

# **USAID Eastern Europe Regional Energy Efficiency Project**

## **Regulatory Reform And Energy Sector Restructuring Contract**

### **IMPLEMENTING ENERGY REGULATION IN POLAND**

October 21 thru 24, 1996, Jachranka Poland

*Prepared for*

**United States Agency for International Development**

**Project Office - ENI/EUR**

Project No 180-0030

*Under Contract*

**Regulatory Reform And Energy Sector Restructuring In Central And  
Eastern Europe And The Baltics**

Contract No - DHR-0030-C-00-5016-00

22934-008-0003

*Bechtel International Consulting Group*

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Implementing Energy Regulation in Poland Concepts and Practices

Sponsored by USAID

Jachranka, October 21-24, 1996

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**October 21, Monday**

15 30 Bus departure PSE HQ - Warsaw, Mysia 2

16 30-17 30 Jachranka check in and orientation

17 30-17 45 Welcome

17 45-18 15 Introduction Who is Who, Program and Goals

18 15-19 00 Key Issues for Regulation of Polish Energy Industries

19 00 Welcoming Reception and Dinner

Agnieszka Sosulska

) Chris Turner (Bechtel/USAID)  
) Andrzej Pierzak (MoIT)

Russ Brown

) Mirek Duda  
) Andrzej Szablewski

**October 22, Tuesday**

8 00-9 00 Breakfast

9 00-12 30 Regulators' Powers and Duties 1

9 00-10 00 Regulatory Approaches Overview  
-Economic Regulation  
-Technical Regulation  
-Environmental Regulation  
-Consumer Protection

Karl McDermott



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October 23, Wednesday

8 00-9 00 Breakfast

9 00-11 00 Case Study. Privatization and Regulatory Reform in Hungary

- What Happened
- Powers and Duties of Regulator
- Organisation and Structure of the Hungarian Energy Office
  
- Lessons for Poland (Questions & Discussion)

) John Gulliver  
) Cathy Conners

) ERA Working Group Chairpersons

11 15-12 30 Price Regulation 2. Key Issues

- Industry Sectors and Price Regulation
- Definition of Costs
- Estimating Revenue Requirements (Including Investment)
- The Time Dimension Forward or Backward
- Alternative Approaches
  - Rate of Return
  - Price Cap
  - Benchmarking, Standard Costs
  - Combinations

) Chris Turner  
) Jon Stern

12 30-14 00 Lunch

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October 23, Wednesday (cont.)

14 00-15 30 Price Regulation 3. More Key Issues

) Jon Stern  
) Chris Turner

Tariff Transitioning

- When the Prices are Too Low or Too High (and for Whom?)
- When the Subsidies are "Hidden"
- When the Costs are "Questionable"

Inter-Sector Price Distortions

- Efficient Pricing and Politics
- Price of Imported Gas

15 45-18 00 Price Regulation 4. Workshop

Price Regulation and the Implications for Utility Management

- Commercial Operations of Utilities
- Regulated vs Unregulated Business Units
- Effects of Incentives on Management Behavior
- Price Cycling
- Cost-based versus market-based rates
- Regulation of the market
- Implications for Demand-side management

Moderator Cathy Connors  
) Jon Stern  
) Waldemar Ochnio (T&D Ass'n)  
) Mirek Duda  
) Tom Simpson  
) Karl McDermott  
) Chris Turner  
) Andrzej Szablewski

18 30 Dinner

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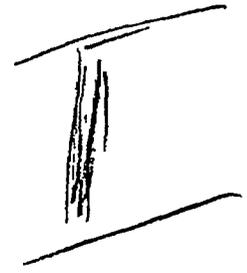
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October 24, Thursday

8 00-9 00	Breakfast	
9 00-11 30	<u>Organisation and Structure of the Regulatory Authority in the U.S and Elsewhere</u> Relations of Regulatory Authority - with Regulated Companies - with other Governmental Institutions - with Non-Governmental Institutions Internal Organisation of Regulatory Authorities - by function - by industry - matrix	Karl McDermott
11 45-13 15	<u>Facilitated Discussion. What Will Work for Poland?</u>  Perspectives on the Regulatory Process in Poland - Polish Energy Law - Update on Process to Establish Regulatory Authority  Panel--Facilitated Discussion - What can ERA do? - How do we get there? - Key transition/policy issues	Moderator Russ Brown  ) Mirek Duda ) Andrzej Szablewski  ) Karl McDermott ) Andrzej Szablewski ) Chris Turner ) Working Group Chairs
13 15	Closing Remarks	Peter Amato (USAID)
13 30-14 00	Lunch	
14 00	Bus Departure for Warsaw	

March 26, 10  
7-10<sup>00</sup>

Chris



**REGULATION APPROACHES OVERVIEW**

**IMPLEMENTING ENERGY REGULATION IN  
POLAND:**

**CONCEPTS AND PRACTICES**

**KARL A. MCDERMOTT  
COMMISSIONER  
ILLINOIS COMMERCE COMMISSION**

- **ECONOMIC REGULATION**

- **COSTS AND PRICES**

- **Natural monopoly characteristics**

- **Methods of pricing**

- **cost of service**

- **value of service**

- **Price discrimination issues**

## ● TRADITIONAL REGULATION

- Public Interest Standard
- Equilibrium Principle/Static Analysis
- Prudent costs of service
- Totality Principle
  - $TC = TR$
  - no single issue ratemaking
- Test year principle
  - normalized
- Obligation to serve
- Cost causality principle
- Collective service principle
- Principle of non-discrimination

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- **TRADITIONAL REGULATION (CONT'D)**

- Incentives created by regulatory lag
- Two part process that is performed simultaneously.
- Determine the total prudent costs and set Revenue Requirement equal to this amount.

SEE FIGURE 1

- The cross-hatched area theoretically represents the total cost of production.

$$TC = \frac{TC}{Q} \cdot Q$$

- So the total revenues that a firm requires is equal to the total costs.

$$TR = TC$$

- What is included in the total costs?
- 10

- **TRADITIONAL REGULATION (CONT'D)**

$$\text{TR} = \text{TC} = [\text{RB}-\text{D}] \text{ROR} + \text{OE} + \text{d} + \text{T} - \text{OSS}$$

---

**RB = Ratebase = Total historic Cost of Capital construction**

**D = Accumulated Depreciation**

**ROR = Rate of return = cost of borrowed funds**

**OE = Operating expenses = wages fuel costs, etc.**

**d = annual depreciation**

**T = Taxes paid by utility**

**OSS = off system sales**

- **The total revenues are generally allocated to various customer classes through the use of cost allocation studies.**

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- TRADITIONAL REGULATION (CONT'D)
  - Typically three general classes of customers:
    - Industrial
    - Residential
    - Commercial
  - Study the timing of their consumption to see who causes plants to be built.
  - Examine total usage of each class.
- 
- The second part of the process involves setting the prices
    - Equity-efficiency conflict

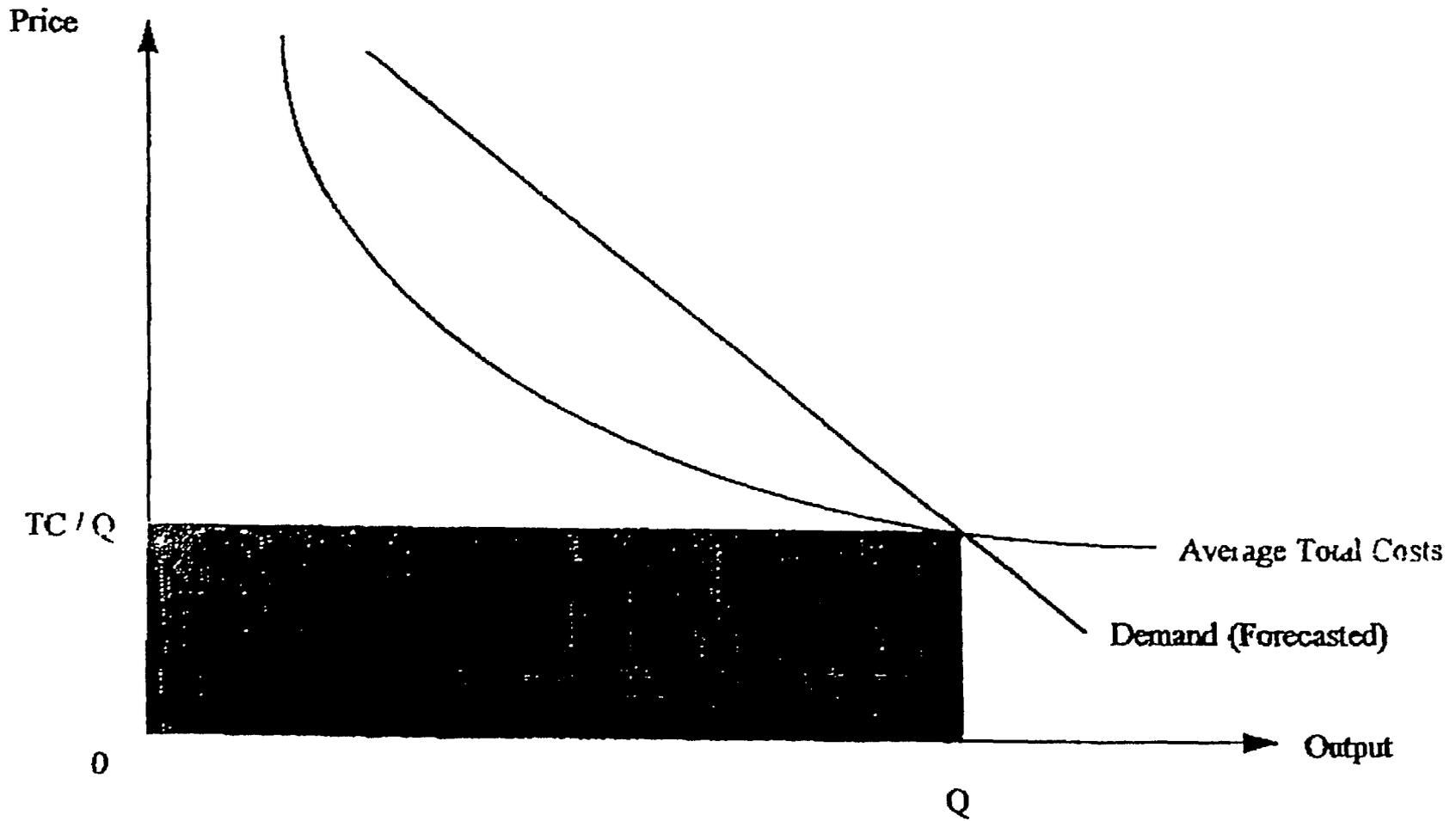
SEE FIGURE 2

- If we price at  $p = ATC$  we are being fair to the utility but not efficient.

- TRADITIONAL REGULATION (CONT'D)

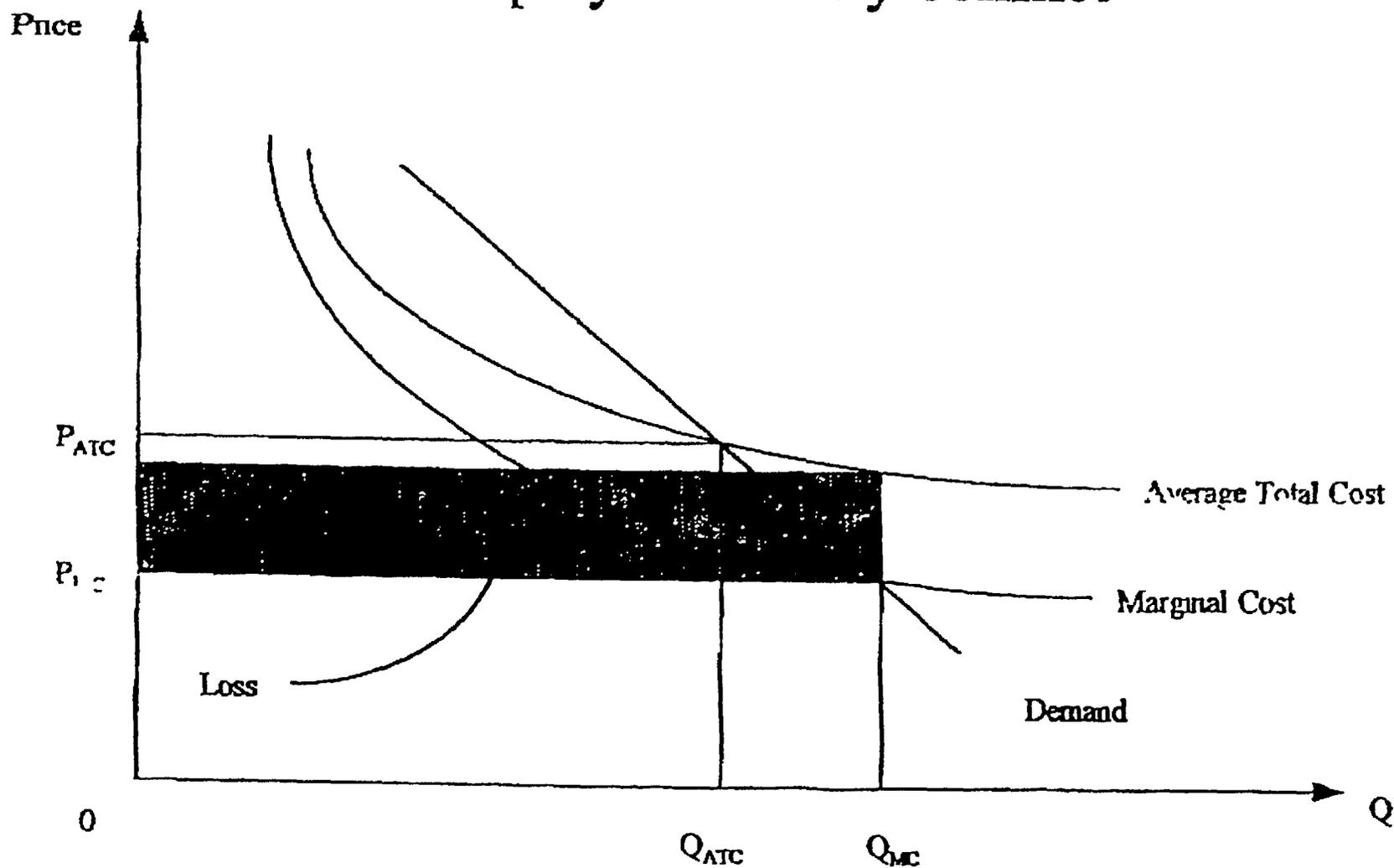
- If we price at  $p = MC$  we achieve an efficient allocation and use of resources but the firm loses money.
- How do we balance these interests?
  - Two (multi) part rates.
    - A fixed charge to cover fixed costs
    - A variable charge per unit of consumption equal to the marginal cost.
    - Block pricing
    - Real time pricing (TOD)

# Figure 1



# Figure 2

## Equity-Efficiency Conflict



● PROFITABILITY ASSESSMENT

- Regulation establishes a “fair rate-of-return” for the regulated company.
- A fair rate-of-return is a level of profit that would just keep the entrepreneur willing to maintain his or her investment in the company.
- Thus, a fair rate-of-return must match the opportunity costs of the next best investment of equal risk.
- In the United States, we use the returns on stocks of companies with comparable risk as a proxy to estimate the allowed profit for a utility.
- This level of profit is not guaranteed. Once the prices have been set, if costs rise, the company’s actual profit may fall and if costs fall actual profits rise. The company has the incentive to reduce and control costs.

● WHY SET THE ALLOWED RATE OF RETURN EQUAL TO THE COST OF CAPITAL

- The basic notion here is that if the allowed rate of return is set equal to the utility's cost of capital then the market value and book value of the utility should be equal. Consider the following simplified example.

(1)  $MV = PV$

(2)  $PV = I/r$

(3)  $I = (BV)ROR$

(4)  $MV = ((BV)ROR)/r$

If  $r = ROR$  then

(5)  $MV = BV$

where:  $MV$  = market value

$PV$  = present value of an asset

$I$  = income of a firm

$r$  = cost of capital

$ROR$  = allowed return

$BV$  = book value of company assets

1

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- **SOCIAL CONSIDERATION FOR PRICING TRANSITIONS**

- Gradual movement to 100% of cost standard.
- Minimize cross-subsidies
  - uneconomic bypass
  - predatory pricing
- subsidies via lump-sum payments, not through pricing decisions.

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- **DYNAMIC PROBLEMS**

- **Inflation**
  - **Fuel Adjustment Clause**
    - **violates single issue**
  - **Construction work in progress**
- **Excess Capacity and Cancellations**
  - **Forecasting problem and the obligation to serve**
  - **ERAM**
- **Pricing Issues**
  - **Marginal cost**
- **Riders**
  - **Violates single issue restriction**

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- DYNAMIC INCENTIVES

- Performance Based Regulation

- Benchmark/yardstick

- Sharing mechanisms

- Price CAP formulas

*Up... .. 100... .. no interd...*

**REGULATOR'S POWERS AND DUTIES**

*h/... .. regulatory energy policy*

**IMPLEMENTING ENERGY REGULATION IN  
POLAND:**

**CONCEPTS AND PRACTICES**

*U team practices*

**KARL A. MCDERMOTT  
COMMISSIONER  
ILLINOIS COMMERCE COMMISSION**

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- **WHAT DOES THE REGULATORY AUTHORITY DO?**

- The ICC regulates investor-owned companies that provide the public with telecommunications, electricity, natural gas, water, and sewer utilities.
- The Commission is responsible under Illinois law for ensuring the citizens of Illinois safe, efficient, reliable, and uninterrupted utility service at reasonable prices. In exchange for this, utilities are given the opportunity to earn a reasonable profit.
- The ICC has five members, one of whom is designated Chairman by the Governor. Each Commissioner is appointed by the Governor and confirmed by Illinois Senate for a five-year term.

Wydaje postanowienia i rozstrzygnięcia  
prezesa i prezesa przedsiębiorstwa

- **DETERMINE REGULATIONS AND ENSURE COMPLIANCE WITH LAWS AND REGULATIONS**

patrz vp 3

**SEE FIGURE 3**

- Administration and management of the technical, professional, and support staff of 297, is the responsibility of the executive director who is hired by the collective Commission.
- The professional Staff conducts hearings involving utilities' rates, audits of operations, investigating customer complaints, assisting in the planning 9-1-1 systems, and long-range energy planning.
- The ICC's authority to regulate rates is not unlimited but before making changes must consider the effects of any changes <sup>on</sup> both consumers and the utility.

- **REGULATE PRICES**

- Balance between economic efficiency and fairness to customers and stockholders.
- $P = MC$  and recovery of fixed costs.

- **ASSESSING INDUSTRY PERFORMANCE**

- Commission receives quarterly reports on the financial performance of each utility.
- If the company overearns then the Commission can call the company in for a rate decrease.

- **MEDIATE DISPUTES**

- Commission has a complaint process where territorial boundary disputes or other complaints regarding service provided between utilities can be resolved.

- **GRANT LICENSES AND CONCESSION PERMITS**

- In the electric and gas industries we have traditionally granted franchises to a utility for the monopoly right to service customers in a specific territory.
- Today, the situation is changing. In the telecommunications industry, entry is allowed for any company that can show managerial, technical and financial ability to serve customers.
- In the gas industry, we have allowed third party marketing companies to offer services to customers directly. Once again, you many <sup>may</sup> impose minimum standards on these companies.
- Retail wheeling is the next step in the electric industry and the same conditions will likely be imposed.

- **HOW DOES THE REGULATORY BODY DO THE JOB?**

- **CONDUCT PROCEEDINGS**

- Under law, a utility may not increase rates until it receives approval from the ICC.
- Rate Cases must be decided within 11 months.

**SEE FIGURE 4**

- Disputes among the parties usually revolve around four issues.
  - The utility's rate base - this includes the amount of money invested to provide utility service and the capital requirements of the company.
  - The utility's expenses - these are the normal operating expenses of the utility for a twelve month period.

- **HOW DOES THE REGULATORY BODY DO THE JOB? (CONT'D)**

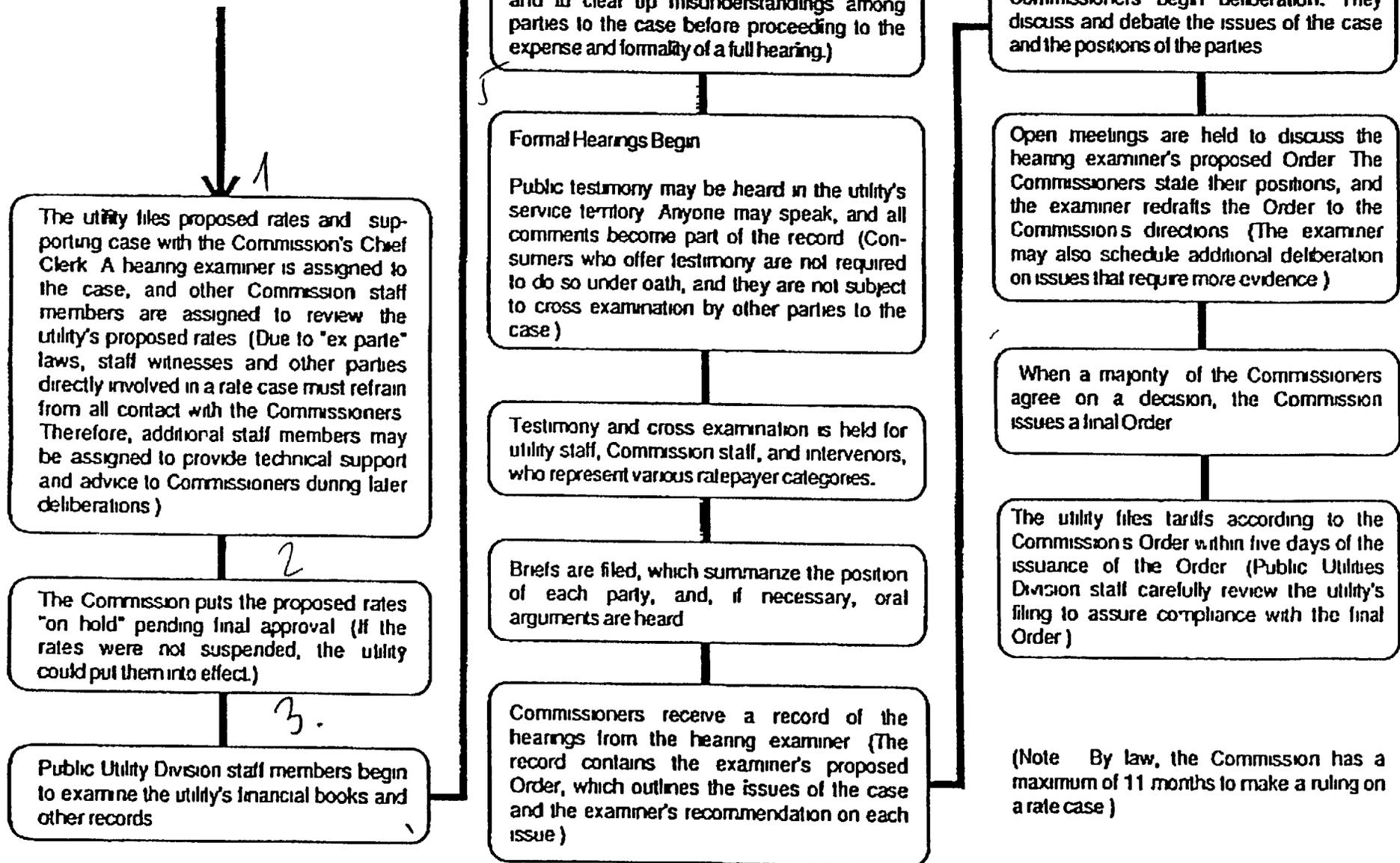
- The utility's rate of return - this is determined by the fair rate of return on investment.
- The utility's rate design - rate design is the process by which the utility's cost of service is allocated among classes of customers (residential, commercial, and industrial) and determines the amount each customer will pay of the total revenue needed by the utility.

- **PUBLIC PARTICIPATION**

- The process permits both the utility and customers to voice their interests in rate case proceedings.
- Parties include the utility requesting the rate change, intervenors representing residential, business, and industrial customers. The Staff of the ICC also participates in the hearings.
- Each party is represented by an attorney and parties may present expert witnesses on various technical aspects of the case at hand. Certain ICC attorneys will act as hearing examiners who conduct hearings, develop a full record and make a report and recommendation to the ICC based on the testimony. The Commissioners then collectively make a final decision.



# Steps In A Rate Case



Baumol and Sidak noted:

...that the proper role of regulation<sup>7</sup> is that of a substitute for competitive market forces where those forces are weak or absent. The regulator's task then becomes a two-part undertaking: first to determine the rules of behavior that a regulated firm could have been expected to follow if it had operated free of regulation in a market with fully effective competitive forces; second, to constrain the regulated firm to behave as it would in such a competitive market and to circumscribe its behavior no less and no more than this.

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# **Establishing the Energy Regulatory Authority in Poland**

## **Key Features of Energy Sector Regulatory Bodies in Six Countries**

**Training Workshop  
21-24 October 1996**

**Jon Stern**  
*n/e/r/a*

# Framework for Session I

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Session will concentrate on:

- how different countries handle **economic regulation** for electricity and gas;
- organisational arrangements for regulation (roles, powers and duties) of Ministry, specialist regulator, other agencies.

# Framework for Session II

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## Main topics discussed

- Who has responsibility for:
  - development planning, capacity expansion and fuel use;
  - price regulation;
  - license/authorisation approvals and modification
- The key functions and degree of "Independence" of the regulators and the regulatory bodies

# Framework for Session III

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The countries discussed are:

Western Europe: Denmark, England, and Wales

Central Europe: Hungary

Asia: Malaysia

Latin America: Argentina

North America: US (State-level regulation)

Countries have been chosen to give a spectrum of:

- more independent and less independent regulatory agencies;
- developed and middle-income countries

# Key Aspects of "Independence" for a Regulatory Agency

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- Which issues are the responsibility of the Regulator and the regulatory agency and which issue are the responsibility of the relevant Ministry;

(Scope/coverage of regulation)

- How the Regulator and the regulatory agency are financed
- Appointment period (fixed term or undefined) and dismissal provisions;
- Discretion for Regulator and reporting powers

# Responsibilities of the Regulatory Agency and Ministry I

	Denmark		Hungary		England and Wales	
	Regulator	Ministry <sup>1</sup>	Regulator	Ministry	Regulator	Ministry
Issuing licenses		✓	✓		✓	
Approving development plans		✓		✓	?	
Approving new projects and fuel use		✓ (with substantial local authority involvement)		✓		??
Price regulation	✓		✓ Advisory only until 1997	✓ Until 1997	✓	
Enforcing competition arrangements	-	?	?		✓	

<sup>1</sup> Danish Energy Agency acts as Ministry implementation agency and is an executive body of Ministry

# Responsibilities of the Regulatory Agency and the Ministry II

	Argentina (Gas)		Malaysia		US - States	
	Regulator	Ministry	Regulator	Ministry	Regulator	Ministry
Issuing licenses	✓			✓	✓	
Approving development plans	✓			✓	✓	
Approving new projects and fuel use	-			✓	✓	
Price regulation	✓			✓ (Electricity)	✓	
Enforcing competition arrangements	✓		✓		?	

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# Financing of Regulatory Agency

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From Central Government Funds

From License Fees/Other

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Denmark

✓

Hungary

✓

England and Wales

✓

(subject to Government approval)

Argentina

✓

Malaysia

✓

US-states

✓

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n/e/r/a

# Appointment Term for Regulation and Dismissal Procedures

	Appointment Term		Dismissal powers		
	Fixed	Not Fixed	At Government Discretion	Government and legislature	Only for serious misdemeanours
Denmark		✓ (Government appoints Chairman only)			? (Chairman only)
Hungary		✓	✓		
England and Wales	✓				✓
Argentina	✓			✓	
Malaysia		✓	✓		
US-states	✓				✓

n/e/r/a

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07

# Key Discretionary and Reporting Issues

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## Denmark

- Minister presents reports to Parliament
- Denmark a highly consensual, decentralised, co-operative political system

## Hungary

- Ministry maintains many powers over operations of HEO (organisation, rules and functions)
- Ministry has many political powers over regulatory issues from ability to issue secondary legislation (eg. obligatory power purchase obligations)
- HEO prepares annual report but Minister presents it to parliament

## England and Wales

- Some residual potential powers with Minister
- All regulatory reporting by regulatory offices

# Key Discretionary and Reporting Issues II

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## Argentina

- Young agency only established in last 5 years
- Much discretion from description of legal framework, unclear how much political intervention in practice

## Malaysia

- Minister has wide-ranging powers over operations, functions and procedures of regulator

## US-states

- Considerable discretion for Regulators within a tightly defined legal process

# **Overall Judgement On Degree of Independence of Energy Regulators**

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## ***High***

**England and Wales**

**US-states**

**Argentina**

(as specified in legal provisions,  
yet to be confirmed in practice)

## ***Low***

**Denmark**

(as specified in legal provisions,  
more in practice)

**Hungary**

(both in legal documents and  
so far in practice)

**Malaysia**

(very low to date)

# **Establishing the Energy Regulatory Authority in Poland**

## **Key Factors of Energy Sector Price Regulation in Six Countries**

**Jon Stern**

*n/e/r/a*

**Training Workshop 21-24 October 1996**

# Framework for Session I

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The key features of Price Regulation covered are:

- Which energy prices are regulated (end-user prices only or the main (and monopoly) elements of the price chain);
- The criteria used in assessing costs of supply and regulatory prices;
- The roles of (a) Ministries and (b) the Regulatory Authority for
  - setting cost and price regulation criteria;
  - regulating energy prices
- Method of price regulation used (forward looking or backward looking, rate of return, price cap, yardstick/benchmark etc)

# Framework for Session II

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The countries discussed are:

Western Europe: Denmark, England and Wales

Central Europe: Hungary

Asia: Malaysia

Latin America: Argentina

North America: US (State-level regulation)

# Which Energy Prices are Regulated

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	End-user prices only	All key elements of price chain
Denmark		✓
Hungary	✓	
England and Wales		✓
Argentina		✓
Malaysia	✓	
US (state-level)		✓

# The Criteria Used for Energy Price Regulation I

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- Denmark
- cost related;
  - explicit guidelines for depreciation, re-investment allowances and interest on capital
  - since 1995, profits allowed to be earned and used elsewhere in special circumstances
  - no price regulation of private generations under 25 Mw or gas sales to large consumer (over 300 thousand m<sup>3</sup>)

- Hungary
- prices set accordingly to minimum justifiable costs (subject to Ministerial direction on bulk power purchase obligations);
  - criteria in Electricity Act "prices shall include the recovery of reasonable investments and the costs of license holders operating efficiently, as well as the profit necessary for ongoing operations".

# The Criteria Used for Energy Price Regulation II

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England & Wales – minimum necessary cost to maintain supply and development of network,  
– cash financial viability of energy enterprises,  
– no regulation of competitive elements (electricity generation, gas purchase)

Argentina – gas transport and distribution only, not gas purchase  
– prices set must be sufficient to enable a reasonable rate of return

Malaysia – cost based but no guarantee that cost pass-through will occur in practice, at least for electricity  
(September 1993 formula suspended in 1995 when changes in independent producer costs would have triggered electricity tariff increase)

– cost based with emphasis on revenue requirement for continued operation and approved investment

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# Allocation of Responsibilities for Price Regulation

	Who sets Pricing Methodology		Who Regulates Prices	
	Regulator	Ministry	Regulator	Ministry
Denmark		✓	✓	
Hungary	✓			✓ (Until 1997)
England and Wales	✓		✓	
Argentina	✓ (Largely)		✓	
Malaysia		✓		✓
US States	✓		✓	

# Methods of Price Regulation Used

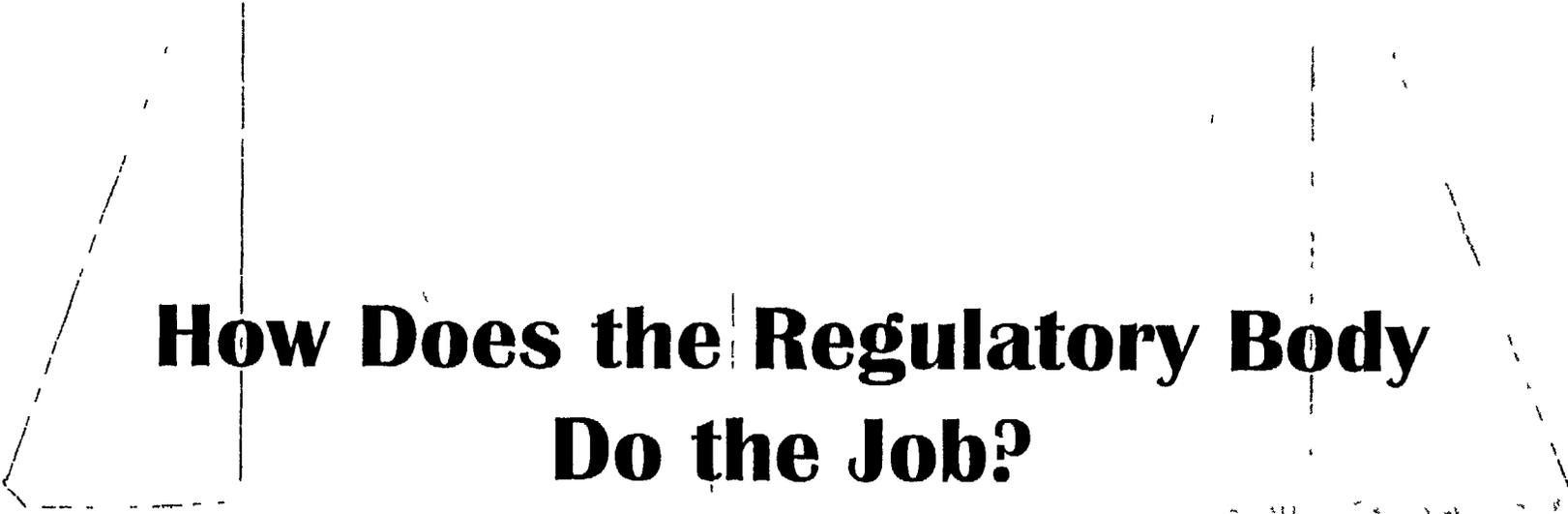
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- Denmark
  - monitoring and regulation by persuasion and negotiation with residual powers to enforce changes
  - application of detailed criteria to many entities;
- Hungary
  - no settled price regulation method in place;
- England & Wales
  - forward-looking price-cap regulation, but rate of return criteria becoming more important;
- Argentina
  - forward looking price cap but with explicit rate of return condition in law
  - indexation to US dollar rate (standard for all industries in Argentina),
- Malaysia
  - no settled price regulation method in place
- US States
  - rate of return on installed assets, but forward looking aspects important via revenue requirement and agreement on rate base

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# **IMPLEMENTING ENERGY REGULATION IN POLAND: CONCEPTS AND PRACTICES**



**How Does the Regulatory Body  
Do the Job?**

***Lawyers and Intervenors***

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***U.S.AID/Bechtel, World Bank/ESMAP***

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# HOW THE REGULATOR DOES THE JOB: LAWYERS AND INTERVENORS

- **LEGALLY DRIVEN PROCESS**
- **LEGAL INPUT (LAWYERS) ESSENTIAL**
- **LEGAL NEEDS OF REGULATORS**
  - » **Public Hearing Process**
  - » **Paper "Hearing" Process**
  - » **Establish Procedural Rules**
  - » **Timing**
  - » **Evidence**

# HOW THE REGULATOR DOES THE JOB: LAWYERS AND INTERVENORS

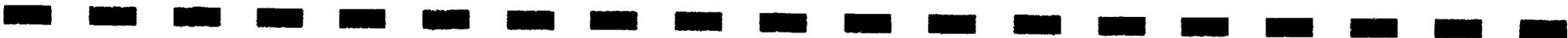
- » **Written Testimony**
- » **Oral Testimony**
- » **Intervenors**
- » **Adjudication**
- » **Contents of Written Decisions**
- » **Appeals**

# INTERVENORS

- **PUBLIC RIGHT TO PARTICIPATE**
- **HALLMARK OF OPEN, TRANSPARENT, ACCOUNTABLE SYSTEM**
- **INTERVENORS MAY REPRESENT**
  - » **Organized Customer Groups**
  - » **Industrial, Commercial, Residential Customers**
  - » **Single Ratepayers**
  - » **Environmental Groups**
  - » **Labor**
  - » **Other Public Interest Groups, NGOs**

# INTERVENORS

- **INTERVENOR ISSUES**
  - » **Price**
  - » **Licenses**
  - » **Fuel**
  - » **Line Siting, EMF**
  - » **Environmental Impacts**
  - » **Customer Credit and Shut Off**
  - » **Other**
  
- **PARTICIPATION CAN INCLUDE**
  - » **Public Statements**
  - » **Memos, Briefs**
  - » **Expert Witnesses**
  - » **Full Participation In Case As Equal Party**



# Regulatory Process Case Study: Competition versus Monopoly

- ◆ How do the stakeholders participate in the regulatory process?
  - ◆ Regulatory Authorities
  - ◆ Regulated Companies
  - ◆ Customers
- ◆ What are the perspectives of the stakeholders?
- ◆ What are appropriate regulatory approaches for resolving conflict?

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# Fundamental Principles of Competition in the Power Sector

- ◆ **Freedom to establish new companies, and one set of rules for both new and existing players**
  - ◆ independent power producers
  - ◆ marketers and suppliers
- ◆ **Choice of supplier and access to networks**
  - ◆ for distributors
  - ◆ for large industrial consumers
  - ◆ for small consumers?
- ◆ **Franchise monopolies for**
  - ◆ Local distribution companies (wires, metering, billing)
  - ◆ Transmission (planning contracting, maintenance)
  - ◆ Independent system operator, dispatcher, central buyer

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# Fundamental Principles of Competition in the Power Sector

## ◆ Regulation of

- ◆ franchise monopolies
- ◆ market power of dominant players
  - ◆ mergers and acquisitions
- ◆ security of supply
- ◆ service to “unwanted” customers
  - ◆ customers who do not pay full cost
  - ◆ customers who are more costly to serve than the class norm (e.g. rural)
- ◆ environment
- ◆ conservation

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# Regulation of Local Distribution Company Franchises: Key Issues

## ◆ Mechanism for setting base revenues

- ◆ Cost plus (“rate-of-return”)
  - ◆ Regulatory oversight of capital program
  - ◆ Regulatory oversight of expenses
- ◆ Indexed Capped Price (“RPI-X”)
  - ◆ Determining X
  - ◆ Index mechanisms for
    - ◆ Fixed costs
    - ◆ Costs per kWh sold
    - ◆ Costs per customer
  - ◆ Provision for extraordinary events

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# Regulation of Local Distribution Company Franchises: Key Issues

## ◆ Service quality

- ◆ Standards
  - ◆ quality of supply
- ◆ Incentives for Customer Programs
  - ◆ customer satisfaction
  - ◆ conservation
  - ◆ distribution losses

## ◆ Service to “unwanted” customers

- ◆ Obligation to serve
  - ◆ customers who do not pay full cost
  - ◆ customers who are more costly to serve than the class norm (e.g. rural)
- ◆ Form of subsidy for poor consumers
  - ◆ block tariffs
  - ◆ special tariff
  - ◆ direct subsidy (e.g. need-based coupon, tax relief)

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# Regulation of Local Distribution Company Franchises: Key Issues

## ◆ Differentiation in tariff schedules

- ◆ standardized national tariffs
- ◆ regional cost-based tariffs
- ◆ market-based pricing
  - ◆ potential for price discrimination

## ◆ Choice of supplier

- ◆ CHP and industrial sources
  - ◆ Pricing
  - ◆ Obligations
- ◆ Pool purchases
- ◆ Direct purchases from Generators
  - ◆ Requires open access to transmission

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# Regulation of Local Distribution Company Franchises: Key Issues

- ◆ **Taxes and Duties**
  - ◆ VAT
  - ◆ Local taxes
  - ◆ Stranded investment tax?
- ◆ **Metering**
- ◆ **Accounting requirements**

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# Tariff Transitioning: Key Issues

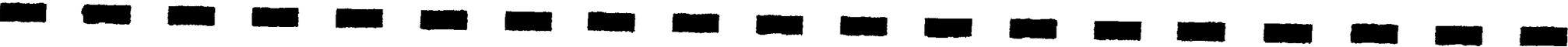
## ◆ Cost-based Tariffs

- ◆ Recovery of full cost of providing services (average cost of service)
  - ◆ Allocating shared costs to customer classes
- ◆ Marginal cost pricing for incremental consumption

## ◆ Direct and Indirect Subsidies

- ◆ Inter-generation subsidies due to current ‘low’ tariffs
  - ◆ Decapitalization of utility companies
  - ◆ Higher tariffs in the future
  - ◆ Reduced service quality in the future
- ◆ Inter-class tariff subsidies
  - ◆ Subsidy from the industrial class to the household class
- ◆ Inter-sector subsidies
  - ◆ Fuel input prices
  - ◆ CHP and industrial power purchase prices

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# Tariff Transitioning: Key Issues

- ◆ **Macroeconomic Effects of Tariff Increases**
  - ◆ Demand-side impacts
  - ◆ Industrial competitiveness
  - ◆ Inflation
  - ◆ Jobs
  - ◆ Social effects
- ◆ **Tariff Increases during Periods of High Inflation**
  - ◆ Decreasing ability of consumers to pay
  - ◆ Billing and collection complications
- ◆ **Timing of Tariff Increases to Cost-based Levels**
  - ◆ Big bang
  - ◆ Gradualism
- ◆ **Stranded Investment**

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# Inter-sector Price Distortions: Key Issues

## ◆ Efficient Pricing

- ◆ Marginal cost pricing for incremental consumption
- ◆ Price relationships for competing fuels
  - ◆ Heating (District Heating, gas, electricity, fuel oil)
  - ◆ Electricity generation (gas, coal)

## ◆ Social Objectives

- ◆ National Fuel Security
- ◆ Stimulation of the Polish Coal Industry
- ◆ Special consideration for subsistence household heating

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# Inter-sector Price Distortions: Key Issues

- ◆ Environmental “Externalities”
  - ◆ Encouraging clean fuel choices
    - ◆ Use of societal cost of pollution for decision-making
  - ◆ Emissions incentive mechanisms
    - ◆ Taxation
    - ◆ Fines for non-compliance
    - ◆ Pollution allowances
      - ◆ Allowance trading

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# The EU and energy

## Three phases of concern:

- 1 Up to early 70s, the dominant area was the coal industry under the terms of the Coal and Steel Community
- 2 From 1974 to mid-80s, the concern was supply security to offset the OPEC oil cartel
- 3 From 1988, concern has been to liberalise the internal market following the Single Market legislation in 1984



Poland has agreed to implement the original provisions of the ECSC and EC treaty relating to competitiveness and public aids beginning in April, 1997. The main impact of these are in the coal and primary gas industries.

In 1988, The Internal Energy Market was published by DG XVII of the European Commission.

Since then, the EC has been attempting to liberalise both the electricity and gas markets of the EU.

Progress in the electricity market has always been faster than in gas because of existing advantageous trading arrangements and the lack of long-term bilateral contracts.

Two EU Directives common to gas and electricity have been accepted

⇒ price transparency a requirement for suppliers to communicate their prices to the EU statistical office

⇒ transit agreements in these, owners of high tension/pressure transmission systems are obliged to facilitate the transit of electricity/gas through their system between other grid owners

These Directives would impact upon the Polish ERA after accession if the duty of overseeing these requirements was added to its responsibilities

**No big deal**

Electricity new Directive has now been agreed and will probably become law next a year

It will require EU countries to adopt a form of TPA including:

- ⇒ some form of open access for new capacity by tendering or authorisation
- ⇒ opening up market for large consumers: initially over 40GWh
- ⇒ this can be done either by “voluntary negotiated access” (VNA) or by “single buyer procedure” (SBP)

- ⇒ In VNA, suppliers and consumers anywhere in the EU conclude contracts between themselves and the power is moved over intervening grids according a published tariff. Only capacity constraints allow refusal to transport the power.
  - ⇒ In SBP, a single national entity buys the power from an EU supplier and resells it to an eligible customer. The nominated entity is obliged to cover contracts agreed between producers/customers except for capacity constraints. Again a full tariff must be published.
- Both cases, it is likely that administration of this system would fall upon the ERA. This could be a heavy task.

the situation is much vaguer as negotiations were suspended in 1994  
without agreement

EU gas industry is very rigid and dominated by a few large state-owned  
companies

However, some form of TPA is being pressed by the European Commission and  
a new draft Directive has just been issued. This resembles the Electricity  
Directive in some respects. However, it has some way to go before any  
agreement is reached and there are strong interests opposing TPA in any form

There are also powerful interests pressing for reform apart from the Commission  
including the British (now to be linked to the continental grid), the power  
companies, the Russians (!!!), and energy consultants

Problems for TPA in the gas sector include

- ⇒relatively few transmission lines compared to electricity
- ⇒trade dominated by huge long-term bilateral contracts
- ⇒market entry level is very high restricting potential players

However each of these problems is being eased

- ⇒more trunk lines are being built
- ⇒spot and short term gas is becoming available from U K and Russia
- ⇒power sector provides a baseload bulk market immediately

Ironically, the so-called Yamal line may provide a big impetus to the breakup of the old system as it could release a flood of cheap Russian gas on the lookout for a market

The regulation of gas under emerging EU rules will, ultimately, be a big responsibility for the ERA

However, as the structure of the Polish gas industry under EU rules is itself problematic, it is difficult to comment on the precise role of ERA

A final thought.

Who will regulate the regulators?

or

Will the EU eventually seek to set up a supra-regulatory body whose function is to harmonise energy regulators?

# Rationale for Energy Price Regulation

Energy price regulation is imposed to achieve:

- “Fair” prices
- Reasonable profits
- Acceptable efficiency
- Quality of service

# Criteria for “Good” Price Regulation

An effective system of price regulation will achieve:

- Cost reflective prices
- Incentives for efficiency
- Reasonable profitability
- An acceptable level of commercial risk
- Transparency
- Stability

# Method of Approach - 1

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Utilities are complex, multi-product business, with varying cost structures. Price regulation approach is 2 stage

- 1 Assess the Revenue Requirement
- 2 Set Tariffs for Individual Services

Tariffs must of course reconcile with the revenue requirement

## Method of Approach - 2

In assessing the revenue requirement, a wide range of factors need to be considered.-

- Expected output volume
- Variable costs, in particular -
  - fact
  - other consumables
  - some labour costs
- Fixed costs, in particular:
  - some labour
  - other maintenance costs
  - capital costs, in terms of depreciation and return on investment

# Method of Approach - 3

---

Capital costs often the most problematic area

Useful to distinguish between.-

- Existing assets
- Any requirement for new assets

Revenue and tariff implications may differ significantly

## Method of Approach - 4

---

Cost implications of existing assets depend on 3 factors

- Valuation
  - historic cost of asset base
  - theoretical current replacement cost
- Depreciation
  - in short-term the need for repairs and renewal is important
  - longer term, other factors such as financing implications and pricing signals are important
- Return on Capital/Financing Costs

For existing assets, servicing of existing liabilities is the main consideration

## Method of Approach - 5

---

Requirement for additional assets has clear implications for revenue requirements. Needs to taken account of:-

- Need for the asset
- Efficiency in procurement
- Asset life and depreciation policy
- Financing costs

Revenue must be adequate and secure if assets requirements are to be met

# Method of Approach - 6

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- Setting tariffs to enable revenue recovery raises different issues
- A given revenue requirement can be collected through a variety of tariff structures
- Preferred tariff structures taken account of -
  - equity, with consumers paying for what they get,
  - reliable revenue recovery, reflecting fixed and variable costs,
  - system expansion costs, with price signals reflecting long-run marginal costs of the system.
- Tariffs operating as realistic price signals for consumers and utilities are vital for the long-term development of the industry

# Alternative Systems of Price Regulation (1)

Systems commonly discussed are:

- Rate of return regulation
- Price ceilings (RPI - x)
- Others, such as yardstick regulation or benchmark regulation

# Alternative Systems of Price Regulation (2)

They are similar, as all must consider *income* and *tariffs*.

They differ in that they provide:

- Varying levels of commercial risk
- Different incentives for efficiency

# Possible Price Regulation Solutions (1)

For electricity, generation, transmission, and distribution clearly need separate treatment, depending on the final structure.

## *Generation*

- regulating generation costs is difficult, because of variable fuel costs and load factors
- power pooling or competitively tendered contracts, or some combination of both, offers the best approach
- pooling of procurement entity should be regulated on processes and financial position

5.1 x

13

# Possible Price Regulation Solutions (2)

## Electricity, cont.

### *Transmission*

- stable cost base makes this sector easy to regulate
- RPI-X or RoR can be applied, but attention needs to be paid to incentives for optimum expansion, and economic and secure operation

### *Distribution*

- distribution per se can be regulated in a similar way as transmission
- supply activity can be regulated with generation, transmission, and distribution costs as allowed expenses

# Possible Price Regulation Solutions (3)

For gas, the central issue is the purchase cost of gas and how it is dealt with in price regulation

- gas transmission costs, as in the case of electricity, are relatively stable and can be regulated through RPI-X or RoR
- gas purchase costs are very difficult to deal with on a justified cost basis, and should be handled separately input costs to the distribution business

*Gas purchase costs* can be dealt with on an arm's-length basis, through

- establishing “commercial” contracts for all existing gas purchases by the distribution business
- providing that all future gas purchases should, as far as possible, be on a competitive basis

# Transitional Issues (1)

Progress towards a stable regulatory framework depends on overcoming transitional problems.

Chief transitional problems are.

Accurate identification of the economic price level

- A realistic path to achieve that level

# Transitional Issues (2)

Accurate identification of the economic price level requires:

- detailed cost analyses and projections, enterprise by enterprise
- forward-looking assessment of capital requirements

This is a complex undertaking, but manageable.



## Transitional Issues (3)

Charting the *path* to “economic” levels is dependent on

the scale of the identified gap

- the underlying role of inflation

social and political pressures

Uncertainties in all three factors suggest this is significantly more difficult than long-term price regulation.

# Transitional Issues (4)

Subsidies required during the transition period should ideally take account of:

- the over-riding need for transparency in subsidies
- the desirability of “economic” tariffs, with separate subsidies

A fall-back option of *transparent* subsidies directly to enterprises would

- ensure full revenue recovery by enterprises, *but*
- the reduced level of some tariffs gives distorted signals to consumers

6.4

**ENERGY RESTRUCTURING GROUP  
JACHRANKA TRAINING CENTRE  
POLAND**

**23 October 1996**

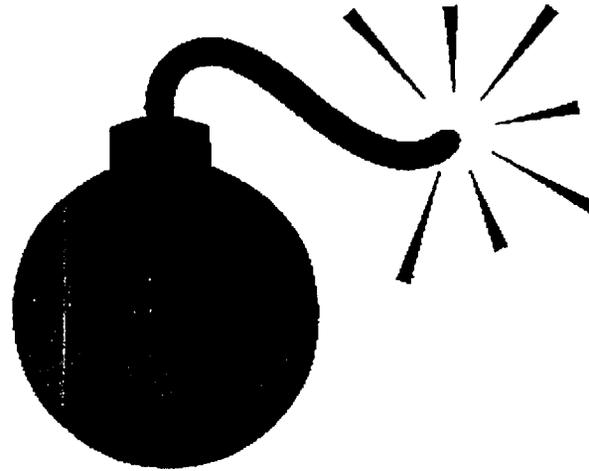
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# THE "BIG BANG"



## HUNGARY: A CASE STUDY IN PRIVATIZATION AND REGULATORY REFORM

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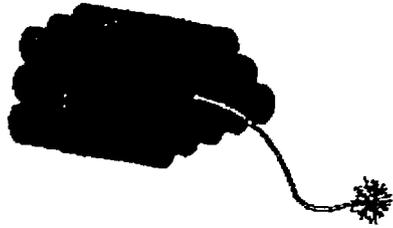
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# I. THE FUSE: PRE-"BANG" ECONOMIC AND POLITICAL FACTORS

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- **NEED FOR CAPITAL**
    - » Investment in energy sector
    - » For state budget
  - **DESIRE FOR DEMOCRATIZATION**
  - **DESIRE TO RETURN ECONOMY TO PRIVATE OWNERSHIP**
  - **LOOK TOWARD THE WEST**
    - » Competition
    - » EU
    - » Strategic partners
- 
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# I. THE FUSE: PRE-“BANG” TECHNICAL FACTORS

---

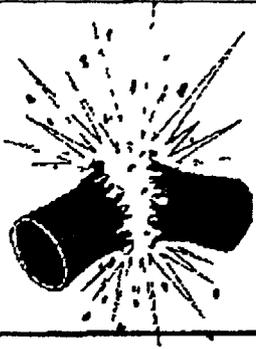
- **FUEL SUPPLY**
    - » **Lignite**
    - » **Nuclear**
    - » **Little domestic natural gas**
    - » **Few hydro resources**
  
  - **GRID CONNECTIONS**
  
  - **DISTRICT HEAT**
  
  - **MANAGEMENT SKILLS**
- 
-



# I. THE FUSE: PRE-"BANG" PRICING FACTORS

---

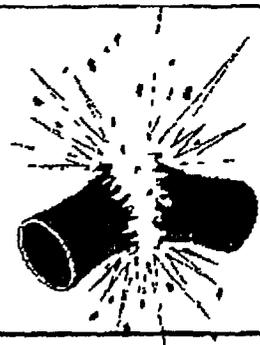
- **SUBSIDIZATION**
    - » **Industrial - residential - commercial**
    - » **Electricity - heat**
  
  - **NO TRANSPARENCY**
    - » **In price-setting process**
    - » **In price result -- lack of separate accounting**
  
  - **NOT COST-BASED**
    - » **No depreciation**
    - » **No marginal cost or least cost concepts**
- 
-



## II. "BOOM": SUMMARY

---

- **AGGRESSIVE PRIVATIZATION -- "JUST DO IT" ... AND THEY DID**
  - **SIGNIFICANT DISAGGREGATION -- THROUGH PRIVATIZATION AND LEGAL LIMITS**
  - **RE-STRUCTURED LEGAL AND REGULATORY ORGANIZATION -- FROM PARLIAMENT TO HEO**
- 
-



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## II. "BOOM": PRIVATIZATION

---

- **SCHEDULE**
    - » **The first round - the fuse sputters**
    - » **The second round - the fuse lights**
    - » **Later sales/future sales**
  
  - **PARTICIPANTS**
    - » **APV**
    - » **Bidders**
    - » **HEO involvement (second round)**
    - » **Schroeders (second round)**
  
  - **SALES PRICES -- IN EXCESS OF BOOK**
- 
-

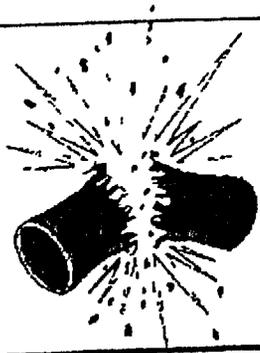


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## II. "BOOM": UNIQUE ISSUES

---

- MVM
  - NUCLEAR
  - TIE-INS
    - » Good plant with bad
    - » New capacity
    - » Mines
  - THE SALESMAN'S FACTOR
    - » Industrial plants
    - » Promised expansions
- 
-



## II. "BOOM": DISAGGREGATION

- **SEPARATION OF GENERATION, TRANSMISSION AND DISTRIBUTION**
  - » Sold separately; bidding limits in second round
  - » MVM must sell remaining generation
  - » Limits on distribution companies
  - » Nuclear
  - » Municipalities
  
- **CURRENT OWNERSHIP LIMITATIONS**
  - » Monopoly law
  - » Licenses
  - » Proposed specific limitations: tender process, share ownership

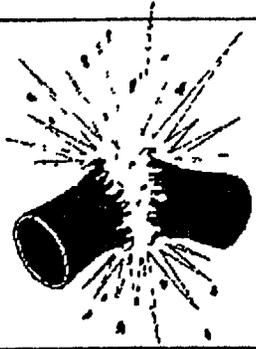


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## II. "BOOM": LIMITS ON COMPETITION

---

- **NO THIRD PARTY ACCESS**
    - » Monopoly distribution
    - » Except limited "direct supply"
    - » Forced purchase by MVM or distribution companies of renewables, CHP
  
  - **CENTRALIZED STATE RESOURCE PLANNING**
  
  - **REGULATED PRICES**
    - » Wholesale
    - » Retail
    - » Inability to contract
- 
-



---

## II. "BOOM": LEGAL AND REGULATORY STRUCTURE

---

- **GOVERNING LAWS**
    - » **No New Constitution Yet (in the Works)**
    - » **Electricity Act**
    - » **Pricing Acts**
    - » **Government Decrees**
    - » **Ministerial Resolutions**
    - » **Operational Code**
    - » **Licenses**
    - » **Individual HEO Resolutions**
    - » **Environmental**
    - » **Labor**
- 
-



---

## II. "BOOM": LEGAL AND REGULATORY STRUCTURE

---

- **GOVERNING BODIES**
    - » **Parliament**
    - » **Government (cabinet)**
    - » **MOIT**
    - » **MOF**
    - » **HEO**
    - » **Environmental**
    - » **Public/NGOs**
      - › **Consumers' interest group**
- 
-



---

## II. "BOOM": ROLE OF THE HEO - OFFICIAL

---

- LICENSING
  - PRICING
  - CONSUMER PROTECTION
  - RESOURCE AND CAPACITY PLANNING
  - ENFORCEMENT
- 
-

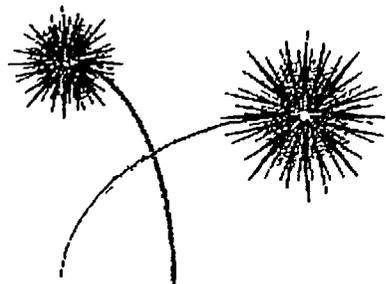


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## II. "BOOM": ROLE OF THE HEO - PRACTICAL

---

- **VOICE FOR COMPETITION**
    - » **Tender process**
    - » **License terms on ownership limitations**
  
  - **VOICE FOR STRONG, INDEPENDENT REGULATOR**
    - » **Important role in tender process/selections**
    - » **Full exercise of existing powers, with limited resources**
    - » **Without centralized planning of private transactions**
    - » **Big picture view**
  
  - **CONSULTED BY OTHERS IN AREA OF EXPERTISE**
- 
-

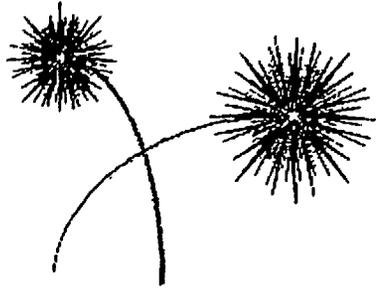


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### III. POST-“BANG”: IMPLEMENTATION ISSUES

---

- **PRICING – TENSION BETWEEN**
    - » Price rationalization and social costs
    - » Price rationalization and inflation
  
  - **RE-AGGREGATION**
    - » Natural tendency without constraints - e.g., UK
    - » Foreign buyers
  
  - **DISPATCH ISSUES**
  
  - **DEVELOPING NEW CAPACITY**
    - » Security of supply
    - » Current pricing questions
- 
-

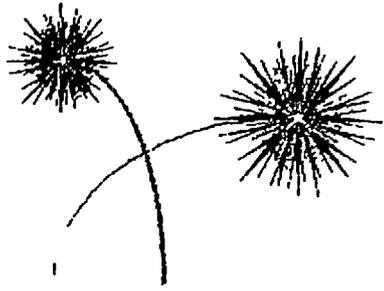


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### **III. POST-“BANG”: LESSONS FOR POLAND?**

---

- **SUCCESS OF PRIVATIZATION**
  - **IMPACT OF NO THIRD PARTY ACCESS**
  - **LIMITATIONS ON HEO AUTHORITY**
    - » **Individual decisions without general application**
    - » **Funding and hiring constraints**
    - » **Pricing -- investor confidence**
  - **CHP, OTHER PREFERENCE LOOPHOLES**
  - **STRIKE LAWS**
- 
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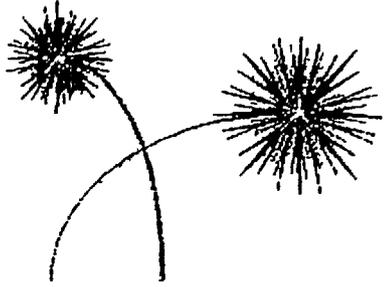
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### **III. POST-“BANG”: ROLE OF THE REGULATOR**

---

#### **Why is Independence Good?**

- **CONSUMER CONFIDENCE**
  - **INVESTOR CONFIDENCE**
  - **DEFENSE OF COMPETITION, PRICE EFFECTS**
  - **STABILITY AND PREDICTABILITY**
  - **FAIRNESS**
    - » **Public perception**
    - » **Transparency**
- 
-



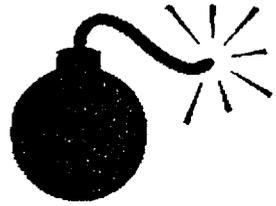
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### **III. POST-“BANG”: ROLE OF THE REGULATOR**

---

#### **How Do You Support Independence?**

- **SELF-FUNDING AND ADEQUATE BUDGETS**
  - **PROTECTION FROM POLITICAL MISCHIEF -- FIXED TERMS**
  - **DEVELOPMENT OF REQUIRED SKILLS (ECONOMIC, ENGINEERING, LEGAL, MANAGEMENT)**
  - **POWER TO ISSUE GENERAL DECREES**
- 
-



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## **IV. THE "BIG BANG": CONCLUSIONS**

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- **EFFECTIVE REGULATION/COMPETITION KEY TO  
SECTOR REFORM**
  - **CLEAR LEGAL BASIS FOR STRONG, INDEPENDENT  
REGULATOR**
  - **MOVE QUICKLY, DECISIVELY**
  - **LEADERSHIP SKILLS, CAPABLE STAFF CRUCIAL TO  
SUCCESS**
- 
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# I. LEGAL FRAMEWORK IS TOOL TO IMPLEMENT POLICIES OF GOVERNMENT OF POLAND

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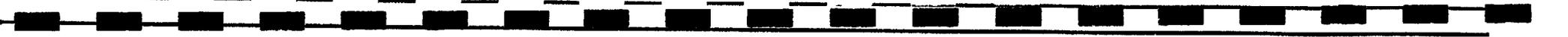
- POLICY CHOICES DRIVE LAW, NOT VICE VERSA
- GOP POLICY GOALS FOR ELECTRIC SECTOR
  - » Increase Efficiency
  - » Reduce Costs
  - » Meet Demand

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## II. HALLMARKS OF AN EFFECTIVE LEGAL AND REGULATORY FRAMEWORK

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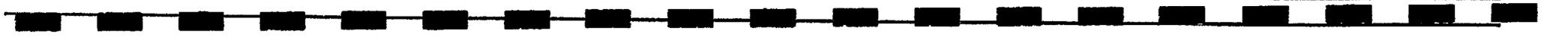
- **INTERNALLY CONSISTENT**
  - » **Balance Obligations with Authority**
  - » **Balance Duties with Rewards**
  - » **Balance Market Pricing Forces with Open, Effective Markets**



## **II. HALLMARKS OF AN EFFECTIVE LEGAL AND REGULATORY FRAMEWORK**

---

- **CONSISTENCY WITH OTHER LAWS**
  - » **Environmental**
  - » **Financial, Commercial**
- **PROMOTE OVERALL NATIONAL POLICIES**
  - » **Private Investment**
  - » **National Energy Security Issues**



## II. HALLMARKS OF AN EFFECTIVE LEGAL AND REGULATORY FRAMEWORK

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- **CLARITY**
  - » Standards are Specific and Understandable
- **TRANSPARENCY**
  - » Open Process, Participants Can Be Heard
- **PREDICTABILITY**
  - » Outcomes Generally Consistent

### III. LAWS vs. REGULATIONS

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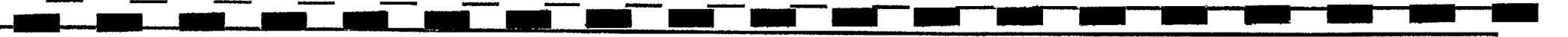
- **ENABLING (OR PRIMARY) LEGISLATION -- (WHO DOES WHAT)**
  - » **Defines General Parameters, Establishes Overall Authority**
- **REGULATORY AUTHORITY AND PROCESS (HOW IS IT DONE)**
  - » **Follows Substantive Criteria; Functions in Open, Predictable, Reviewable Manner**



### **III. LAWS vs. REGULATIONS**

---

- **COMMERCIAL STRUCTURE -- (HOW PRIVATE PARTIES PARTICIPATE)**
  - » **Facilitates Commercial And Investment Expectations**
- **ANTI-MONOPOLY -- (HOW TO KEEP A COMPETITIVE MARKET COMPETITIVE)**
  - » **Prevents Anti-Competitive Behavior in Markets**



### **III. LAWS vs. REGULATIONS**

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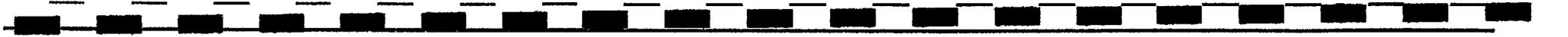
- **LAWS ADDRESS BROAD POLICY ISSUES**
  - » **Markets vs. Regulation**
  - » **Franchises vs. Competition**
  - » **Cost Based Pricing vs. Incentives**
  - » **Delegation to Managers vs. State Oversight**
  - » **Transitional Considerations vs. Long Term Strategies**

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### **III. LAWS vs. REGULATIONS**

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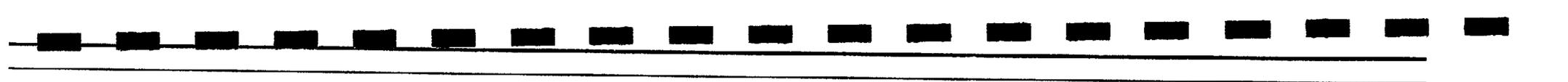
- **DELEGATE TO REGULATORS**
  - » Implementation of Policy
  - » Transitional Issues
  - » Decisions within Expertise of Regulator
- **CHANGE IN LAWS GENERALLY MORE SIGNIFICANT THAN CHANGE IN REGULATORY DECISIONS**
- **POWER OF REGULATOR (APPOINTED) SHOULD ONLY FLOW FROM LEGISLATURE (ELECTED)**



### III. LAWS vs. REGULATIONS

---

- **PARLIAMENT, GOVERNMENT AS CHECK ON REGULATOR**
- **JUDICIAL PROCESS AS CHECK ON REGULATOR**
  - » **Adherence to substantive standards**
  - » **Procedural rights**
  - » **Not exceed delegated authority**



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**24 October 1996**

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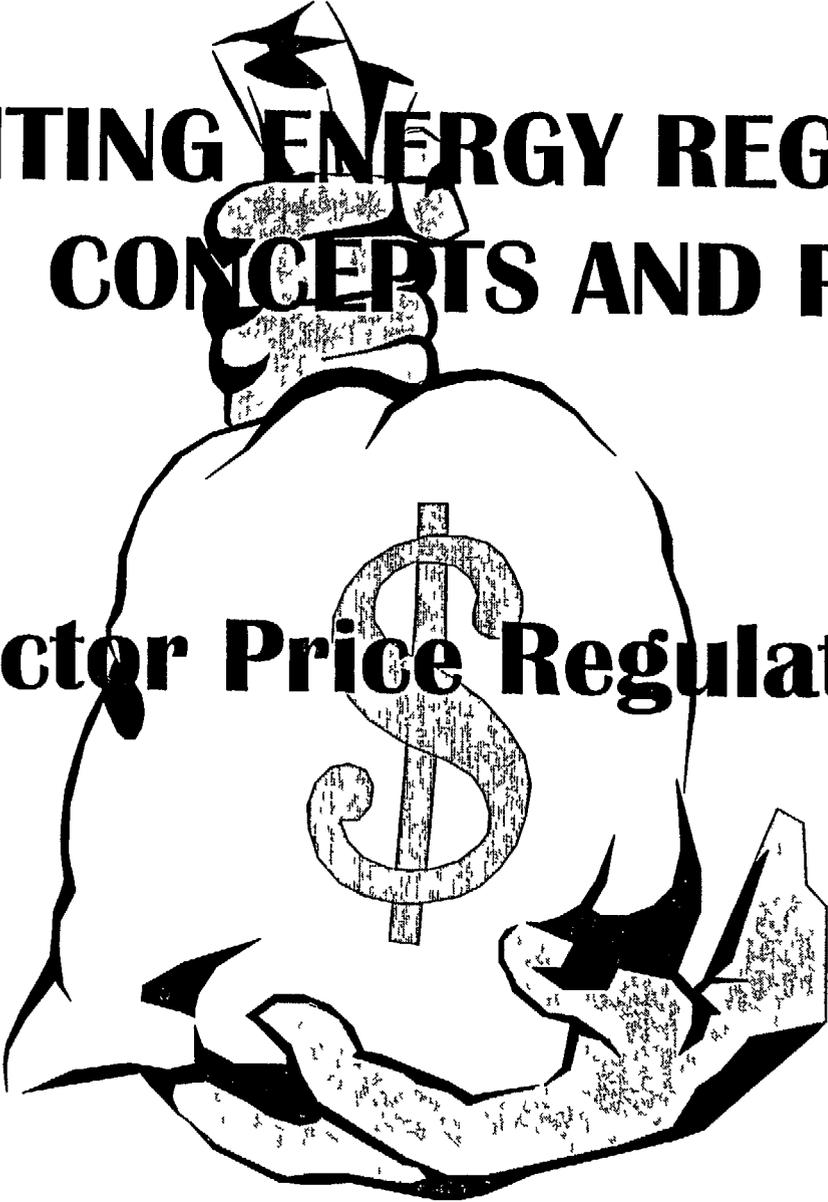
***U.S.AID/Bechtel, World Bank/ESMAP***

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# **IMPLEMENTING ENERGY REGULATION IN POLAND: CONCEPTS AND PRACTICES**



## **Sector Price Regulation**

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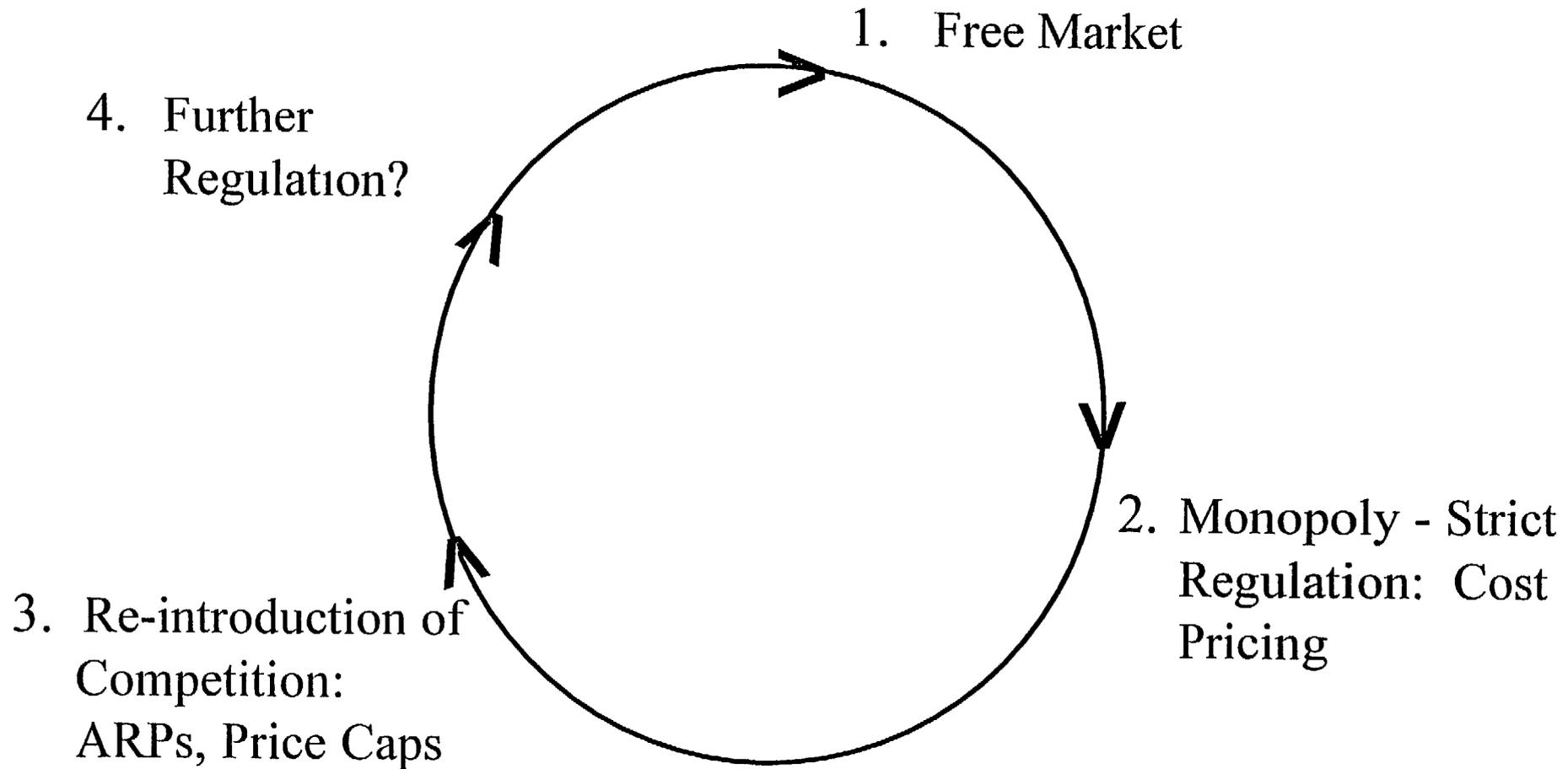
*U.S.AID/Bechtel, World Bank/ESMAP*

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# I. PRICE CYCLES

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*Poland: ERG*

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## II. SOME “BIG-PICTURE” PRICING QUESTIONS:

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- IS PRICE CYCLING INEVITABLE?
- IS “COST-BASED” PRICING EVER REALLY COST-BASED?
- DOES MARKET-BASED PRICING LOWER PRICES?
- IS THE REGULATOR’S ROLE EVEN GREATER IN MARKET-BASED VS. COST-BASED PRICING ENVIRONMENT?
- HOW DO YOU PRACTICE DSM WITH MARKET-BASED PRICING?

# III. IS “COST-BASED” PRICING EVER REALLY COST-BASED?

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- POLITICAL INFLUENCES
  - » Residential Class Votes
  - » Industrial Class Has Money, Influence and Jobs
  - » Commercial Class Is Squeezed
- NEVER TOTAL MONOPOLY
  - » Self-Generation
  - » DSM
  - » Change Fuel Source
  - » “Across the Fence” TPA
- NEVER INCLUDES ALL COSTS -- ENVIRONMENTAL EXTERNALITIES, SOCIAL COSTS

# IV. DOES MARKET-BASED PRICING LOWER PRICES?

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- LOWERING PRICES OVERALL VS. CREATING DIFFERING PRICES
- EFFECT ON OVERALL, AVERAGE PRICE
  - » UK, US Telephones
  - » Impact of New Entrants

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# IV. DOES MARKET-BASED PRICING LOWER PRICES?

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- EXPERIENCE IN ULTIMATE PRICES
  - » U.S. Telephone -- Price Similarity Among Competitors
  - » U.S. Result Makes Sense
  - » Difference Lies in Service, Marketing
  - » After Herd Thinned, Is Rest of Pack Fungible?
  - » New Entrants
  
- IMPACT OF MARKET-BASED PRICING ON FUEL SECURITY
  - » Immediate vs. Temporary Impacts
  - » How Important for Poland?

# V. IS THE REGULATOR'S ROLE EVEN GREATER IN A MARKET-BASED VS. COST-BASED PRICING ENVIRONMENT?

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- ROLES
  - » Cost-Based Environment -- Oversight of Tariff Proposals and Back-up Information
  - » Market-Based Environment -- Referee, Anti-Monopolist
- IS ONE ROLE LESS DIFFICULT OR TIME-CONSUMING?
- IS STRENGTH AND INDEPENDENCE REQUIRED FOR THE REGULATOR IN BOTH?

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## VI. HOW DO YOU PRACTICE DSM WITH MARKET-BASED PRICING?

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- DOES MARKET PRICING ENCOURAGE EFFICIENT OR EXCESSIVE USE?
- DO WE CARE ABOUT DSM? WHY?

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*Poland: ERG*

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## MEMORANDUM

To Chris Turner  
From Marek Grzybowski  
Date October 29, 1996  
Subject Jachranka Seminar Feedback Report

On October 21- 24, USAID Bechtel/Poland team--Chris Turner, Mirek Duda, Marek Grzybowski, and Agnieszka Sosulska, supported by Tom Simpson, Bechtel, USA--and presenters from the US, UK and Poland organised and delivered a 3-day seminar Implementing Energy Regulation in Poland-- Concepts and Practices The training program was primarily addressed to the members of the Working Group for the Establishment of the Energy Regulatory Authority, and secondly to the representatives of the regulated companies as well as representatives of consumer groups Support for the program was given in remarks by Dir Andrzej Pierzak of MoIT, Peter Amato of USAID, and Christian Duvigneau of the World Bank

The following report is a summary of comments received by means of a feedback questionnaire, as well as some remarks collected in personal talks The detailed agenda with a specification of speakers is attached

### Participants

The sessions were attended by a total of 60 people, of which about 2/3 were accommodated at Jachranka and 1/3 commuted from Warsaw Unfortunately, a meeting of the Energy Law Joint Commission, unexpectedly postponed from earlier date to October 23 and 24, resulted in the absence of a few important participants on the second and third day of the training Otherwise, attendance was reasonably consistent throughout

The following table presents the composition of Jachranka participants

Organisation	Head count
Ministry of Industry and Trade, Ministry of Planning	11
Power distribution companies	6
Power plants and CHPs	4
Consulting organisations	4
Consumers' Federation and other representatives	2
Polish Power Grid Company	5
Polish Oil and Gas Company	2
The Board of Oil Industry	2
Antimonopoly Office	2
Municipal authorities	1
Energy Restructuring Group	8
World Bank/USAID observers	3
Lecturers	7
Interpreters	2
Total head count	60
Organisers and Observers	21
Trainees	39

### Feedback Questionnaire

Near the end of the program, each trainee was asked to fill out a feedback questionnaire. Of the 39 trainees, we received 24 questionnaires back, or 62%

The following table summarises the answers which may be quantified. The figures represent the number of respondents to each question. The figures in brackets show the percentage of respondents.

Evaluation	Excellent	V good	Good	Mediocre	Poor
Trainees' expectations met	2 (8%)	16 (67%)	6 (25%)		
Detail of the presentation		13 (54%)	9 (38%)	2 (8%)	
The scope of the information		21 (88%)	3 (12%)		

### The most interesting subjects

Most of the trainees scored highly the very practical approach to regulatory issues, especially the presentations of Carl McDermott, the Illinois State Commissioner.

- "Organisation and Structure of the Regulatory Authority in the US and Elsewhere" - 11 mentions, and
- "What the Regulatory Authority Does" - 10

Some other subjects mentioned by trainees

- "Overview of the Regulatory Process" - 3
- "Price Regulation" - 3
- "Hungarian Case Study" - 3
- "Other countries experience" - 5
- "Key Problems of Regulation in Poland" - 2

### Subjects of no interest (found improper)

Very few respondents found improper or uninteresting subjects at our seminar. Some of the comments included here concerned

- "Price Regulation" - 2 respondents considered that this subject should be moved and expanded in the next seminar,
- "Regulatory Experience in Malaysia and Argentina" - 2 respondents pointed out that the experience of such countries is too exotic and the presentation should be more focused on EU countries.

### Subjects that should have been included

The training program to a large extent met the participants' expectations, therefore not many respondents had complaints as to subjects that should have been included. Two participants expected a separate presentation on licences, one wanted a presentation on district heating regulation, and another expected a workshop on utility price making. Two believed that we covered probably too many subjects, while four thought that the seminar should have included even more detailed proposals, and six wanted more emphasis on working solutions for Poland. In that light, the Hungary case study was seen as useful for comparisons with Polish conditions.

### Organisational Comments

The trainees either had good comments or expressed no complaints about the organisation of the seminar, handout materials and accommodations. Two respondents would like better translation, two complaints concerned the hotel and meals, one did not like the evening session and wanted longer breaks.

### Next Steps

Several participants, including the MoIT liaison, expressed a desire for additional training as soon as the next program can be developed. Additional specific-to-Poland price regulation training is of considerable interest, the group was aware that the introductory material on price regulation is to be supplemented in a second program. One suggestion was for an early session on licenses. The overall need appears to be for more practical training in ways that relate to the likely course of regulatory/utility relationships once the ERA is established, with the interim seen as a time for elevating participants' knowledge and skills.