonizing their licensing requirements with those of the home State of the undertaking seeking a license. Instead, at least in theory, they respect the primary responsibility of the home State to regulate the undertaking and must assume that the home state is imposing adequate conditions for the undertaking to carry out its activities throughout the region, including the host State.

As the derogations to the new Service Directive indicate, however, when a service such as gas or particularly electricity is involved, for which security of supply can be of concern, each State is permitted to impose its own service obligations, and the general concept of mutual recognition is diluted. Instead, the EC promotes the elimination of duplication and establishment of streamlined or domestically unified licensing proceedings to reduce the transaction costs and delays in obtaining multiple licenses.

Under the EC’s approach, when separate licensing is permitted, the host State must take steps to avoid duplication and narrow its focus to the special circumstances requiring additional regulation. The less harmonization of regulations within a region, the more difficult it is for a host State to determine whether duplication is occurring or to otherwise fulfill streamlining goals. Put simply, it is easier to compare apples to apples than to oranges, so if each license in each State in a region talks in terms of apples, it is easier for the other States to graft onto the home license their own overlay of requirements.

Hence, in the absence of mutual recognition or to facilitate eventual acceptance and implementation of mutual recognition, in the interim, regional markets can be promoted through harmonization of terms and requirements. So, for example, when the Energy Community Regional Board (“ECRB”) is established, one step it may contemplate to develop the regional market is to develop template licenses and definitions, with standard terms.

A. Standard Definitions

As the EFET and SEETEC comments suggest, a starting point could be in using clear and common definitions for supply and trade (including export, import and transit). A part of this definitional exercise could include an analysis of the differences between the two concepts from the point of view of security of supply, system operation, relationship with other traders and customers, monitoring of the licensed activity and enforcement of regulators’ and TSO’s actions. After such an analysis, it could better be determined whether trade, as defined, should be subject to licensing, and, if so, how to divide regulatory responsibility between the energy and financial institution regulator with respect to financial as opposed to physical trades.
B. Other Harmonization Efforts

1. Benchmarking or “gap analysis”

Multiple licensing is much less likely to occur if the regulatory body from the country where a business is about to enter has comfort that the home country where the business was initially licensed will ensure that the business conducts itself appropriately and will take action if it does not. Hence a first step toward reducing unnecessary multiple licensing is to benchmark ERRA countries’ performances in this area.

The general power of the regulatory body, its specific market monitoring authority, and its license conditions and procedures could be identified and shared. Such a survey, which would identify the differences or gaps between each country’s regulatory regimes, could help the regulatory authorities to: 1) gain a better understanding of their neighbors’ regulatory practices, and 2) assist in the harmonization of licensing terms, conditions and procedures. Because previous benchmarking reports regarding the regulatory activities of subsets of ERRA members have already been prepared, this gap analysis would not have to start from scratch.

2. Gap analysis follow-up

Based on such a gap analysis, the basic principles and common platform of a licensing and monitoring regime applicable to the ERRA region could be established. Such a platform would include a common application procedure (the list of documents to be submitted together with the application and a list of the key license conditions); monitoring conditions; and conditions regarding enforcement of the license terms.26 The gap analysis could also cover the division of competences between governments and regulatory authorities, and, based on the analysis, regulators could propose changes to governments to harmonize material differences.

As noted, the anticipated result of such an analysis would not be immediate elimination of multiple licensing, but rather an attempt to harmonize national licensing requirements and processes. Currently, EU law does not provide the same level of legislative protection to the energy industry as it does to the banking sector. Mutual recognition of banking licenses was established by the Directive 2000/12/EC, also explicitly implementing the principles of freedom of establishment and the freedom to provide services. As a result, banking services provided by a credit institution registered and licensed in one EU Member State and acting in another Member State either temporarily or through a branch are not subject to separate license. While a

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26 It should be noted that such a model licensing system can be as comprehensive or limited as the participants desire, and that preparation of the model need not wait for formal or legal adjustments to any national regulatory framework. For example, in the United States, applications to universities used to be a complicated and expensive ordeal, as each university had its own application, charged its own fee, and the applications and attachments had to be filed in hard copy. Now, however, through voluntary cooperation, various universities devised one common application, to be completed on-line. Each university can supplement that common application as it chooses (making sure it avoids duplication). Some universities waive or reduce fees if the applicant uses the uniform application and applies on-line. ERRA regulators could use a similar application process with minimal changes to the existing legal and regulatory frameworks.
similar facility of cross-border service provision may be the ultimate goal at least to some aspects of the electricity and gas sectors, the Services and Electricity and Gas Directives recognize that the predicate for a similar elimination or reduction of State-by-State licensing and regulatory scrutiny has not yet arrived, even within the EU. Varying levels of electricity market opening and other differences in internal markets, among other factors, currently justify derogation with respect to the energy services under the rules of the Service Directive on the free movement of services.

Also, the level of market development in some Eastern European countries and ERRA member states is not yet sufficiently developed to support the initiatives of the industry players to liberalize fully a strict licensing regime.

These countries lack strong, competitive, liquid and transparent (at least wholesale) electricity markets in which market mechanisms, through the contractual arrangements of the market players together with the market regulations, can ensure proper operation and substitute for some of the enforcement tasks of the regulatory authorities practiced through licensing procedures.

One of the main obstacles of a robust and well-functioning electricity market is the existence of the long-term power purchase agreements (LTPPAs) between generators and electricity wholesalers in many countries of the region, tying up capacity and foreclosing the necessary liquidity to allow market forces to substitute for regulatory oversight and intervention. EC authorities are devoting increasing attention to LTPPAs as a brake on the establishment and maintenance of competitive markets, and are taking steps to suppress this problem.27 EU Member States, including ERRA countries, are encouraged to modify their current market structures if necessary to encourage industry players to terminate or significantly modify their LTPPAs in order to improve the functioning of their electricity wholesale markets.

With the increased efforts being taken to develop well-functioning markets, an evolution toward the goal of State-by-State licensing and regulatory oversight can occur.

3. Informal harmonization

While the rules of the Services Directive on the freedom of establishment, applicable to the electricity and gas industry, do not, as a practical matter, prevent Member States from imposing their own licensing systems, and while there are no direct requirements or at a minimum incentives to Member States to give up their individual licensing regimes, the implementation of the provisions of the Services Directive should move Member States toward “lighter touch” licensing regimes. Directive requirements such as non-duplication of conditions; prompt

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27 See, e.g., DG Comp investigation procedure C 41/2005 (ex NN49/2005) against Hungary; Stated Number 43/2005. (ex N 99/2005) – Polish Stranded Costs; Official Journal of the European Union C 52/8, 2.3.2006; Decision C-17/03 of the European Court of Justice in June 2005 in a Dutch case (VEMW-case) where preferential rights have been granted to a company in cross-border transmission of electricity.
issuance of licenses upon establishment of the branch; and one-stop shopping are all steps that ERRA countries can take to work together on reducing the imposition of unnecessary costs on market participants.

Based on the provisions of the Services Directive, regulatory authorities of the Member States must cooperate by way of information exchange, performance of on-site controls for each other, and imposition of appropriate instructions to businesses that provide cross-border electricity trade services through an establishment in another Member State. To facilitate such coordination, and in the event the regulatory authorities would prefer to strengthen their cooperation and harmonize their procedures beyond the minimum suggested by the Services Directive, or would like to introduce mutual recognition of trade licenses on a regional level, they must identify a solid legal basis for doing so.

Due to the lack of relevant binding EU law, regional cooperation relating to the harmonization of laws and regulatory procedures and to the establishment of a regional market can only be supported through international treaties or multilateral agreements like the Energy Community Treaty; the agreement between Portugal and Spain to establish the Iberian electricity market; and the memorandum of understanding for the establishment of the Forum of Nordic Energy Regulators, signed by the regulators of Denmark, Finland, Iceland, Norway and Sweden.

While the above referenced time consuming procedure is under way, regulatory authorities of ERRA countries can take interim steps to facilitate the entry of prospective participants into their domestic markets:

- They can maximize access to information by posting their licensing requirements and other useful information on their web sites. This measure can be taken as a voluntary action of the regulators based upon the suggestions of ERRA to its member states. It would be a significant step forward to help applicants learn the requirements of the relevant licensing authority and to simplify and reduce the duration of the licensing procedure.

- They can propose changes to legislative authorities addressing the greatest concerns articulated by traders. For example, traders claim that the amount of licensing fees (including the application fee and annual fees) are unnecessarily high. Regulators can determine whether the amount of the fee is a true market entry barrier or not. If the result of the analysis justifies this concern, then the fee could be modified (e.g. the amount of the initial fee could be decreased and the amount of the annual fee could be adjusted to the annual trade volume).

- They can begin to act as the one-stop shopping forum for a prospective market entrant, identifying the steps the entrant must take to obtain all necessary legal authorizations and taking whatever actions it can under the existing legal and regulatory framework to coordinate its licensing process with those of other national authorities.
VI. Conclusion and Next Steps

The market and regional environment is not yet ripe to eliminate multiple licensing within the region. Steps, however, can be taken to address traders’ primary and immediate concerns, and to evolve toward a “lighter touch” licensing and monitoring regime. We recommend:

- A gap analysis to identify material differences among the ERRA countries licensing and enforcement regimes in the context of their markets;
- Immediate steps to make individual licensing processes more user friendly, including posting of information on websites and the use of electronic filing processes;
- Preparation of a cooperative model online license application; and
- Based on consultation with traders, identification of the primary aspects of multiple licensing found deleterious to cross-border trade, followed by focused recommendations to governmental authorities for changes to existing national licensing regimes to address legitimate concerns.
ADDENDUM
Addendum 1-A
Hungary

QUESTIONNAIRE
ERRA – Mutual License Recognition Project

Please circle one of the short answer options (e.g., “yes” or “no”) and include any additional explanation you would like. Please e-mail your response to Catherine Connors at cconnors@pierceatwood.com or Erika Nemeth at e.nemeth@axelero.hu no later than July 11, 2006 if possible. If you have any questions, please contact any of the above-cited e-mail contacts. Thank you very much!

1. Does the national law on electricity licensing differentiate between electricity wholesale (trade) and retail (supply to final customers)?  No
2. Must a provider obtain a license for supply?  Yes
3. Must a provider obtain a license for trade?  Yes
4. Does a license for supply allow the licensee to trade?  Yes
5. Does a license for trade allow the licensee to supply?  Yes
6. If a license is required to trade:
   a. are the criteria for obtaining a license contained in the national law or a regulation?  Yes.
   b. if the trader is licensed elsewhere, does the licensing authority in your country accept that license as if it was obtained in your country, or must the trader apply for a license from your country?  Must apply
   c. if the trader licensed elsewhere must apply for a license from your country, is the process streamlined, or must the trader comply with the same criteria for a trading license in your country as any trader not licensed anywhere else?  Same criteria as other applicants
   d. in setting criteria for a trader’s license, did the licensing authority in your country coordinate or adopt criteria from other countries or did it choose to set its own criteria independent of any examination of criteria from elsewhere?  Independent
   e. does the licensing authority in your country reciprocally acknowledge licensing of traders elsewhere in any way?  No
7. If a license is required to supply retail customers:
a. Are the criteria for obtaining a license contained in the national law or a regulation?  
   Yes

b. If the supplier is licensed elsewhere, does the licensing authority in your country accept that license as if it was obtained in your country, or must the trader apply for a license from your country?  Must apply

c. If the trader licensed elsewhere must apply for a license from your country, is the process streamlined, or must the trader comply with the same criteria for a trading license in your country as any trader not licensed anywhere else?  Same criteria as others

d. In setting criteria for a trader’s license, did the licensing authority in your country coordinate or adopt criteria from other countries or did it choose to set its own criteria independent of any examination of criteria from elsewhere?  Independent

e. Does the licensing authority in your country reciprocally acknowledge licensing of traders elsewhere in any way?  No

8. Are the criteria for licensing traders or suppliers in the regulated market the same as in the competitive market?  No

   Explanation: In the regulated market the trading activity and the supply of the customers are differentiated. The criteria are different.

9. Do foreign entities need to establish a local company or a branch or a representative office to be able to trade or perform activities on the national market?  Yes

10. Are there any bilateral agreements in place with other counties in respect to mutual recognition of licenses or to the cooperation between the regulatory authorities?  No

11. Does the law of your country require financial guarantee from the trader/supplier and if yes in what amount?  Yes

   Amount: Depending on the trading volume. Min. 20 million HUF, max. 500 million HUF.

12. The EU uses the concept of 'services of general economic interest'. This means that Member States are entitled to obligate certain companies to provide services of general economic interest when market conditions are inadequate to ensure services necessary for the people's basic needs. Does your law acknowledge the principle of services of general economic interest?  No

   Explanation: There is a new law under preparation in the subject.
QUESTIONNAIRE
ERRA – Mutual License Recognition Project

Please circle one of the short answer options (e.g., “yes” or no”) and include any additional explanation you would like. Please e-mail your response to Catherine Connors at cconnors@pierceatwood.com or Erika Nemeth at e.nemeth@axelero.hu no later than July 11, 2006 if possible. If you have any questions, please contact any of the above-cited e-mail contacts. Thank you very much!

1. Does the national law on electricity licensing differentiate between electricity wholesale (trade) and retail (supply to final customers)? **No**

   **Explanation:** The is only a supply licence that cover both retail and trade on wholesale activities

2. Must a provider obtain a license for supply? **Yes**

3. Must a provider obtain a license for trade? **Yes, the same supply license**

4. Does a license for supply allow the licensee to trade? **Yes**

5. Does a license for trade allow the licensee to supply? **N/A**

   **Explanation:** We have no specific license for trade.

6. If a license is required to trade:

   a. are the criteria for obtaining a license contained in the national law or a regulation? **No**

      **Explanation:** N/A

   b. if the trader is licensed elsewhere, does the licensing authority in your country accept that license as if it was obtained in your country, or must the trader apply for a license from your country? **Must apply for a supply license**

      **Explanation:** no legal provision in this moment for acceptance

   c. if the trader licensed elsewhere must apply for a license from your country, is the process streamlined, or must the trader comply with the same criteria for a trading license in your country as any trader not licensed anywhere else? **Same criteria as other applicants**

      **Explanation:** legal requirement
d. in setting criteria for a trader’s license, did the licensing authority in your country coordinate or adopt criteria from other countries or did it choose to set its own criteria independent of any examination of criteria from elsewhere? **Independent**

**Explanation:** The criteria are setup by Government Decision, but in line with international practice

e. does the licensing authority in your country reciprocally acknowledge licensing of traders elsewhere in any way? **No**

**Explanation:** not yet in this moment because there are not in this moment legal provision for reciprocity acceptance.

7. If a license is required to supply retail customers:

a. are the criteria for obtaining a license contained in the national law or a regulation? **Yes**

b. if the supplier is licensed elsewhere, does the licensing authority in your country accept that license as if it was obtained in your country, or must the trader apply for a license from your country? **Must apply**

c. if the trader licensed elsewhere must apply for a license from your country, is the process streamlined, or must the trader comply with the same criteria for a trading license in your country as any trader not licensed anywhere else? **Same criteria as others**

d. in setting criteria for a trader’s license, did the licensing authority in your country coordinate or adopt criteria from other countries or did it choose to set its own criteria independent of any examination of criteria from elsewhere? **Independent**

**Explanation:** The criteria are setup by Government Decision, but in line with international practice

e. does the licensing authority in your country reciprocally acknowledge licensing of traders elsewhere in any way? **No**

**Explanation:** not yet in this moment because there are not in this moment legal provision for reciprocity acceptance.

8. Are the criteria for licensing traders or suppliers in the regulated market the same as in the competitive market? **No**

**Explanation:** For captive customers the license condition are different. **There are specific rules regarding electricity acquisition (price, quantities), performance standards compliance, obligation to supply all captive customers for a specific area.**
9. Do foreign entities need to establish a local company or a branch or a representative office to be able to trade or perform activities on the national market? **Yes.**

**Explanation: legal requirement**

10. Are there any bilateral agreements in place with other counties in respect to mutual recognition of licenses or to the cooperation between the regulatory authorities? **No**

11. Does the law of your country require financial guarantee from the trader/supplier and if yes in what amount? **Yes. Amount: 100,000 EURO for granting, and 30 days turnover on supply business in operation**

**Explanation: Legal provision.**

12. The EU uses the concept of 'services of general economic interest.' This means that Member States are entitled to obligate certain companies to provide services of general economic interest when market conditions are inadequate to ensure services necessary for the people's basic needs. Does your law acknowledge the principle of services of general economic interest? **Yes.**

If yes, does regulated trade and/or supply activity or certain parts thereof fall under this principle? **Yes**

**Explanation: for residential and small customers and for low income customers in the supply license for captive customers; there are legal provisions**
QUESTIONNAIRE
ERRA – Mutual License Recognition Project

Please circle one of the short answer options (e.g., “yes” or no”) and include any additional explanation you would like. Please e-mail your response to Catherine Connors at cconnors@pierceatwood.com or Erika Nemeth at e.nemeth@axelero.hu no later than July 11, 2006 if possible. If you have any questions, please contact any of the above-cited e-mail contacts. Thank you very much!

1. Does the national law on electricity licensing differentiate between electricity wholesale (trade) and retail (supply to final customers)? Yes/No

   Yes. In accordance with Law of Ukraine On “Electricity Sector” of NERC licenses such types of supply:

   Wholesale (Independent System Operator, basic criteria: sale of electric power to the suppliers on the regulation tariff);

   Supply of electric power on the regulation tariff (basic criteria: buys electric power from a wholesale market; the owner of electric networks, fastened territory of activity, tariff, sets a regulator; does not have a right for resale of electric power to other supplier);

   Supply of electric power on unregulation tariff (basic criteria: buys electric power at a wholesale market or produces; pays for transit to the proprietor of networks; contractual tariff with an user; does not have a right for resale of electric power to other supplier).

   Term “trade” in Law is not used.

2. Must a provider obtain a license for supply? Yes/No

   Yes. For all three types of delivery.

3. Must a provider obtain a license for trade? Yes/No

   Yes, if under a term “trade” it is implied „wholesale delivery”.

4. Does a license for supply allow the licensee to trade? Yes/No

   No, if under a term “trade” it is implied „wholesale”, and under a term «supply» is supply to final customers.

5. Does a license for trade allow the licensee to supply? Yes/No

   No, if under a term „trade” it is implied „wholesale”, and under a term « supply » is supply to final customers.
6. If a license is required to trade:
   a. are the criteria for obtaining a license contained in the national law or a regulation? Yes/No

   Criteria are set by Law of Ukraine „On electricity Sector” and the licensed terms.

   b. if the trader is licensed elsewhere, does the licensing authority in your country accept that license as if it was obtained in your country, or must the trader apply for a license from your country? Accept/Must apply

   Must apply. Licenses are given out only to organizations passing registration on territory of Ukraine.

   c. if the trader licensed elsewhere must apply for a license from your country, is the process streamlined, or must the trader comply with the same criteria for a trading license in your country as any trader not licensed anywhere else? Streamline/Same criteria as other applicants

   Same criteria as other applicants.

   d. in setting criteria for a trader’s license, did the licensing authority in your country coordinate or adopt criteria from other countries or did it choose to set its own criteria independent of any examination of criteria from elsewhere? Coordinated/Independent

   Independent. We study experience of other countries, but hallmark its depending on the features of work of the power system.

   e. does the licensing authority in your country reciprocally acknowledge licensing of traders elsewhere in any way? Yes/No

   No.

7. If a license is required to supply retail customers:
   a. are the criteria for obtaining a license contained in the national law or a regulation? Yes/No

   Criteria are set by Law of Ukraine „On electricity Sector” and the licensed terms.

   b. if the supplier is licensed elsewhere, does the licensing authority in your country accept that license as if it was obtained in your country, or must the trader apply for a license from your country? Accept/Must apply

   Must apply. Licenses are given out only to organizations passing registration on territory of Ukraine.
c. if the trader licensed elsewhere must apply for a license from your country, is the process streamlined, or must the trader comply with the same criteria for a trading license in your country as any trader not licensed anywhere else? Streamline/Same criteria as others

*Same criteria as other applicants.*

d. in setting criteria for a trader’s license, did the licensing authority in your country coordinate or adopt criteria from other countries or did it choose to set its own criteria independent of any examination of criteria from elsewhere? Coordinated/Independent

*Independent. We study experience of other countries, but hallmark its depending on the features of work of the power system.*

e. does the licensing authority in your country reciprocally acknowledge licensing of traders elsewhere in any way? Yes/No

*No.*

8. Are the criteria for licensing traders or suppliers in the regulated market the same as in the competitive market? Yes/No

*At the competition market process of licensing simplified. On regulation - more serious, as at the managed market companies work are proprietors of electric networks, to which NERC sets a tariff and which can not say no to the user in supply.*

*Normative documents set the certain list of documents for the receipt of one or another license.*

9. Do foreign entities need to establish a local company or a branch or a representative office to be able to trade or perform activities on the national market? Yes/No

*Yes. Licenses are given out only to organizations passing registration on territory of Ukraine.*

10. Are there any bilateral agreements in place with other counties in respect to mutual recognition of licenses or to the cooperation between the regulatory authorities? Yes/No

*It is not such agreements in the electricity sector.*

11. Does the law of your country require financial guarantee from the trader/supplier and if yes in what amount? Yes/No
Declarant on the receipt of license to supply of electric power on an unregulation tariff must give the financial guarantee in size of cost of monthly volume of supply of electric power.

12. The EU uses the concept of 'services of general economic interest.' This means that Member States are entitled to obligate certain companies to provide services of general economic interest when market conditions are inadequate to ensure services necessary for the people's basic needs. Does your law acknowledge the principle of services of general economic interest? Yes/No.

If yes, does regulated trade and/or supply activity or certain parts thereof fall under this principle? Yes/No

Yes. Supply of electric power to final customers gets under this principle. A supplier on the regulation tariff does not have right to say no to the user in supply. Now on Ukraine this principle operates at supply of electric power to the householders, because tariffs for the householders are fixed and below than the real level.
Addendum 2
HEO’s Communications

To: Jan van Aken
Secretary General
EFET European Federation
of Energy Traders
Amstelveenseweg 998
1081 JS Amsterdam


Dear Mr Aken,

Based on the standpoint of the Hungarian Energy Office, the Hungarian law does not contradict, neither the spirit of the Directive 2003/54/EC, nor the articles of the Directive. On the contrary, for the sake of the success of the full market opening as well as of the protection of the household customers and the small and medium-sized enterprises as customers it deems it necessary to maintain the licensing regime (procedure) based upon the current practise as long as, in our opinion, this promotes rather than sets back the realization of the above-mentioned aims and objectives; the full market opening and the protection of the customers.

In Hungary, the security of supply and the handling of possible market power problems on the national market require the monitoring of the players in the electricity industry. The Hungarian Energy Office fulfils this task within its monitoring scope, which is prescribed by Law (Article 10 c of Act CX of 2001 of the Electricity Act). The licensing procedure does not create an artificial entry constraint for traders. The goal is simply to ensure the sound financial background, the necessary supply of data and the fulfilment of such minimal professional conditions that the implementation of the activity requires. This is particularly necessary in the respect of security of supply, the protection of customers and the transparency of competition.

During the consultation process on the current licensing regulation, market players, including also the representatives of the consumers and traders, have welcomed the concept that it is necessary to fulfil certain minimum conditions for the implementation of energy industry activities. Since the opening of the market several foreign companies practicing active electricity trade activities through their subsidiaries that are registered in Hungary. That is to say, in case of serious interest the national licensing regulations do not impede the market entry of foreign market participants.
As the Directive 2003/54/EC of the European Parliament and of the Council directly does not regulate the licensing activity, therefore, as long as the system of mutual recognition of licences between the Member States, already existing in case of services, is not established or as long as the national market does not reach a development level where the current practise becomes unnecessary, the Hungarian Energy Office wishes to sustain the current practise for the sake of the monitoring of the licensee.

In addition, we would like to mention that within the ERRA, the HEO began the joint thinking regarding the issue of Mutual Recognition of Licenses.

Yours sincerely,

**Ferenc Horváth J.**
President of Hungarian Energy Office

Cc
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Deputy State Secretary for Energy and Industry,
Ministry of Economy and Transportation
Honvéd u. 13-15.
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