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# ENERGY REGULATORS REGIONAL ASSOCIATION

*Legal Regulation Working Group*

*Issue Paper*

# REGULATORY INDEPENDENCE

*PREPARED BY*

KEMA International B.V.

November 2008



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## **REGULATORY INDEPENDENCE**

**ERRA Legal Regulation Working Group**



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Prepared by



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November 2008

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# 1 Executive Summary

KEMA has been commissioned by ERRA to draft and complete an issue paper on Regulatory Independence. This paper reflects the predominant features of independence of ERRA members' respective regulatory bodies. It also identifies best practices based on international experience and provides recommendations for the ERRA members to operate and function independently.

For this assignment KEMA prepared and sent out a questionnaire to all ERRA members covering the following main areas of independency: political, legal, sociological and financial independence and transparency.

Independent regulators are important because they can limit political interference in business decisions which minimizes regulatory risks. This regulatory role is particularly important given the nature of regulation in the energy sector. The gas, electricity and heat sectors are capital intensive and characterized by long term asset life. These industries are essential for the overall economic development of the country and require a predictable and credible regulatory regime.

## Political independence

In order to assess political independence it is essential to understand the regulator's role in relation to ministries and political executives as well as other stakeholders.

Separating regulators from ministries, giving them more autonomy and responsibility for regulatory tasks, and holding them accountable for their performance should improve efficiency and better regulation.

## Legal independence

The independence of a regulator may be formally established in legislation and usually refers to the objectives, functions, duties and powers that a regulator possesses, as well as, rules on appointment, decision-making structure and dispute resolution.

Therefore, a key feature of independent decision making is a robust legal framework governing regulated activities and their associated objectives, principles and values, including the legal basis for adequate and stable financing of regulated activities and a constitution governing appointment and conduct of business.

## Sociological independence

Regulatory independence also depends on the acceptance of the regulator's authority and its credibility in the eyes of the public, industry, and stakeholders. As perceptions regarding fairness and transparency of the regulatory process influence public acceptability of the regulatory system, the key is to communicate with various stakeholder groups. This leads to the necessity to design and implement a structured public relations strategy where appropriate.

### Financial independence

A regulator's effectiveness is determined largely by the adequacy of its resources, both human and financial. Insufficient financial resources may compromise the ability of the regulator to carry out its tasks, while too many resources may result in a lack of focus in regulator activities.

In general, competitive level of salaries, other social, and/or educational benefits, and good working environment are essential to attract, develop and retain highly qualified staff. This will enable the regulator to be competitive with the other companies in the energy industry.

### Transparency

Transparency may be defined as the way the regulators communicate and exchange information and how the regulatory process is conducted. Good communication, well organised and consistent consultation, access to relevant documents and information and accountability through appeal mechanisms are key features of a transparent regulatory process.

In terms of accountability the regulatory authorities need to carry out appropriate reports on performance. The regulator should be exposed to the stakeholders, and held accountable in this in its decision-making. Moreover the regulators should be held accountable before government or parliament for the utilisation of the agreed budget.

The abovementioned dimensions of regulatory independence are linked together and usually overlap with each other. There is no fine line to separate these factors completely from one another.

Regulatory authorities in the ERRA countries face some constraints that influence its ability to function effectively. This typically includes funding limitations, partial lack of legal independence, in some cases environment characterised by political instability and absence of stakeholder support, and inherited problems from the past. Therefore, the best practices based on international experience should be not mechanically transferred to each of the ERRA countries. Differing conditions within the region require individual approaches towards the implementation of the suggestions, providing the countries with the flexibility to incorporate these standards according to the country-specific prevailing conditions.

## 2 Introduction

The Energy Regulatory Regional Association (ERRA) integrates 24 regulatory authorities as Full Members, 2 as Associate and 4 Affiliate Members in the region of Central and Eastern Europe and Central Asia. KEMA is assisting ERRA's Legal Regulation Working Group in drafting and completing an issue paper on Regulatory Independence.

The objective of this paper is to provide ERRA members with a closer look into regulatory independence in terms of political, legal, sociological and financial independence and transparency. This paper highlights the main factors that influence these areas, identifies good practices and measures, and makes recommendations for minimizing interference and for effective regulatory performance. This paper also describes best practices in the foregoing areas based on international experience.

In the course of the project work KEMA prepared and sent out a questionnaire to all ERRA members in order to gain a deeper insight into the predominant features of independence of members' respective regulatory bodies. The questionnaire includes questions on the degree of separation and independence of the regulatory authority based on the five areas mentioned above. Please refer to Appendix 3 for the questionnaire. The responses from the questionnaire provide a valuable source of information that is considered in our conclusions and recommendations.

In this paper we emphasize electric and gas regulation including all the dimensions of regulatory independence. The remainder of this issue paper is set out as follows:

### Chapter 3: General Introduction to Regulatory Independence

This chapter will explain the general meaning of regulatory independence and define the major dimensions of independence. The next sections will focus in detail on each of the defined dimensions.

### Chapter 4: Political Independence

In this chapter we discuss how government and parties who lobby the regulatory authority may have an influence on regulatory decision making. In addition, discussion on the influences from stakeholders will also be presented.

### Chapter 5: Legal Independence

This chapter considers the independence a regulator has depending on laws governing the regulatory process, and discusses specific statutory provisions in terms of the role, duties and powers they bestow on the regulator.

### Chapter 6: Sociological Independence

This chapter discusses the legitimacy and acceptance of a regulator's authority and whether the regulator has sufficient credibility in the eyes of the public, industry, and stakeholders.

### Chapter 7: Financial Independence

In this chapter, we present the type of funding a regulator has and the regulator's financial autonomy in decision making. Additional considerations include the level of expertise and human resources available to the regulator.

### Chapter 8: Transparency issue

This chapter explains the importance of transparency and the most common measures available to enhance transparency. It also looks at obstacles that may potentially constrain regulatory transparency.

In addition, this chapter introduces the concept of accountability, explains the relationship between independence, accountability and transparency and presents a number of mechanisms designed to make regulators accountable in their decision-making.

### Chapter 9: Summary of Questionnaire results

The results of the KEMA questionnaire are summarised by country, based on the feedback received.

### Chapter 10: Conclusions and Recommendations

This chapter looks at how ERRA members can improve their levels of regulatory independence based on the findings from the questionnaire as to the issues that affect the autonomy of the regulators. We also make recommendations and suggest best practices so that regulators can operate more independently of political, legal, sociological and financial pressures.

At ERRA's request, in our recommendations we also take into account the results of two additional surveys: "Regulatory Benchmarking Report for the CIS" and "Regulatory Benchmarking Report for South East Europe". These two surveys are briefly summarised in Appendices 1 and 2.

The appendices are as follows:

Appendix 1: "Regulatory Benchmarking Report for South East Europe"

Appendix 2: "Regulatory Benchmarking Report for the CIS"

Appendix 3: Questionnaire on Regulatory Independence

Appendix 4: Questionnaire Responses Graphs

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Appendix 5: Questionnaire Responses (included in a separate document)

### **3 General Introduction to Regulatory Independence**

This section introduces the background and establishment of regulatory authorities. It summarizes the roles and tasks and highlights the development and evolution of regulatory authority in various countries. It also describes the importance of regulatory independence and the essential factors that are required to ensure an effective regulatory system.

#### **3.1 Background and the Role of the Regulator**

Most regulatory authorities in the energy industry were established as a result of reform (e.g. restructuring, privatization, liberalization of the electricity and gas market) and legislation. The main purpose of establishing regulatory authorities was to regulate the monopolistic areas of electricity and gas activities and to promote competition in generation and supply activities. One of the main arguments in favour of regulation is the role of regulators in correcting market failures (e.g. natural monopolies, externalities) (Larson et al 2004). The existence of market failures such as the presence of natural monopolies in transmission and distribution networks requires the existence of an independent party - i.e. a regulatory authority - ensuring that all competitors have access to networks and resources are spent in an efficient way to provide quality of supply at reasonable prices to consumers.

Even where regulatory authorities<sup>1</sup> are already established (such as in Canada and the USA) their roles and functions have been extended to areas related to the introduction of competition due to regulatory reforms.

The following presents the differing roles of regulatory authorities among various countries.

In the USA the aim of introducing regulatory authorities for utility regulation is to protect consumers from vertically-integrated monopolies. Therefore, the critical feature of independence is the independence from the utilities and the avoidance of regulatory capture<sup>2</sup> by them.

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<sup>1</sup> Regulatory Authority is known as Utilities Commissions in the USA.

<sup>2</sup> In this context, regulatory capture means that it is in the private interest of a regulatory authority to allow regulatory programs to reflect the interest of powerful utilities.

In OECD countries<sup>3</sup> the move to establish independent regulatory authorities can be justified on the grounds of consumer welfare and regulatory quality through better governance. The goal should be the development of a regulatory system that balances the powers of ministries / government and the interest of consumers and operators in the energy sector.

In contrast, in emerging market economies (such as Asia, Latin America, Central and Eastern Europe), one of the main objectives is mitigating regulatory risk<sup>4</sup> for investors. Through independent regulators investors (in particular foreign investors) should be assured that they can expect to earn a reasonable rate of return. Hence, in emerging market economies the key aspect of independence is independence from government intervention (Stern 1997).

### **3.2 Independent regulatory authority: an institutional model for regulation**

Creating and sustaining an effective regulatory system depends on effective regulatory governance. Regulatory governance is concerned with the institutional environment and the processes of regulatory decision-making. Eberhard (2006) specified the following governance elements that are required to ensure an effective regulatory system:

- Regulatory commitment,
- Clarity of roles and functions between the regulator and policy makers,
- Regulatory autonomy,
- The organizational structure and resources of the regulator, and
- Issues such as transparency, participation, accountability, predictability, proportionality and non-discrimination.

Different combinations and degrees of such elements result in different regulatory models such as:

- Direct regulation by government,
- Regulation by independent regulatory authorities,

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<sup>3</sup> Currently the OECD has 30 member countries including countries from Western Europe, Scandinavia, Australia, Japan, and USA. For a full list please refer to [www.oecd.org](http://www.oecd.org).

<sup>4</sup> Regulatory risk: a change in the law or in regulations that can directly affect the regulated company's cost of capital and lead to inefficient investment.

- Regulation by contract, and
- Out-sourcing of regulatory functions to third parties.

These options are not mutually exclusive and often coexist. The choice of regulatory model should fit the political, constitutional, and legal arrangements of individual countries. However, a high level of regulatory commitment, competent institutions and human resources capacity are pre-conditions for the success of any independent regulator. In addition, some regulatory functions may be contracted out if it is seen as cost effective.

### 3.3 Importance of regulatory independence

In the literature several arguments are presented in order to explain the significance of regulatory independence. For example (Larson et al 2004) states the basic idea behind the creation of independent regulators is their ability to minimize government failures.

Independent regulators can limit political interference in business decisions and minimize regulatory risks. This regulatory role is particularly important given the technical nature of regulation in the energy sector. The gas, electricity and heat sectors are characterized by long term large capital intensive investments that require a stable regulatory regime. In other words, short term political events and political cycles should not interfere with the regulatory framework, which should remain consistent and stable over time.

Separating regulators from ministries, giving them more autonomy and responsibility for regulatory tasks, and holding them accountable for their performance should improve efficiency and produce better regulation.

#### **Example: Creating incentives for cost reduction**

The United States (US) has had Independent Regulatory Commissions for more than a hundred years. In the 1980s, the United Kingdom and Chile introduced such agencies as part of sector reform and privatization initiatives.

Typically, Independent Regulatory Commissions in the US adopted rate of return regulation complemented with management audits to promote efficiency. Conversely, the United Kingdom and Chile's regulators introduced incentive regulation (e.g. price caps) rather than rate of return regulation creating incentives for cost reduction but at the same time maintaining a certain level of quality of supply. Studies show improved regulatory incentives have contributed to substantial savings as regulated companies have incentives to reduce costs given mandated

quality and reliability standards.

Source: Berg et al (2000)

Independent regulation is preferred regardless of one's perspective, as we describe below.

- Independent regulation may be motivated by social fairness and redistribution concerns. This occurs when the regulator acts in the interest of consumers to protect them against (for example) price discrimination.
- Externalities such as environmental problems and insufficient information and transparency in the market can be minimized through an independent entity.
- Politicians/governments may have an incentive to create independent regulatory authorities and delegate unpopular and complex decisions to them to avoid having a negative public image (as discussed further in chapter 4).
- Finally, national approaches to sector-specific regulation are often linked to international agreements and legislation. The text-box below looks at the current European Union (EU) framework and improvements suggested by European Regulators' Group for Electricity and Gas (EREG) on "Powers and Independence of National Regulators".

### **Case Study: European Union (EU) framework – 3<sup>rd</sup> Legislative Package**

In the EU, the powers and competences of national regulatory authorities are established in the electricity and gas Directives (2003/54/EC and 2003/55/EC) and in Regulations 1228/2003 on electricity and 1775/2005 on gas.

Under the Directives, Member States must give responsibility for a number of decisions to "designated regulatory or competent authorities". The underlying rationale for such authorities is the promotion of the internal energy market through strong co-operation and coordination between Member States. In particular, when a cross-border dispute occurs the responsible authority shall be the one with jurisdiction over the system operator refusing use / access to the system.

In many cases, country reviews suggest that the effectiveness of regulators is frequently constrained through a lack of independence from government and insufficient powers and discretion.

Under Commission Decision 2003/796/EC the role of the EREG was formalized. This group shall among other things "contribute to the consistent application of the provisions set out in electricity and gas Directives as well as possible future Community legislation in the field of electricity and gas".

The ERGEG's advice on the 3<sup>rd</sup> legislative package presented additional EU legislative requirements necessary to enhance the role of regulators in the EU. These additional requirements are briefly summarized as follows:

- National Legislation shall be in accordance with the new “European System of Energy Regulation<sup>5</sup>”;
- All elements of the Board of each national regulatory authority shall have a standard duration for the term of office;
- Each national regulatory authority should have adequate human and financial resources. The regulators should preferably be funded by levies;
- National regulatory authorities shall be properly accountable. The particular form of accountability is a decision left open to each Member State;
- Member States shall ensure that information submitted to one regulator can be made available to another and/or to national competition authorities. The same level of confidentiality as imposed by the originating authority must be guaranteed;
- The regulatory authority should have powers to facilitate the use of networks on a non-discriminatory basis;
- Market rules regarding the compulsory market (e.g. compulsory gross pool, bilateral markets) should be subject to regulatory approval;
- National regulators shall identify, implement and monitor transparency requirements; and
- National regulators must ensure that unbundling is effective and they should monitor its compliance.

Source: ERGEG (2007)

### 3.4 Concept and dimensions of regulatory independence

Regulatory independence is a relative concept which involves a number of players and is far from being linear. Stern (1997) argued that independent regulation depends on how much independence is effective and sustainable on a sliding scale.

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<sup>5</sup> For details on European System of Energy Regulation we refer to ERGEG's paper on the 3rd legislative package: “Paper 2: Legal and regulatory framework for a European system of energy regulation”.

Effective independence requires that the regulatory authority is free from many of the political and administrative pressures of central government. In parallel, as regulation affects many players in the market and in the society a balance between the interests of producers, consumers and other parties is of fundamental importance. Assuming that players in the regulatory domain are rational they will try to influence the regulatory process in order to advance their own interests, as illustrated by Figure 1. Typically, shareholders want to maximise share value, customers want access to high quality service at low prices, employees want to retain their jobs and incumbent companies want to retain market share.

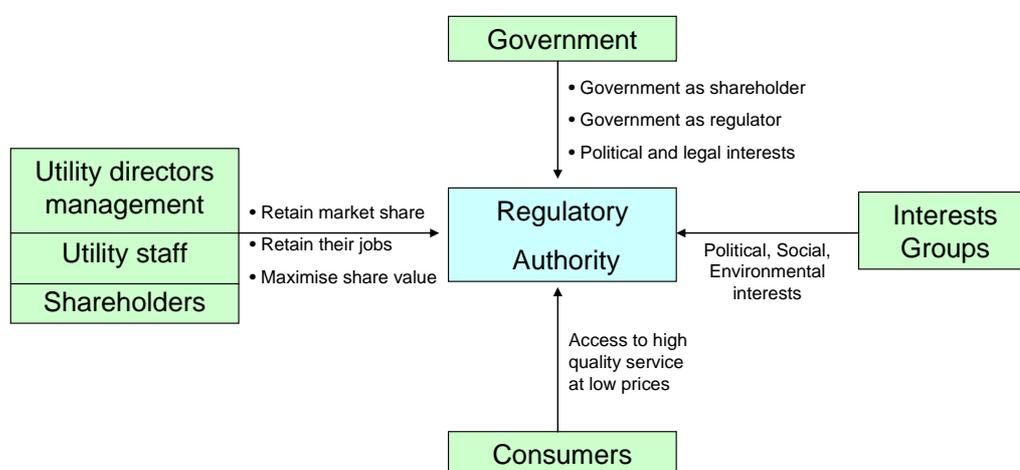


Figure 1: Relationship between the main players and the regulatory authority

In addition, effective regulation needs to be sustained over time. In the long-term the regulatory framework needs to have continued acceptance by companies, consumers and the government in order to be sustainable. Laws and institutions may not operate in practice as they were expected to operate in theory. The political and legal culture may not support it sufficiently. It is possible to identify the following desirable features of a regulatory authority:

- Autonomy,
- Authority,
- Accountability, and
- Ability.

Autonomy requires minimizing direct and indirect influences from the government, utility companies and the general public in the regulator's sphere of intervention. Authority is necessary to give legitimacy to the regulator in tariff setting, license issuing and monitoring. Accountability serves to promote transparency and brings credibility to the regulatory process. Finally, ability means the capacity of a regulator to conduct its functions and duties.

These characteristics may also be translated into different dimensions of regulatory independence such as political, legal, sociological and financial independence, transparency and accountability. It should be noted that these dimensions are not strictly separable; on the contrary, there is a broad spectrum of possible relations and over-lap between them. For example, in an appeal process if the regulator is not free to allocate resources as necessary then it might be reluctant to investigate/prosecute because it does not have the funds to meet the legal costs. This simple example shows how the lack of financial independence can have an impact on accountability and, consequently, on transparency.

The next chapters discuss each of the dimensions in more detail.

## 4 Political independence

One important dimension of regulatory independence is political independence. Political independence means that the regulatory authority is free from interference of a government ministry or department and the regulator has control over its internal administration as well as protection from removal from office for political reasons. However, there is also the risk that other groups (e.g. industry, consumers and interest groups) will exert influence or pressure on the regulator. Thus, in order to assess political independence it is essential to understand the regulator's role in relation to ministries and political executives as well as other stakeholders.

### 4.1 Independence from government

In this chapter we start with the institutional approaches to utility regulation and more specifically on the establishment of autonomous regulatory authorities and their relationship to superior ministries and political executives.

There is a wide range of institutional options regarding the degree of political independence as briefly summarized in Table 1.

Table 1: Forms of Regulatory Institutions

Regulatory Approach	Form of Regulatory Institution	Description
Regulation	Identifiable regulatory units	Group within central government ministry characterized by a certain degree of administrative and (if not legal) independence.
	Independent advisory bodies	External panels of experts providing external advice to a regulating minister that retains executive regulatory powers. Transparency and independence may be enhanced when expert advice is made public.
	Ministerial agency	The ministry retains all regulatory powers but delegates the management of some regulatory functions to a ministerial agency.
	Independent regulatory body	Regulatory entity is detached from ministerial intervention. Ministries may provide some advice but only on non-economic matters.

Industry Self-regulation	There is no specialized regulatory organization. This approach is characterized by a high degree of institutional independence from government, politics, consumers and other interests but it contributes to a reduction in social welfare.
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Source: based on Jacobs (2003)

Independent regulatory authorities have been established in several countries such as the USA, UK, Canada, Australia, France, Italy, Denmark etc. These entities are autonomous bodies with specific powers and are administered by an individual or group (i.e. a Commission) appointed for a definite non-revocable period. Regulatory authorities vary in their scope of authority and responsibilities. Typical regulatory duties include regulating the monopolistic activities of transmission and distribution of gas and electricity networks, setting network tariffs and quality standards, supervising operator commitments, handling complaints, providing policy advice, monitoring competition and dispute resolution. Regulators in the USA, the UK, Canada and Australia have a broad mandate to regulate broad range of regulatory and competition issues. Conversely, regulatory authorities in, for example, France, Italy and Denmark have more limited and specialised powers mainly related to economic network regulation (Ocana, 2002). The situation is similar in Germany, where the regulator deals only with the electricity and gas network and not the energy markets; competition issues are tackled by the antimonopoly authority.

On the contrary, in countries such as Austria regulation is institutionally linked to the ministry. In Austria, E-Control GmbH is a non-profit company whose shares are reserved for the federal government and administered by the Federal Minister of Economics and Labour. In Finland, the Netherlands, Norway and Sweden the regulatory authorities operate within the administration of the ministries.

Nevertheless, even if regulators are given “formal” independence through legislation (see chapter 5), the government can influence regulators in various ways, e.g., by dismissing/replacing senior regulatory officials, cutting regulatory budgets, or overruling decisions. For example, in the case of sensitive issues such as tariff-setting even when legislation empowers regulators to set tariffs, government will exert pressure on regulators to not increase prices. Slovenia’s experience (see Case Study below) clearly illustrates this issue.

**Case Study: Slovenia’s experience**

In 2002, the Energy Agency of the Republic of Slovenia (AERS) decided to introduce incentive regulation over network activities, namely for the application of price-cap regulation. When setting price-caps, AERS had considered that the cap level should be sufficient to cover the efficiently incurred O&M costs and an adequate return on

both inherited capital and new investment.

In the past, electricity prices in Slovenia were entirely controlled by the Government. Generally, the pricing policy was not built on the economic rules of cost recovery and real efficiency. For several years, growth in electricity prices was kept below the inflation rate, so that prices decreased in real terms. In 2000, a new network pricing design was developed. For this exercise, the network (transmission and distribution) revenue requirements were quantified on the basis of the prevailing level of sector revenue.

With the EU accession the pressure to keep inflation low in the country increased. Controlling electricity prices was considered essential to inflation control in Slovenia. It was understandable that normative regulatory principles had to be reconciled with the political reality in the country and with the macroeconomic requirements (inflation control) resulting from the EU accession. Given the autonomy of the regulatory decisions granted to the AERS by the energy legislation, the right (but also the only possible) way to reconcile the macroeconomic objectives with the required and agreed with the Government price increases was to use a coordinated approach and fund a compromised supported by AERS, the Government and the industry.

The agreed-upon 15.03% price increase was not feasible politically. However, instead of looking for a coordinated and consensus-based approach, the Government overruled the decision of AERS and forced the regulator to reopen the price control process and adopt lower price increases. The new target level of feasible price increases was determined politically and the computation efforts following the price control reopening were solely directed to “justify” the new “artificial” revenue targets. It is understandable and logical that this unexpected price review triggered by political pressure had a negative effect on the credibility of AERS. Moreover such regulatory review had no solid economic basis as AERS was forced to seek all possible methods to justify lower revenue requirements.

The AERS view that the regulator had independence and autonomy to set prices was not well received by the Government and led to increasing tension and deterioration of the relationship between the two institutions. In 2004, the AERS's independence was legally restricted by amending the Energy Act. The amended Act established a new body, the Regulatory Council. The Council was composed of five external senior officials and would control the decisions of AERS. Not unexpectedly, the Regulatory Council also included governmental officials, effectively leading to a take-over of AERS by the Ministry. The independence of the regulatory decision making process thus became an illusion.

Source: Ajodhia, Petrov and Scarsi (2005)

In addition, informal pressure from political authorities may also place a strain on the regulatory authority. This may happen, for example, where the regulator takes direction from political authorities in order to get reappointed. In summary, there is a large gap between “literal independence” and “effective independence”.

## 4.2 Independence from stakeholders

The regulatory authority shall balance interests of the different stakeholder groups. Each of the major groups will be explained separately below.

### Regulated Industry

The regulator’s relationship with the regulated industry is crucial to the effectiveness of the regulatory process and it depends primarily on the regulator’s institutional design. In particular, three main critical issues shall be mentioned here:

- Information asymmetry;
- Public and private ownership; and
- Conflict of interests.

Information asymmetry is particularly relevant when there are few market players. Normally, these players come into possession of information not made available to the regulator such as information on technological advances in the industry and on the nature of their own activities, e.g., cost data. In these circumstances the regulator’s decisions may be based on erroneous or misleading information at the expense of the principles of competition and consumer welfare. However, even when there are many players in the market they may organize themselves into lobbying groups to enhance their power in relation to the regulator. The Case Study below on the price-cap approach in the Netherlands can be seen as an example of how the industry can exert pressure on the regulator to modify or overrule decisions.

### **Case Study: Price cap approach in the Netherlands**

In 1998, the Electricity Act introduced a completely new approach towards price regulation in the Netherlands. The Dutch Office of Energy Regulation (DTE) published its first decision on the X-factors for electricity transmission and distribution networks in September 2000. These factors were strongly driven by the results of a Data Envelopment Analysis (DEA) benchmark report. DTE used a single input factor, which was the total cost of each network company. DTE’s motivation for the total cost approach was that it is the company’s responsibility to trade-off between short and long-term costs. By simultaneously considering operating and capital

expenditure in the efficiency analysis, DTE bypassed the regulatory problem of investment appraisal.

The September 2000 decisions on the X-factors led to a wave of protest and formal appeals by the industry. The direct translation of efficiency scores into X-factors made the Dutch price-cap system extremely sensitive to data errors. This was exploited well by the regulated industry. Not only did they bring this as an argument in their legal case against DTE, but also they took the opportunity where possible to strategically manipulate the results of the analysis in their favour. Overall, this resulted in an instable price regulation system with results that had to be revised multiple times.

A regulator who continually resets prices for reasons of data correction tends to lose credibility. This loss of credibility became an important argument for the Ministry of Economic Affairs, under which DTE falls, to gradually shift more and more responsibilities from DTE to itself.

Legally, DTE's independence cannot be challenged as this stems from the Electricity Act. Thus, DTE remains legally independent, but in practice its independence has been reduced.

Source: Ajodhia, Petrov and Scarsi (2005)

Ownership is a further issue. It is commonly accepted that a publicly-owned operator is more subject to governmental intervention. Furthermore, public companies may impede competitive entry of new companies and pricing is generally less efficient with public companies (Jacobs, 2003).

Finally, there is a risk that the regulator's independence is compromised by the regulator's private interest in the sector, directly or indirectly, e.g., when the regulator holds stock in the regulated industry. Regulated parties may also try to "capture" the regulators, e.g., by bribing them or by promising them well-paid jobs in the future, to influence their decisions in favour of themselves.

It is important that the board of the regulatory authority is free of conflicts of interest and where such conflicts arise they should be publicly disclosed as well as the consequences of such conflicts of interest. For example in the context of part-time employees who are pursuing other activities in addition to regulation, procedures for the management and control of potential conflicts of interest are necessary.

Most European countries apply provisions to avoid conflicts of interest before, during and after regulatory action. According to Larsen et al (2004) the board of the regulators in Austria, Italy and Luxemburg are not allowed to have held a position in

the energy industry or its associations in the years preceding appointment and in France, Italy, Portugal and Spain the same applies after the appointment. In all of the foregoing countries, regulators may not have personal or financial interests in the energy industry.

### Consumers

Consumers are another party potentially interested in influencing the regulatory process especially on prices, quality and access to services provided by utilities. There are two basic ways in which consumers may influence regulatory practices: directly or indirectly (via politicians). The latter occurs when politicians try gain voter support by pressuring the regulator to pursue short-term political interests (e.g. reliable electricity at lower prices). Consumers organized in trade or industry associations may exercise a direct influence on the regulatory process. This could be for example the role of consumer watchdogs (normally non-profit) in protecting the interests of consumers (see the example of Energywatch in the UK).

#### **Example: Energywatch in the UK**

Energywatch is the independent gas and electricity watchdog in the UK. It was created in November 2000, is a Non Departmental Public Body and is independent of Government and Industry although funded through grant aid by the Department of Trade and Industry. The purpose of Energywatch is to protect the interests of consumers of gas and electricity by providing advice and information to consumers, public authorities and other persons and investigating consumer complaints. Energywatch has gained support from the public, Parliament, the regulator and the media and is an accepted and recognised body.

Energywatch may not have direct impacts on the decision-making of the regulator but due to its ability to publicize information, such as customer satisfaction levels and complaint handling they can have an indirect influence on certain regulatory outcomes affecting consumers.

Source: [www.energywatch.org.uk/](http://www.energywatch.org.uk/)

### Investors

Investors seek a regulatory process that is stable over time, so that investors are protected against opportunistic government intervention. This is particularly important in the countries in transition because their economies are dependent on private sector involvement in the productive sectors and investment in infrastructure.

### Competition authorities

In most countries the regulator and the competition authority are separate entities although they often cooperate in their efforts (see example below). In this case, regulatory authorities often have a role in assisting competition authorities (e.g., monitoring the market) and providing advice on decisions. The rationale for such separation may be found in the different nature of regulation and competition policy that requires different knowledge and approaches.

#### **Example: Overlapping jurisdictions in Finland**

The Energy Market Authority has partly overlapping jurisdiction with the Finnish Competition Authority. On the basis of the Act on Competition Restrictions the Finnish Competition Authority has general supervisory authority mandate over all sectors of the economy including electricity and natural gas markets.

As a general rule, the Energy Market Authority does not have any powers regarding the competitive aspects of the electricity and natural gas markets, with the exception of supervising the retail supply of electricity and natural gas monitoring the security of supply. In January 2006, the Energy Market Authority and the Finnish Competition Authority signed a Memorandum of Understanding. The document contains a description of the areas and modes of cooperation.

Source: [www.emvi.fi/](http://www.emvi.fi/)

Less frequently, regulators may also have power to set competition policy, such as where both entities merge into one entity. This is the case, for example, of the Australian Competition and Consumer Commission (ACCC). The ACCC was formed in 1995 to administer the Trade Practices Act 1974 and other acts.<sup>6</sup> It works together with the Australian Energy Regulator (AER) which is part of ACCC.

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<sup>6</sup> The Trade Practices Act's purpose is to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection. The Act deals with almost all aspects of the marketplace: the relationships between suppliers, wholesalers, retailers, competitors and customers. In broad terms the Act covers the regulation of industries such as telecommunications, gas, electricity and airports.

## 5 Legal independence

The existence of a legal independence is an important dimension of regulatory independence contributing to enhanced credibility and effectiveness of the regulatory process. Indeed, the legislative framework is essential, as this provides the basis for the regulatory activities. In general, on an EU level most countries have an Energy Law, Electricity Act and Gas Act that establishes, among other things, regulatory independence.

The legislation may state the objectives, functions, duties and powers that a regulator possesses, e.g., to issue licences, set prices, impose quality standards, and monitor market performance. In addition, legal independence includes legal provisions on appointment, decision-making structure and dispute resolution. These main issues will be further discussed below.

### 5.1 Regulatory objectives

The specific regulatory functions and objectives usually are stated in several different pieces of legislation with differing degrees of priority.

In general, regulatory authorities do not have a single regulatory objective, but many objectives that are closely related to economic issues. Regulatory authorities may also have social and environmental objectives (see Table 2).

Table 2: Objectives and tasks of some regulators in Europe

Country	Competition	Market transparency	Consumer protection	Economic efficiency in the supply	Environmentally friendly electricity supply	Security of supply	Socially responsible price policies
Austria	✓	✓	✓		✓	✓	
Denmark	✓	✓	✓	✓	✓		
Finland	✓	✓					
France	✓	✓	✓	✓			✓
Greece	✓	✓	✓	✓	✓	✓	✓
Ireland	✓	✓	✓	✓	✓	✓	✓

Italy	✓	✓	✓	✓	✓		
Luxemburg	✓	✓	✓				
Netherlands	✓	✓	✓	✓		✓	
Norway	✓	✓	✓	✓	✓	✓	
Portugal	✓	✓	✓	✓	✓		✓
Spain	✓	✓	✓	✓		✓	

Source: Larsen, Pedersen, Sorensen and Olsen (2004)

The table above shows that the role of energy regulators (at least in Europe) is largely concentrated in two interrelated areas: monopoly control and consumer protection.

Legislative changes to the competencies and roles of the regulatory authority have a direct impact on regulatory development as in the case of Slovenia.

#### **Example: The regulator's activities in Slovenia since 2004**

In 2004 the governance of the Energy Agency was changed. From the beginning of the Energy's operation in 2001, the Energy Agency was managed and represented by the director appointed by the Government of the Republic of Slovenia. After the Energy Act was amended, the Energy Agency had two governing bodies: the director and the Council of the Energy Agency.

The amended Energy Act expanded the responsibilities of the Energy Agency and gave it more tasks in new areas. Crucial changes included expansion of the Energy Agency's authority to give approvals and issue opinions in the areas of heat supply and natural gas, reflecting the transition from a market with privately negotiated third-party access to regulated third-party access.

The Energy Agency's authority to resolve disputes also expanded. In accordance with the amendment, the Energy Agency now resolves disputes arising from an alleged breach of general supply conditions and system-operation rules. The Energy Agency also handles administrative appeals of interconnection decisions.

The implementation of the Energy Act also led to preparation of methodologies for setting network charges, tariff systems and the general conditions for supply and consumption.

Source: Annual report of the Energy Agency

As a general rule electricity and gas are regulated by one single entity but there are some exceptions. In Romania there was one regulator for electricity and heat (ANRE) and one for gas (ANRGN) but recently they have merged into one entity responsible for all activities. Having a regulator that oversees both electricity and gas is appropriate depending on the size of the industries, scarcity of human resources, political risks, imperfection of the decision-making process, coordination capacities and the relevance of industry boundaries. Although there is no general consensus on this issue, a single regulator seems to be an efficient option in a relatively small economy with short supply of regulatory experts and where there are high synergies between the regulated activities. On the other hand, industry-specific regulators benefit from greater specialization and may be more effective in terms of implementation.

Electricity and gas are regulated by the same authority in several countries such as Austria, Denmark, Finland, France, Greece and Italy reflecting significant interdependence between the two industries. This should not come as a surprise because network industries face similar regulatory issues and are under a similar regulatory approach.

## 5.2 Decision-making structure

The decision-making structure is, in general, explicitly defined in the legislation, statute, administrative procedures, etc. In this context, regulation may be assigned either to an individual or a group (e.g. a commission). In both cases, the person or group at the top of the structure assumes the legal responsibility of the regulatory body.

Having a single individual responsible to issue decisions provides more consistency in decision making and more expediency in executing regulatory functions. By the same token, there is regulatory uncertainty associated with change of a single regulator.

In the case of a commission (the more usual approach) additional options are available. The group may have both full-time executive members and part-time non-executive members<sup>7</sup>. The first option has the main advantage of providing human resources at reduced cost. Nevertheless, it may create problems on management

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<sup>7</sup> Alternatively, the number of members in a commission may change according to the circumstances. This is the approach followed in Ireland for electricity. The Commission in Ireland is headed by up to three Commissioners at any one time. Currently, it consists of three members as a new Commissioner joined the team on 1 July 2008.

and control of regulators' personal interests. The second option introduces a certain degree of flexibility in terms of the regulators' membership but this may occur at the expense of independence.

Table 3 indicates which structure (individual or commission) is stronger on a range of characteristics.

Table 3: Decision-making structures – Individual versus Commission

Characteristic	Individual	Commission
Speed of decision-making	✓	
Accountability for decisions	✓	
Resource demand	✓	
Predictability of decisions	✓	
Invulnerability to individual preoccupations		✓
Invulnerability to improper influences		✓
Potential to reflect multiple perspectives		✓
Potential to stagger terms to enhance stability and weaken links with particular government		✓

Source: Smith (1997)

A further issue when comparing different top-level regulatory structures is related to regulatory capture. The successful capture of a single regulator will be fully effective but probably more transparent than in the case of a group.

The choice of a single or group structure will also depend on other factors such as available persons for appointment, financial resources, size of the industry, etc.

Figure 2 and Figure 3 represent two simplified examples of organisational regulatory structures. Under the first structure, the Chairman and members are responsible for decision-making whereas technical tasks are responsibility of specialized departments (subject to supervision of an executive director). The second structure members of the Board have managerial tasks and are head of each specialised department.

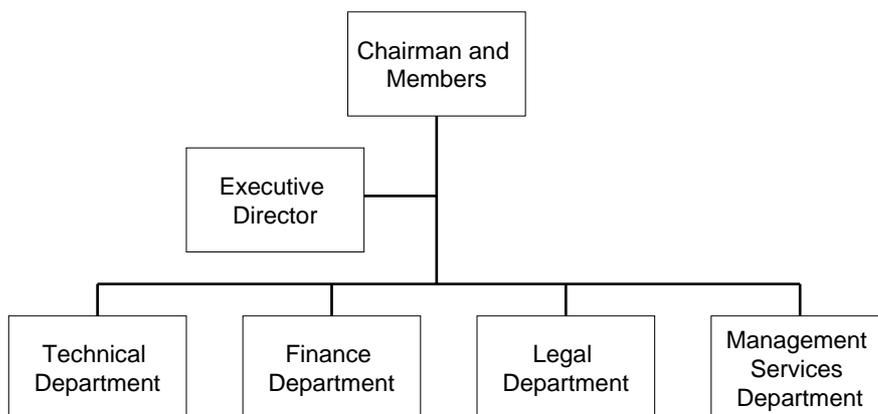


Figure 2: Example of organizational structure - I

Source: Berg (2000)

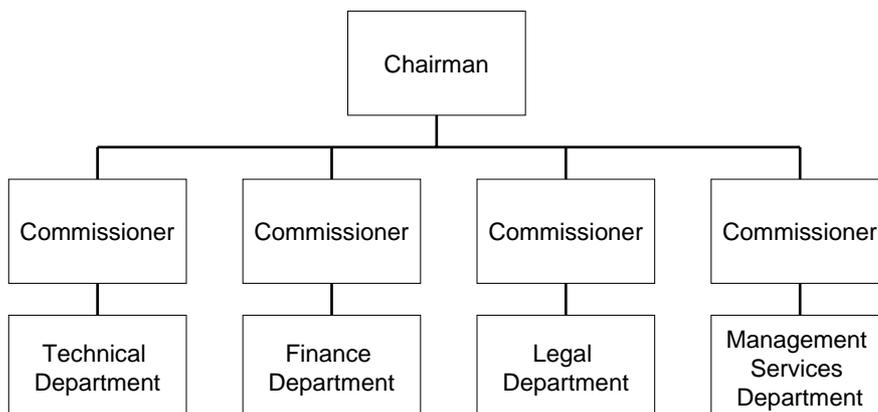


Figure 3: Example of organizational structure - II

Source: Berg (2000)

The size of commissions including the Chairman can vary in terms of number. The Irish regulator is formally a commission made of three members: a chairman and two commissioners. The Commission for Energy Regulation (CER) has four divisions, each managed by a divisional director. For example, in Portugal and Italy there are three-person commissions, consisting of a president and two members. The UK, Belgium, France and Denmark have larger commissions. For instance, in France CRE's is composed of a College of Commissioners with 9 members, a Dispute Settlement and Sanctions Committee and departments run by a Managing Director under the authority of the Chairman. The Danish Energy Regulatory Authority (DERA) comprises a chairman and 6 members of which one is designated as vice chairman.

In Austria the regulatory tasks are divided between an executive non-departmental public body and a commission consisting of three members, one of whom must be a judge.

In Finland and Norway the regulatory authorities operate under the administration of the ministries with a Director as a leader.

### **5.3 Appointment of regulators**

Many instruments can be used to protect independence of the regulators. The appointment of regulators (or commissioners) remains largely a government responsibility and questions such as term of office, reappointment, removal from office and restrictions on personal interests are usually included in specific legislation, regulator's statutes, contracts or decrees, etc.

In many countries there is a fixed term of appointment and reappointment of regulators. Even more important than the fixed term of appointment is staggered terms so that they do not coincide with the election cycle. As a general rule mandates are irrevocable but removal from office may occur in special circumstances (e.g. personal incapacity, proven corruption). In general, regulatory independence is more effective if the removal from office requires the approval of the legislature.

In addition, explicit provisions are written down to constrain regulators from pursuing interests in conflict with their regulatory functions during and after their mandate in the regulatory institution (see also section 4.2).

### **5.4 Appeals of regulatory decisions**

The particular mechanisms and procedures for appealing regulatory rules and decisions might be defined in legislation and they vary widely from country to country.

It is possible to distinguish different types of appeals as follows:

- To the regulatory authority: stakeholders ask the regulator to reconsider a decision;
- To an administrative tribunal: checks whether the law was followed by regulator;
- To a court system: consider whether the regulator was substantially correct or not;
- To a licensing authority (in case of countries that regulate by license): the operating license is revised; and
- To a legislative body or president: the idea is to change the law under which the regulator operates.

In some countries it is also possible to solve eventual disputes through arbitration. In this case, the parties involved in the dispute resolution process agree in having a third party (a group of experts) responsible to find a solution for the dispute. In the UK, for example, the antitrust agency hears appeals relating to license amendments.

In summary, two main aspects shall be considered in an appeal process: appellate body and matters of appeal. In order to ensure that the regulator remains accountable the appellate body should be independent. In addition, an appeal shall be against a substantial decision i.e. being based on errors of fact or law or failure to follow a certain process.

## 6 Sociological independence

Besides political and legal independence another important dimension of independence is the sociological one.

### 6.1 Perception and reputation

The extent to which the regulator is perceived in the society to be independent of political control and separate from government institutions is a key factor in the legitimacy and acceptance of its authority. In this context independence means that the regulator has sufficient credibility and is able to influence the industry, consumers and other government institutions. On the contrary, if the regulator lacks legitimacy and accountability then there is potential for constant appeals, lack of support from government, and consequently ineffective regulation.

In practice, effective regulation is closely related to the reputation of the regulatory authority. Regulatory reputations take time to build up and can also be quickly lost.

Some authors suggest that effective regulation may well require the establishment of arrangements that allow stakeholders to present their opinions through open processes like public debate or, alternatively, through contracts with investing companies.

The prestige (perception) of a regulator in the society can be enhanced through an effective public relations strategy. Public relations involve popularizing successes, media appearances and reputation management in order to create and maintain a positive public image. Essentially it is a management function that focuses on two-way communication and fostering of mutually beneficial relationships between a regulator and its stakeholders.

### 6.2 Development of a public relations strategy

The regulatory authority should develop and implement a public relations strategy in order to facilitate effective communication between the regulator's staff and other institutions (such as trade unions and employees associations) and the general public. This means that communication should be bi-directional, impartial as much as possible and provide useful information on stakeholder views.

The main objective of a public relations strategy should be enhancing public understanding of the role and activities of the regulatory authority as well as implications of the regulatory framework on consumers, regulated companies and the overall economy.

An important step in implementing a public relations strategy is the choice of the appropriate tools i.e. workshops, seminars, articles, newspapers and internet. The choice of a certain tool in detriment of another will depend primarily on the scope of information and the target audience. Table 4 shows the most important communication instruments available to regulators and situations where they are more adequate and effective.

Table 4: Adequacy of the main communication tools

Communication tools	Adequacy
Internet	<ul style="list-style-type: none"> <li>• access to legislation, regulation, decrees</li> <li>• regulatory cases, proceedings and investigations</li> <li>• newsletter briefly describing current activities and main legislative changes</li> <li>• web sites of other institutions (national and foreign) involved in regulation</li> </ul>
Radio and TV media	<ul style="list-style-type: none"> <li>• members of the regulator could give interviews or participate in debates on economic regulation</li> </ul>
Press	<ul style="list-style-type: none"> <li>• inform general public about activities of the regulator</li> <li>• inform local representatives and citizens about region-specific issues</li> </ul>
Workshops, seminars	<ul style="list-style-type: none"> <li>• open discussion about the establishment, progress and setbacks of the regulatory framework</li> </ul>
Publications	<ul style="list-style-type: none"> <li>• inform the public about the regulator's purpose, activities and performance e.g. the Annual Report</li> </ul>

For example, if the objective is to inform the general public about activities of the regulator then it makes sense to select a daily newspaper with high coverage rates instead of a specialized magazine. Conversely, when the regulator deals with region-specific issues then an effective way to communicate with local administration representatives and citizens is probably to publish articles in regional or local newspapers.

Furthermore, a clear procedure for consumers, energy companies and other institutions on how to communicate with the regulator should be defined and have a fixed time frame. This is particular important in the following situations:

announcements by the regulator to the stakeholders; stakeholder consultations, requests for clarifications and complains.

Managing media relations effectively presents challenges to regulators as they need to develop skills allowing them to communicate with the public. Case studies show that quality communication with the public plays an important role in securing acceptance of difficult / unpopular decisions. In some cases a spokesperson is employed to act on behalf of the regulator in media appearances (see example below). This person is usually specialised in public relations and know how to communicate effectively and brings the desired message across.

#### **Example: Public relations in Slovakia**

After 2003 the mass media has significantly increased the interest in the activities carried out by the Regulatory Office for Network Industries in Slovakia. This was because the Office took over the responsibilities of the Ministry of Finance of the Slovak Republic as of 1 January 2003 governing price regulation of network industries.

The relations with mass media and the public are provided by the official spokesman, who is in everyday contact with press agencies, editorial boards, institutions and social organisations. The public was informed on the relevant conclusions on the activities of the Office at the press conferences and meetings on specific topics organised by the Head Office.

In 2004 the Office became a fully functional independent body that has won its reputation among state administration bodies and authorities. The members of the Regulatory Council, directors of divisions and other employees presented regulatory approaches enforced by the Office at various sessions and events such as international sessions, conferences and seminars as well as to mass media. The chairman and the vice-chairman of the Office often hosted in public mass media, including TV and radio channels.

Source: Annual Report of the Regulatory Office for Network Industries

## 7 Financial independence

A very important indicator of the regulator's independence is the source of its budget e.g. licensing fees, state budget, etc. Financial independence should be looked at from a two-dimensional perspective: the funding of the regulatory authority and its financial autonomy. The main problem occurs when the regulator's budget is allocated and approved by institutions that may seek to use the budget to influence regulatory decisions. The impact and adequacy of the source of funding on independence is of fundamental importance. Insufficient resources may compromise the ability of the regulator to carry out its tasks, while too many resources may result in a lack of focus in regulator activities.

Additional considerations include the level of expertise and human resources available to the regulator. There may also be significant differences between the regulatory budgets in different countries including cost of external services and staff employed. These variations may reflect different regulatory philosophies; existence of alternatives to regulation; size of the energy market; use of external consultants; cost of living and salary rates and how salaries of regulatory staff compare with those in the other sectors.

In summary, a regulator's effectiveness is determined largely by the adequacy of its resources, both human and financial.

### 7.1 Financial resources

At present, the source of regulatory funding varies significantly from country to country. Licensing fees are the most common methodology used for funding the costs of energy regulation. However, the funding of the regulators can be also arranged through a direct funding from the budget of the ministry or state, a levy incorporated in the regulated tariffs, a percentage of administrative fines and penalties or a combination of two or more of the basic sources. Some country-based examples are provided in Table 5.

Table 5: Examples of countries with different sources of funding

Source of funding	Examples / Countries
Licensing fees	Greece, UK, Ireland
Direct funding from the budget of the ministry or state	Portugal

Levy incorporated in the regulated tariffs	Denmark, Slovenia,
Combination of two or more sources	The Netherlands, France

Source: Regulators' websites

It is commonly accepted that a regulator financed by a fee levied on the regulated companies is more independent than one dependent on the state budget. Financial dependence on the government budget can detract from a regulator's political and administrative independence. Conversely, regulatory financing by consumption taxes for example may make a regulator over-sensitive to short-term public opinion at the expense of long-term economic efficiency.

However, there are no internationally accepted standards for funding sources ERGEG's advice on 3<sup>rd</sup> legislative package on EU legislative requirements recommends that the regulators should preferably be funded by levies. Although fee based funding is seen as more independent than state budget funding the former may leave a regulator short of funds in the event of a financial crisis when the industry will not be able to pay its fees. However, in more stable economies this is unlikely and from our research we have not found a case where this happened.

A related issue is the regulator's control over how fees and funds are available for its activities. Budget approval processes by the government is often still necessary which may result in delays compromising regulatory activities.

For example, in Austria the Supervisory Board of E-Control Commission is responsible to approve the budget and to fulfil a general control function. While the Supervisory Board of E-Control may by law approve or reject E-Control budgetary decisions, however in practice it has never rejected a submission from E-Control.

## 7.2 Human resources

When it comes to matters of internal organisation and personnel policy most regulators decide by themselves. However, in some cases the government may participate in the decision-making process. Some regulatory authorities are structured with a board of directors appointed by the executive branch of government, while others are managed by an executive director. Usually the legislative branch participates by confirming the proposed directors or even appointing them. For example in Austria, Denmark and Greece the government participate in the decision-making.

The challenges posed by the management of human resources in regulatory authorities are similar to those in other public organisations and ensuring the

competence and specialisation of staff is particularly important. An element of independence refers to commissioners, members, and heads of the regulator appointed by transparent methods for fixed mandates (as referred in chapter 5.3.).

For an optimal institutional design directors should be highly qualified and independent of regulated firms, consumers, other stakeholders, and the political powers. A wide range of different approaches to recruitment have been adopted by regulatory authorities such as recruitment of ex-staff from the ministry; transfer of civil servants; transfer of regulated industry personnel, hiring expert consultants and experienced academics. In addition, regulatory authorities increasingly contract out particular services to private companies or consultants. In this case, the regulator has to make sure that such private companies or consultants do not have interests and/or are influenced by regulated companies. Ultimately, the regulator must retain responsibility for its decisions in order to ensure legitimacy.

Concerning the number of staff required for performing regulatory tasks it depends on the particular responsibilities of the regulator. Overstaffing will contribute to increase direct costs of regulation and may place unnecessary burdens on industry (to justify the number of jobs within the regulator) whereas a shortage of skills impacts the ability of regulators to conduct their activities. Therefore, a sound general principle is to keep the regulator's staff as small as possible without compromising its tasks and contracting out when necessary. For example, traditionally in the UK the regulator concentrates the main tasks in a few numbers of employees and uses external consultants to assist with specific tasks.

Usually, qualifications requirements are set out in the law establishing the regulatory authority. A common qualification required is significant experience or training in economics, finance, law public administration and industry-specific technical expertise. In addition to the specialists, the regulatory authority will need other professional staff to manage the administration, personnel and financial aspects of the office. Support staff will also be required for all specialist and non-specialist departments.

With regards to staff compensation if the regulatory office is subject to government compensation rules and regulations this might constitute a significant limit to the agency's recruitment process. The regulatory authority should offer compensation terms that is at least as good as those offered by other public sector bodies. Adequate remuneration of regulators can enhance independence both by facilitating the recruitment of persons with sufficient expertise and by limiting the temptation of accepting bribery from industry.

In parallel with an adequate remuneration scheme regulators shall organise training activities for all the regulatory staff in order to increase the capability of regulatory institutions. Training may be best organised as a set of short courses or seminars

covering a range of regulatory areas. Training is usually required in the following main areas: tariff setting, financial analysis, negotiating techniques, appeals against regulatory decisions, energy economics and soft skills.

## 8 Transparency issue

There is no general consensus on the definition of regulatory transparency. For the purpose of this paper, we define transparency as the way the regulators communicate and exchange information in a clear and understandable manner and the regulatory process is seen to be open and accessible. A particular issue in this area is the ability of the regulated entity or other stakeholders to challenge the regulator's decisions – i.e. the so-called accountability.

Transparency can help to prevent political influences, reduce regulatory risk and discourage corruption (see Argentina's experience below). It is therefore complimentary and not contradictory to independence. It is also crucial to the legitimacy of the regulatory process as is the key to attracting efficient investment and, at the same time, creates confidence in the credible commitment from the government / regulator to a set of policies. To sum up, transparency allows the regulator to carry out regulatory functions and to operate independently while promoting the legitimacy of the regulatory process.

### **Case Study: Argentina's experience**

In 1989, the Argentinean Government initiated a privatization process for all utilities. The power sector was regulated by two agencies: ENRE (Ente Nacional Regulador de la Electricidad) and ENARGAS (Ente Nacional Regulador del Gas). It is generally accepted that these two agencies have been effective in conducting their tasks. In addition, they have an acceptable level of independence, autonomy and accountability. They have their own source of funding, have a technically competent well-paid staff and they have to report to the legislative and executive branches of government. In spite of that they have been criticized. There are some concerns regarding the lack of administrative processes in appeals as well as transparency in regulatory decisions, which potentially increases the risk of capture. Furthermore, lack of regulatory accounts across companies is also pointed out as a drawback for effective economic regulation.

Source: Estache (1997)

However, it is important to note that transparency has a cost so that trade-offs between disclosed information and their expected benefits shall be taken into account. Moreover, the degree of transparency shall be consistent with the institutional framework as well as the political, economic and cultural context.

### Measures to improve transparency

Good communication, open consultation and access to relevant documents and information are key features of a transparent regulatory process. In order to improve transparency a range of measures is available to regulatory authorities:

- Detailed specification of the tasks to be performed by the regulator;
- Definition of confidential information;
- Workshops where advisory bodies (e.g. consumer councils) provide inputs into the process;
- Stakeholder consultation in the process of developing new regulatory methodologies and standards;
- Publishing final standards;
- Public hearings/meetings where stakeholders can make submissions and inputs into important regulatory decisions;
- Electronic dissemination of regulatory documentation;
- Written public explanations of regulatory decisions; and
- Accountability through appeal mechanisms; and open access to information.

Figure 4 represents the main steps of the regulatory process.

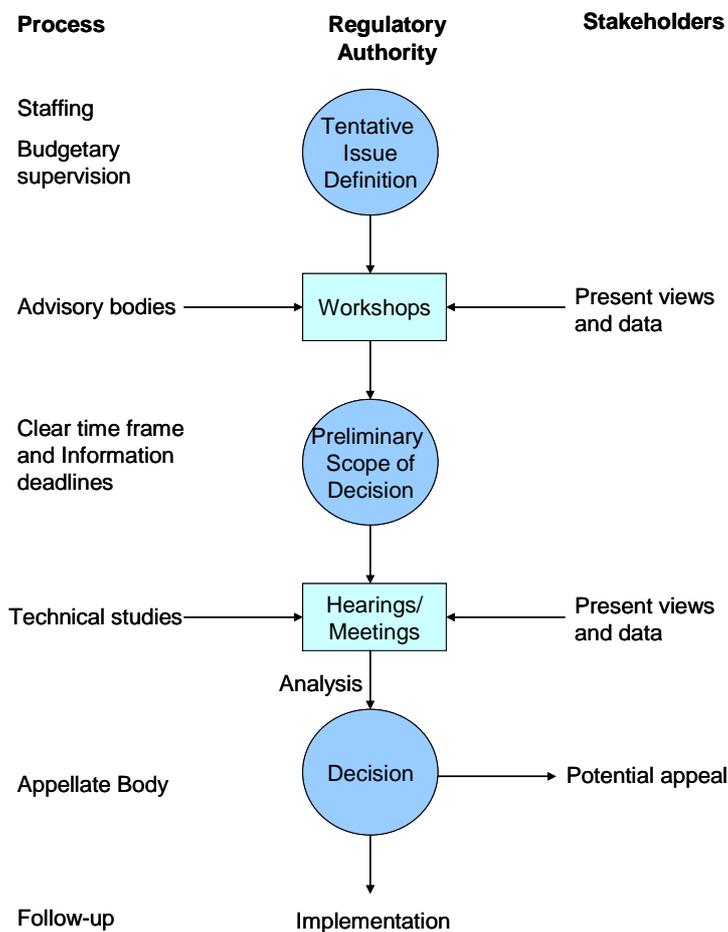


Figure 4: Features of the regulatory process

Source: Berg (1998)

The regulator must be able to publicly explain its policy objectives, and report on its activities and performance in pursuing its objectives. This explanation should not simply be to the industry or government, but to the regulator's stakeholders as a whole. One method for the regulator to promote transparency is to prepare and distribute to stakeholders and the general public an annual report on regulatory activities and sector performance. As part of its transparency, the regulator could publish any assessments made of its compliance with international standards of accepted practice. We may refer the impact assessments carried out by Ofgem as an example.

### Case Study: Impact assessments in the UK

Since 2003 Ofgem is in charge of conducting impact assessments of its important decisions or alternatively to publish a statement setting out its reasons. Conducting an assessment of impacts is a structured approach of Ofgem to policy development and decision-making. In deciding whether to carry out an assessment or not Ofgem

act in line with the principle of proportionality.

To produce good quality impact assessments Ofgem takes into account inputs from the industry and other stakeholders through a process of constructive engagement.

Ofgem may also conduct cost-benefit analysis in order to investigate whether the costs of a proposal are proportionate to the expected benefits. When it is feasible impact assessments will have a quantitative and qualitative nature. In addition, such assessments include impacts on consumers, on competition, on sustainable development and others. Impact assessments shall be developed in accordance with principles of best regulatory practice.

In the interests of transparency the Ofgem's website publishes all the impact assessments carried out by Ofgem.

Source: [www.ofgem.gov.uk/](http://www.ofgem.gov.uk/)

In general, industry, state organisations and consumers interact with the regulator either through formal decision making processes or (informal) personal interaction. Formal and informal decision making processes often have been incorporated into a consultation framework. A consultation process may involve different stages and may vary depending on the nature of the proceeding but it is possible to identify the following main stages:

- First stage: after an issue is identified, the regulator releases a formal consultation paper soliciting comments from the public;
- Second stage: comprehends a comment and reply comment period where outside players and the public at large formally submit their views on the issue;
- Third stage: a decision is reached based on available information and public policy objectives. The regulator's statement presents and justifies its conclusions on the issues addressed in the consultation paper.

As a general rule, the consultation paper, comments, reply comments and the final decision are available to the public on the regulator's website or through official publications, unless there is confidential information. This consultation process and respective stages ensure that the relevant groups are notified of a pending decision, allowed to participate in the process and informed of the final decision and its reasoning.

If parties do not agree with the decision, they can either appeal through the courts or appeal through the regulator by means of a petition for reconsideration (see chapter 8.1).

Key issues are how to protect information on customers and operators that should be kept private and how to provide information in a way that is cost effective for both the regulator and the stakeholders.

#### Constraints to transparency

Although many factors may potentially constraint regulatory transparency we address here three important ones: the historical and institutional environment; local specificities and the cost of regulation processes.

In countries where transparency has been limited, for political, economic or cultural reasons there may be a much greater need for clarification of regulatory processes, objectives and functions of regulation and open access to information. In this case, defining legal requirements for regulatory transparency may be an important tool to enhance transparency.

In addition, local specificities must be taken into account when establishing transparency policies. For example, in countries with limited experience of the regulatory process it is more difficult to communicate the message effectively with customers. Therefore the goal is not only to communicate the decision or message but to bring awareness and educate the respective groups on regulatory issues. As referred previously consultative bodies of consumers and industry representatives are suggested in order to ensure public participation.

Finally, the implementation or improvement of transparency policies is costly. For example, the cost of regulation processes has significantly increased in the UK or in Australia in recent years, in parallel with improved transparency.

## **8.1 Control and supervision circumstances**

Another aspect of regulation is how regulators are accountable and the relationship between regulators and other bodies in the context of monitoring and control of regulatory activities.

One of the main arguments in favour of independent regulators is that they minimize political interference with a negative impact on economic efficiency. The main argument against is a lack of accountability to the government and parliament as the establishment of an independent regulator places considerable power into an individual or group of individuals. Therefore, the challenge for regulatory institutions has been to make the regulatory system accountable without compromising independence of the regulators.

#### Accountability mechanisms

Accountability concerns the obligation to explain processes and reasons for decisions, fulfilled functions and utilised resources and to specify appeals procedures. In that way it is also presented as a tool to assess transparency.

There are many entities where regulators can be made accountable: the parliament or a ministry, the industries they regulate, the judges, the consumers and the society in general. Most regulators report to parliament or to a ministry that may or may not be the line ministry. They are also subject to audits and other controls, generally in line with the procedures applied to other public organisations. These aspects are further discussed below.

It is possible to distinguish three main types of accountability:

- Administrative accountability,
- Accountability through the Parliament, and
- Accountability through the judicial system.

Administrative accountability consists of making regulators responsible for the quality of regulation. Regulators may also have to comply with guiding principles for the development of regulations. For instance the regulator may have to perform an analysis of the impacts on low income or vulnerable customers as a result of a particular policy change or code/charging methodology proposal.

On the one hand, accountability can be seen as a tool to evaluate transparency; on the other hand clear transparency rules applied over the decision-making process is an important accountability mechanism. This would include, for example, a requirement that a regulator should render available its decisions and underlying reasons on its website.

As already anticipated, several independent regulators (most OECD Member countries) are subject to financial control and audit procedures to private or public accounting institutions.

Accountability through the Parliament ensures that the regulators should answer to the legislative branch of state through both presentation of periodic reports and give evidence on regulatory developments. The success of this type of accountability depends directly on the parliamentary interest in regulatory actions and policies, legal framework for supervision and existence of adequate parliamentary resources.

Furthermore, some authors put attention on the role of interest groups in providing additional information to politicians regarding the activities of the regulator. Policy makers will make use of that information in order to assess regulatory performance.

Accountability via the judicial system can provide mechanisms to ensure impartiality and compliance with law. Two main mechanisms are used in practice:

- Judicial review, and

- Appeal of regulatory decisions.

The decisions and circumstances in which judicial review may be applied are usually set up in the regulator's statute or in specific provisions. Stakeholders may appeal to an administrative tribunal or the court when they consider that the law was violated. The judicial review has been criticised because it might be used to delay the implementation of regulatory decisions.

An appeal is a fundamental procedure consisting of a re-evaluation of a certain decision. The specific mechanisms and procedures for appealing regulatory rules and decisions vary from country to country (see also chapter 5.4.).

#### Consequences of accountability

The way in which a regulatory authority may be rewarded or punished as a result of its performance depends on the type and design of a particular institution. However, in general it is possible to mention the following potential consequences:

- In case the regulator is funded by state budget, budgets could be expanded or cut based on the perceived performance of the regulator and on the regulatory outputs (in terms of industry performance);
- Recognition and compensation can be given to employees in case of significant contribution for achievements on sector outcomes;
- Additional legislative and executive supervision may be introduced when it is necessary to increase monitoring activities.

## 9 Summary of Questionnaire results

The questionnaire which was developed by KEMA and sent to all ERRA members consists of questions related to the respective countries' current regulatory independence. The objective of the questionnaire was to assess how the ERRA countries performed in each of the dimensions of regulatory independence.

In the following text, received feedbacks are summarized by country. The description is purely based on the regulatory responses and information provided by the respective regulators. Complete responses to the questionnaires are attached as a separate file (appendix 5). General suggestions to ERRA members on how to improve regulatory independence and derived conclusions are given in chapter 10.

### 9.1 Abu Dhabi

The Regulation and Supervision Bureau regulates the water, wastewater and electricity Sector in the Emirate of Abu Dhabi (the "Bureau"). Pursuant to the relevant provisions under Law No (2) of 1998 Concerning the Regulation of the Water and Electricity Sector (as amended by Law No (19) of 2007) ("Law No (2)") the Bureau shall be managed by no less than three and not more that seven members, including the Chairman. The Board shall be headed by the Chairman. There is a fixed term of appointment of five (5) years which may be renewed.

The Bureau is established pursuant to Law No (2) and is a separate legal personality, and has full legal capacity to act as such. The Bureau has the sole and exclusive authority to regulate the water, wastewater and electricity sector in the Emirate of Abu Dhabi and has full powers to regulate all licensed operators economically and technically in accordance with Law No (2) and Law No (17) Concerning the Regulation of the Wastewater Sector. The Bureau submits an annual report to the Chairman of the Executive Council.

Pursuant to Law No(2) the Bureau may conduct its business according to rules and procedures determined by it which (amongst other things) establish various prohibitions on acquisitions and interests in property and contracts or taking up office with entities operating in the water, wastewater and electricity sector, and disclosure of confidential information.

The Bureau is able to resolve disputes as between sector licensed operators and customers. Such dispute resolution provisions may be written into Regulations, Licence Conditions and Agreements. Any dispute arising between a person conducting a regulated activity and the Bureau shall be determined by arbitration in accordance with Schedule 2, Arbitration Code of Law No (2).

The regulator is separate from government institutions and has a positive public image. Its public relations strategy includes maintaining an informative and up to date website, publishing quarterly newsletters on Bureau activities, and various Bureau publications available in the public domain via its website.

The Bureau has an independent budget to be approved by its members and is funded by licence fees. The Bureau may conduct its business in accordance with the rules and procedures determined it, which includes the allocation of financial resources. The Director General of the Bureau is responsible for staff recruitment, salary and promotion. Salaries are at the higher end of the regulated sector. The benefits package is the same as that in the regulated sector. Funding does not affect the performance of the regulator. The Bureau is able to achieve yearly work plans, annual special projects and recruit the necessary qualified and skilled personnel. The Bureau maintains a register of regulatory decisions. All Bureau consultation papers are disseminated to affected parties as well as posted on its website. Where the Bureau proposes new regulations or rules, model arrangements or substantial changes to existing regulations and rules, a good consultation process is followed. Pursuant to Law No (2) when promulgating new regulations the Bureau is required to consult with whom it sees fit in the sector.

## 9.2 Armenia

There is no fixed term appointment applied to the management staff of Public Services Regulatory Commission of Armenia (PSRC). On the basis of the Law on the Public Services Regulatory Body of the Republic of Armenia adopted on December 25, 2003, only commissioners are appointed for fixed terms. Commissioners are appointed using the annual rotation principle (annual appointment of one Commissioner) with a five-year term of office. According to the Law on the Public Services Regulatory Body RA, commissioners cannot be a member of any representative body, hold any other position or carry out any paid job, except for scientific, teaching and creative work, provided these works are not financed by regulated entities. In addition, Commissioners cannot hold shares, securities, or make any investments in regulated entities and upon completion of the term of office or in case of early termination of the term of office a Commissioner has no right to work in the sphere of public services within 3 years. During the period of their official duties staff members cannot carry out any paid work for regulated entities.

The Government cannot overrule / revoke decisions of the regulator. The regulator can solve disputes / conflicts between industry and customers. Any disagreements arising between license holders are settled through negotiations. Any of the parties

has the right to appeal to the Commission with a request to resolve the disputable issue within the limits within its competence.

The independence of the regulator is formally stated in the Law on the Public Services Regulatory Body adopted on December 25, 2003. The Commission is obliged legally to present to the National Assembly the program of its activities for the next year, and to publish report on its activities of the previous year.

The regulator is perceived in the society to be separate from government institutions and has a positive public image. The Commission has its own official web-site, where detailed information about activities of the Commission is update on a daily basis (including presentation of agendas for pending meetings, draft resolutions); there is a public relations department, which is in charge of these matters.

The budget of the Commission is set on the annual basis in accordance with the Law on the State Budget of the Republic of Armenia for the current year.

Regulated utilities also contribute to the state budget of the Republic of Armenia in the form of mandatory regulation fees. Every year the Commission prepares a budget of expenses and submits to the Government for approval. In the framework of the annual budget approved by the National Assembly of the Republic of Armenia, the Commission sets the size of salaries of Commissioners and staff members of the Commission. Recruitment of professional staff is done on a tender basis (Law on Civil Service). The salary level of regulator's employees in comparison with the administrative sector is higher but lower than the average salaries in the energy industry. There are no social/educational benefits for regulator's employees.

Regulatory decisions are made available on the public domain. The Commission involves relevant parties for preliminary hearings.

### **9.3 Azerbaijan**

The Tariff (Price) Council of the Azerbaijan Republic was established in 2005. The organization structure consists of a Chairman and 12 members (deputy Ministers and vice-heads of departments) 13 Commissioners. There is no fixed term applied to the management staff and there is currently no formal rules prohibiting the Council members to have interest in regulated utilities or execute leading political functions.

The decisions of the Council cannot be overruled by the Government and the Council also has the responsibility to deal with disputes and conflicts between industry and customers. In such cases the Council's role is to provide clarifications for the conflicts. Any disputes between the Council and the industry are solved through the courts.

The independence of the regulator is formally stated in the Regulation “On the Tariff (Price) Council of the Azerbaijan Republic” approved by Decree of the President of the Azerbaijan Republic of December 26, 2005, No. 341. The Council also has to report to another body.

The Council is perceived by society as having a positive public image but needs to improve its legitimacy and accountability. A public relations strategy is in place via the mass media and the internet.

The Council is funded by the state budget and has the discretion to allocate its financial resources without approval from another body. The President of the country is responsible for determining the salaries of the Council and the Secretary is responsible for staff recruitment and promotion. The average salary levels of the Council are comparable to the average salaries in the administrative sector. In comparison with the energy industry the average salaries are lower. For Council employees there are no social or educational benefits. The Council’s opinion on how funding affects their performance is that efficiency is improved and transparency is ensured.

Any regulatory decisions are made available on the public domain. In the regulation “On the Tariff (Price) Council of the Azerbaijan Republic” the procedure on involving government institutions and the regulated industry are defined.

## **9.4 Bosnia and Herzegovina**

The Commissioners will be appointed for a period of five years. No person may hold the position of a Commissioner for more than two terms. There is no fixed term appointment, applied to the management staff of the regulatory authority. However, there are some formal rules that prohibit the regulator to hold shares in regulated utilities or to execute leading political functions.

The independence of the regulator is formally stated in legislation and the regulator has the obligation to report to the Parliament. Nevertheless, the Government cannot revoke decisions of the regulator and the regulator’s jurisdiction includes resolution of disputes among system users, in alignment with applicable State Laws.

No information is available on the way the regulator is perceived in the society and no public relations strategy is in place. Therefore, the regulator agrees on the need to conduct more research on sociological independence.

The regulator is funded by licensing fees and it has full discretion to allocate its financial resources. In Bosnia and Herzegovina, the commissioners are responsible for staff recruitment, salary and promotion. In general, the salary level of regulator’s employees is higher than the average salaries in the administrative sector and equal

to the average salaries in the energy industry. In addition, no social/educational benefits are attributed to regulator's employees.

The regulator provides information on regulatory decisions to the general public and public hearings is the most usual way to involve the government institutions and the regulated industry in the regulatory process. These public hearings may have a different nature: general, technical or formal.

## 9.5 Bulgaria

In Bulgaria, the independence of the regulator is formally stated in the "Energy Sector Act", article 10. The chairman of the Commission has to submit, on an annual basis, a report to the Council of Ministers on the activity of the Commission.

The members of the State Commission for energy and water regulation are appointed for a five-year term. In addition, there are formal rules that prohibit the regulator to have interests in regulated utilities or execute leading political functions. In particular, article 12, paragraph 2 of the Energy Sector Act states the following: "The members of the Commission may not be sole entrepreneurs, stock holders, partners, managers, procurators or members of control bodies, as well as liquidators and consultants of trade companies carrying out activity subject to licensing under this Act or regulation under the Act of regulation of the water supply and sewerage services."

The regulator is allowed to solve disputes between industry and customers. According to Art. 22 of the "Energy Sector Act", the Commission shall consider complaints of consumers against licensees or of licensees against licensees, as well as, complaints of consumers against operators of water supply and sewerage.

Eventual disputes between regulator and industry are solved through contestation or in the Supreme administrative court, regional courts or the Court of Appeal.

In society the regulator is perceived to be separate from government institutions. The regulator has a clear public relations strategy that is stated in the "Energy Sector Act". Usually, the Commission carries out a public discussion with the interested persons on general administrative acts stipulated under the relevant legislation, as well as on other issues of public importance for the development of the energy sector, water supply and sewerage services. Afterwards, the Commission announces in the bulletin its final policy decision, how to apply the respective acts and the rationale for eventual changes. The bulletin is issued every 6 months and published on the web site of the Commission.

The regulator is funded through licensing fees; state budget; percentage of administrative fines and penalties and donations by persons not subject to licensing

under the “Energy Sector Act” or by persons related to them (in the meaning of the Commercial Law). The regulator does not have discretion to allocate its financial resources. This means that the budget has to be approved by the National Assembly and specified by the Council of Ministers, according to full budget classification and in quarters.

The staff recruitment process is carried out by a competition commission which consists of the immediate chief of the free position, employee or person with Law education and a representative of the human resources division. The commission may include also representatives of the trade unions of the civil servants in the respective organization and external specialists in the respective field.

Regarding salaries the minimum and maximum limits of the base salaries are established in an act of the Council of Ministers. The commission responsible for the recruitment determines the adequate compensation for the employee taking into consideration the respective position, individual performance of the employee and conditions established in the act of the Council of Ministers.

The salary level of regulator’s employees is equal to the average salaries in the administrative sector and in the energy industry. In addition, regulator’s employees participate actively in courses and projects improving their knowledge and professional skills.

## 9.6 Croatia

The CERA is led by a President and a Managing Council who are appointed for a term of 5 years. Conversely, Division Directors are appointed for a 4-year term.

There are a number of restrictions to avoid conflicts of interest. Members of the Managing Council (as well as their family members) are not allowed to hold more than 0.5% shares in any regulated utility. In addition, they cannot be members of the management or supervisory board of any regulated utility.

The specific tasks and duties of the regulator are specified in the Act on the Regulation of Energy Activities. Pursuant to the provisions of such Act, every year an annual report on CERA’s regulation activities is sent to the Parliament. In spite of that, the Government does not have the authority to annul decisions made by the regulator.

In the scope of dispute settlement, the regulator is responsible to solve disputes or conflicts between industry and customers with regards to connection to the transmission network. For disputes between the regulator and the industry the rules stipulated in the General Administrative Proceedings Act apply.

The regulator cooperates with the media and provides information to other institutions on the work and activities of the Agency. The Agency's website is a platform to provide this information to the general public. This has been contributed for the positive public image of the regulator in the society.

Regarding the way the regulator is funded two main sources have been used: licensing fees and levy incorporated in the regulated tariffs. The regulator has no discretion to allocate its financial resources being dependent on approval by the Government. Funding is not seen as an issue for the performance of the regulator.

The President and members of the Managing Council are appointed by the Croatian Parliament upon proposal of the Government of the Republic of Croatia. Decisions concerning staff recruitment, salary and promotion of other employees are made by the President of the Managing Council. The salary level of regulator's employees is very competitive in relation to salaries paid in the administrative sector and in the energy industry. Regulator's employees enjoy also from other benefits for example the possibility to attend English language classes.

In general, tariff methodologies are analysed and commented by the regulated industry and the Ministry before being set up by the Agency to ensure transparency in the regulatory process.

## 9.7 Estonia

In Estonia, the independence of the regulator is formally stated in three main documents: The Electricity Market Act, The Natural Gas Market Act and The District Heating Act. With regards to political independence, there is no fixed term appointment for management staff of the regulatory authority but public officials cannot work for or hold shares in regulated utilities.

Decisions taken by the regulator cannot be changed by the government. However, such decisions can be taken to the Administrative Court. This is particularly relevant in case of conflicts between regulator and industry. Normally the regulator solves disputes between industry and customers mainly on the following issues: prices, disconnection of network and access to networks. According to legal requirements the regulator has to report to the European Commission to provide information on the performance of the energy markets.

In terms of sociological independence the regulator is seen as separate from government institutions but no public relations strategy has been implemented.

The Estonian regulator is funded by the state budget and there are limitations in the allocation of financial resources (after the approval of the budget). The heads of divisions/departments are responsible to make proposals concerning staff

recruitment, salary and promotion but the final decision should be taken by the Director General of the regulator. The salary level of regulator's employees is higher than the average salaries in the administrative sector but lower than the level in the energy industry. In the regulator's view, an inadequate source of funding would have a negative impact on recruiting and retention of staff.

Transparency is ensured through two ways: providing information on regulatory decisions to the general public and involving government institutions and regulated industry in the regulatory process (even though this is not a formal procedure).

## 9.8 Georgia

The regulator is an independent authority established on the basis of the provisions of "Law on electricity and natural gas" and "Law on Independent National Regulatory Bodies". Management staff of the regulatory authority is appointed for a period of 6 years. Commissioners and administrative staff are not allowed to have economic personal interests in any licensee, importer, exporter, supplier or system operator. During the term of office Commissioners cannot hold membership in political parties.

The Government is not allowed to revoke decisions of the regulator. However, the regulator is accountable to the President of Georgia and to the Ministry of Energy as follows: every year, the Commission has to submit a report to them on its activities.

The regulator's role in the area of dispute settlement essentially consists in mediation and settlement processes between industry and consumers. The most common disputes are related to debt restructuring and payment of electricity. Disputes between the Commission and licensees are settled by the General Court and disputes related to violations of the constitution are handled by the Constitutional Court of Georgia.

The regulator enjoys fully financial autonomy and administrative independence. Within this framework, the regulator is funded by licensing fees and levy incorporated in the regulated tariffs.

With respect to human and organisational aspects the structure of the Administration is determined by the Commission; whereas staff recruitment, promotion and salaries are determined by the Chairman of the Commission. No significant differences may be found between salary levels of regulator's employees and salaries in the administrative sector. Conversely, salary levels of regulator's employees are as a general rule lower than salary levels paid in the energy sector.

The regulator provides information on regulatory decisions in the public domain and a consultation process is the procedure to involve interested parties in the regulatory

process. Nonetheless, the regulator needs to improve its legitimacy and accountability.

## 9.9 Hungary

The regulatory authority in Hungary is a governmental agency vested with independent powers and jurisdiction (Section 159; Act LXXXVI of 2007 on Electric Energy).

A fixed term appointment of 6 years applies to the President and vice-president of the regulatory authority. In addition, Section 167 of Act LXXXVI of 2007 on Electric Energy clearly specifies that Commission's officers may not be employed by electricity companies neither acquire ownership in any electricity company in order to minimise conflicts of interest. In alignment with section 168 (Act LXXXVI of 2007 on Electric Energy) the Government is not allowed to revoke decisions of the regulator. However, the regulator has to report to the Government (through the Ministry) and inform the competent committee of the Parliament (Act LVII of 2006 on Government Agencies).

Usually the regulator solves disputes between industry and customers mainly on the following issues: distribution activities under disposal of the 54/2003 EC and claims of big customers. In case of conflicts between regulator and industry the Capital Court of Justice is the right institution to solve such disputes.

In terms of financial independence the Hungarian Energy Office (HEO) is funded by licensing fees and it has authority to allocate its financial resources as it sees fit. The activities of staff recruitment, salary and promotion are the responsibility of the President, Chiefs of Departments, Directorate of Finance and Human Resources. The salary level of regulator's employees is higher than the average salaries in the administrative sector but lower than the average salaries in the energy industry. The regulator's employees have right to social and educational benefits through payment in kind and bonus money.

The regulator in Hungary provides information on regulatory decisions and involves the government institutions and the regulated industry in such decisions. Currently, there is no clear public relations strategy in Hungary but it is under discussion.

## 9.10 Jordan

The commissioners of the Electricity Regulatory Commission (the Council) have an appointment term of 4 years. An exception however is when the first Council Commissioners is appointed, the Chief Commissioner and the Deputy Chief

Commissioner have an appointment term of four years, one of them shall be appointed for three years and the remaining Commissioners appointed for two years.

There are formal rules that prohibit the Regulators not acquire, hold or maintain directly or indirectly any financial interest, office or consultancy arrangement, either for remuneration or otherwise, connected with generation, transmission, system operation, distribution or supply.

The Government can overrule decision of the regulator with view to facilitating implementation of the initial privatization contracts and initial IPP contracts. The regulator can solve disputes in matters of connection and supply of electric power, quality of services and electric tariff. Disputes between regulator and industry are subject to appeal to the High Court of Justice. The independence of the Regulator is formally stated in the General Electricity Law. The Commission has to report to the Prime Minister.

At present the regulator does not have a clear public image as it is a relatively young institution. Awareness campaigns in the media have been established and will continue.

The regulator is funded by licensing fees. The regulator does not have discretion to allocate its financial resources and has to seek approval from the Council of the Minister.

The Commission is the authorized body for the employment of the staff and determining their salaries and remunerations. The salary level of regulator's employees in comparison with other people working in the administrative sector is higher and equal to the average salaries in the energy industry. At present there are no social benefits for the regulator's employees.

Information on regulatory decisions is not available on the public domain however non-confidential decisions are available and shall be published. Currently, there is no procedure to involve the government institutions and the regulated industry in regulatory decisions.

## 9.11 Kazakhstan

The Agency of the Republic of Kazakhstan on Regulation of Natural Monopolies (ANMR) was established in 1999, and has 185 staff members. There is currently no fixed term applied to the management staff of the regulatory authority. Article 10 of the Law on the Civil Service set out formal rules that prohibit the regulator to have other interests and include the following:

- To be a member of representative bodies and a member of local self-governing bodies;

- To be involved in other paid activities, except for teaching, scientific or some other creative activities; and
- To be involved in entrepreneurial activities, including participation in management of a commercial organization, irrespective of its organizational-legal form.

Employees of the ANMR have the right to receive income from dividends, gains, revenues from lease of property and other legitimate sources which are not associated with the energy industry.

The Government cannot overrule or revoke the decisions of the regulator. The framework of the Law “On Natural Monopolies” specifies that the ANMR has the right to settle disputes/conflicts between the industry and consumers. ANMR has the right within its competence, to make decisions on preclusion of violations of the legislation on natural monopolies and elimination of their consequences.

Any disputes between ANMR and industry are solved in courts.

The tasks and duties of the ANMR are defined in the Law “On Natural Monopolies” and also in the Regulation of the Agency of the Republic of Kazakhstan for Regulation of Natural Monopolies approved by Decree of the Government of the Republic of Kazakhstan of October 12, 2007, No. 943. There is no formal legal requirement to report to another body.

In society the regulator is perceived to be separate from government institutions.

The ANMR is funded by the state budget and has the discretion to allocate its financial resources. ANMR’s opinion is satisfactory on whether funding affects its performance.

The regulator is guided by the Chairman of the Agency of the Republic of Kazakhstan for Regulation of Natural Monopolies, who determines priority goals and regulatory tasks and control in the state governance spheres (industries).

Governance of the management of the regulator, including recruitment of staff, salaries and promotion of employees are in the competence of the Executive Secretary of the Regulator and he/she carries that out in coordination with the Chairman of the Agency of the Republic of Kazakhstan for Regulation of Natural Monopolies.

The salary level of regulator’s employees in comparison with other people working in the administrative sector is comparable, however when compared to the salaries in the energy industry it is lower. There are no social/educational benefits for ANMR employees.

To ensure transparency of its procedures and activities the information on regulatory decisions is available on ANMR's website ([www.regulator.kz](http://www.regulator.kz)), where all information is published about tariffs (prices, rates) or their cap values and tariff budgets. ANMR involves governmental institutions and regulated industries in regulatory decision-making. For example Members of the Parliament, representatives of state bodies, consumers and their public associations, mass media, independent experts are involved during the procedure of discussing a draft of the tariff (price, rate) or its cap value for regulated services.

## 9.12 Kyrgyz Republic

The regulator is within the structure of the Ministry of Industry, Energy and Fuel Resources and there is no separation of functions and authorities between the regulator and the ministry. However the regulator is a separate legal entity that has its own settlement account, staff and structure. This is formally stated under the Decree of the Government of KR No. 86 of March 25, 2007 – “Issues of the Ministry of Industry, Energy and Fuel Resources of KR”.

In Kyrgyz Republic (KR) the Law on Energy specifies terms of office for the Director of the regulatory body and for members of the Executive Board: two, four and six years for the first, second and third Board member, respectively. The term of office of members of the Executive Board is six years (with the exception of the first composition). Members of the Executive Board can be appointed for the second time but the total length of the appointment should not exceed 12 consecutive years. There are no restrictions related to ownership of shares for members of the Executive Board.

According to article 9 of the Law on Energy, the regulator has authority to set mechanisms for handling complaints and settling disputes between consumers and energy companies and between energy companies as well. In most of the cases disputes and complaints are related to charging tariffs for end-users, compensation of damage to consumers and accuracy of bills for electricity.

The government may revoke decisions of the regulator only when a decision will contribute to worsen the social-economic situation of the KR.

At present, disputes between regulator and industry are settled by the Executive Board chaired by the Minister of Energy taking into account the interests of the Government and the ministries.

Regarding the sociological independence, the regulator needs to improve its legitimacy and accountability. There is no explicitly public relations strategy however, briefings and press conferences are held on a regular basis together with the Ministry of Energy; articles are published in press and there are programs on TV.

The regulator is funded by state budget and the allocation of financial resources must be approved by the Ministry of Finance of KR. Staff recruitment and promotion depends on the Director whereas salaries are set in accordance with the rate schedule for civil servants. The salary level of regulator's employees is lower (approximately by 30%) than the average salaries in the administrative sector and in the energy industry.

The regulator provides information only on decisions related to tariffs and there is no relevant and legally set procedure to involve the government institutions and regulated industry in the regulatory process.

In short, the regulator recognizes the need to change the current legislation to separate authorities and functions of the government, ministry and the regulatory body. Moreover, a range of provisions shall be included in the law, as follow:

- Requirements to positions of members of the Executive Board;
- Term of office and the procedure for appointing Executive Board members;
- Reasons for dismissal;
- Procedures for ensuring transparency;
- Procedures for revising decisions of the regulatory body (only in courts);
- Restrictions for Executive Board members and their family members in terms of ownership of shares of regulated companies;
- Funding at the expense of license fees;
- Submission of reports to the President and Parliament once a year;
- Mandatory placement of reports on the website; and
- Publication of reports in mass media or as a separate brochure.

## 9.13 Latvia

In Latvia, the independence of the regulator is formally established by Law on Regulators of Public Utilities and the Government cannot revoke decisions of the regulator. There is no fixed term appointment to the management staff of the regulatory authority. For Council members there are some provisions to avoid conflicts of interest during and after mandate. For example, a council member for a period of three years after the term of appointment may not be owner, stakeholder or employee of public utilities. In contrast, employees of the executive body have no specific restrictions.

The regulator shall act as an arbitrage body in conflicts concerning the provision of services by public utilities (this excludes issues on the collection of debts from customers). The Law on Regulators of Public Utilities sets a procedure to be followed in case of dispute. Such procedure determines that the regulator examines matters on the basis of its substance and nature taking into account materials and information necessary to protect the interests of third parties, as well as, opinions from independent experts.

In general, the regulator has a positive public image and prestige; however, some functions (e.g. setting tariffs) carried out by the regulator sometimes are misinterpreted by the society.

State fee for the regulation of public utilities is the source of funding of the regulator. Furthermore, the regulator has autonomy to allocate its financial resources. The Executive Director and the head of relevant department / division of the executive body are responsible for staff recruitment and promotion; whereas salaries are within the competence of the Chairman of the Regulator.

In general, the salary level of regulator's employees is equal to the average salaries in the administrative sector but lower than those in the energy industry. Further benefits exist such as health insurance and educational training courses. Funding is seen by the regulator as a source of independence.

In order to ensure accountability, the regulator has to submit to the Parliament a written report on its activities together with financial statements (properly audited) on a yearly basis.

Finally, the regulator provides information on regulatory decisions available on the public domain. If necessary the regulator can conduct a consultation process in order to involve all the relevant stakeholders. Although, opinions/ proposals obtained in the consultation process are evaluated and considered by the regulator there is no formal obligation to take them into account.

## **9.14 Lithuania**

The "Law of Energy" sets the legal framework of the independent energy regulatory commission in Lithuania and the commission members are appointed for a five-year term.

In order to minimise political interference in regulatory activities the "Law on the Adjustment of Public and Private Interests in the Public Service" covers eventual conflict of interests and prohibits a person in central or local public service to hold shares in regulated utilities. In addition, the Government cannot overrule or revoke decisions of the regulator.

The regulator is allowed to solve disputes between industry and customers. The National Control Commission (NCC) holds a preliminary extra-judicial hearing of complaints concerning acts or omissions of energy enterprises in supply, distribution, transmission, storing of energy, connection, balancing of energy supply flows and application of prices and tariffs. Disputes between regulator and industry may be solved in courts.

In the regulator's point of view there is a direct relation between reputation of the regulator and the level of energy prices. In other words, the higher the prices are the less positive is the reputation of the regulator. Additionally, the regulator does not have any public relations strategy.

Although the regulator is funded by state budget there is no need to seek approval from other entity (e.g. the government). In terms of human resources, the Chairman of NCC is responsible for staff recruitment, salary and promotion. The salary level of regulator's employees is equal to the average salaries in the administrative sector but is lower than the average salaries in the energy industry. The salary level is seen as an important factor in attracting and retaining capable staff. Furthermore, no social/educational benefits are available for regulator's employees.

Information on regulatory decisions is available on the public domain and the regulator usually involves the government institutions and the regulated industry in such decisions.

The NCC must submit an annual report to the President of the Republic, the Seimas and the Government and this report should also be made public.

## **9.15 Macedonia**

The independence of the Macedonian regulator (ERC) is stated in the Energy Law. No reference is made to a fixed term appointment for regulatory staff. However, some rules exist to avoid conflicts of interest. In particular, Commission Members are not allowed to perform any other public function or any function at political party. Commission Members (and their close family members) cannot be shareholders, stakeholders or members of the management bodies of the regulated utilities.

One of the duties of the regulator is to resolve disputes (on licensed services) between consumers and licensees or between licensees against other licensees. The disputes between the regulator and industry are solved by an Appellate Commission consisting of three members and their deputies appointed by the Parliament of the Republic of Macedonia. The Appellate Commission shall adopt decisions with majority of votes from the total number of members.

At the request of the Parliament and/or Government, ERC has to submit annual reports to them in order to be accountable. Nevertheless, the Government cannot annul the decisions of the regulator.

In terms of sociological independence the regulator is seen as separate from government institutions and with a positive public image.

Two ways of funding have been used by the regulator: licensing fees and percentage of the annual total revenue of the regulated companies. The way the financial resources are allocated is a sole decision of the regulator although the Parliament may approve the draft annual financial plan.

In Macedonia ERC's members are responsible for staff recruitment, salary and promotion. The salary level of regulator's employees is higher than the average salaries in the administrative sector and equal to the average salaries in the energy industry. In addition, Commission staff attends trainings, seminars and financial grants are available for master studies, PhD and specialization studies. In the regulator's view, funding is important to ensure independent management of the Commission and minimize any kind of external influence.

In order to guarantee transparency the regulator provides information on regulatory decisions and the participation of stakeholders and the public in the decision taking process shall be realised through invitation for the sessions. According to the Energy Law, the sessions of the ERC shall be held in public (except when it involves confidential information) and decisions shall be published in the Official Journal. This procedure is particularly important when the issues are related to tariff setting, and licenses for pursuing energy activity.

## **9.16 Moldova**

Regarding the energy sector, the tasks and duties of the regulator are formally stated across diverse legislation in the areas of gas, electricity and oil. Directors of the regulator are appointed by the Government for the period of 4 years and the Administrative Board cannot hold the position for more than 8 years. Both Law on Electricity No. 137/1998 and Law on Gas No. 136/1998 state formal rules that prohibit the Regulator to have interests in regulated utilities.

The Government cannot overrule or annul decisions of the regulator but the Director General has to report to the Parliament on activities of the Agency. The regulator solves disputes and conflicts between industry and customers via an extrajudicial procedure.

Decisions of ANRE can be appealed to the administrative court in accordance with the procedure and terms set in the Law on the Administrative Court No. 793 of 2000.

The regulator has a positive public image and its public relations strategy includes between other things cooperation with public organisations on protection of consumer rights and publications and information that is useful for consumers.

The main source of funding of the regulator are the dues for regulation. The agency has an exclusive right to use funds that are in its account.

As far as human resources are concerned, staff recruitment, salary and promotion are a responsibility of the Director General. The salary level of regulator's employees is higher than the average salaries in the administrative sector and lower than the average salaries in the energy industry. In the collective agreement additional bonuses for holidays and for vacation are established.

The regulator provides information on regulatory decisions available on the public domain. When elaborating normative acts, the Agency consults with ministries and in case of certain methodologies with the Government. Furthermore, the Agency cooperates with the central industry body, the national Agency for Protection of Competition, with the standardisation and metrology service, with ministries and other interested bodies.

## 9.17 Mongolia

The independence of the regulator is formally stated in the Energy Law of Mongolia adopted by the Parliament in 2001 and Rule of Energy Regulatory Authority approved by the Government in the same year. The former law also states that the regulator shall report to the Cabinet on a yearly basis.

The management staff of the regulatory authority in Mongolia shall be appointed by the Prime Minister initially for 2, 4 and 6 years and thereafter for 6 years (so that expiration of their terms of service has intervals of 2 years). This is in line with the established under the Energy Law of Mongolia (Art. 8.3).

The Board Members and staff are allowed to teach or, more generally, to participate in scientific activities but these cannot occur at the expense of their regulatory duties.

The regulator is in charge of solving disputes between industry and customers. The type of disputes or conflicts range from complaints about the provision of services to requests related to settlement of energy bills. The disputes between regulator and industry are solved in most of the times via negotiation.

With regards to sociological independence the regulator is separate from government institutions. It is perceived that the regulator needs to improve its legitimacy and accountability though. There is no clear public relations strategy.

The regulator is funded by licensing fees and there is no financial autonomy to allocate its financial resources. The regulator has to seek approval from the

Government. Concerning human resources, the Chairman of the Regulatory Board of Energy Regulatory Authority is responsible for staff recruitment, salary and promotion. No significant differences are found in the salary level of regulator's employees when compared to the average salaries in the administrative sector or the average salaries in the energy industry.

In Mongolia, information on regulatory decisions is available on the public domain. Nevertheless, no procedure is foreseen to involve the government institutions and the regulated industry in the regulatory process.

## 9.18 Montenegro

There is a fixed term appointment applied to the management staff of the regulatory authority. The first appointment of three members of the Board is for the period of two, three and four years, and in the second mandate the appointment is for the period of four years. Members of the Board of the Agency may not have any interest in any energy undertaking and may not be ministers or Committee member and elected person in the Parliament. Members of the Board and staff in the Agency may not be members of the Board of any energy undertaking neither have material interests, and be shareholders, major owners or staff in the energy undertaking.

The Government cannot overrule or revoke decisions of the regulator. The regulator is allowed to solve disputes or conflicts between industry and customers. Any dispute between the regulator and industry is solved by discussion and last resort would be through the courts.

The Energy Law (Of.G. RMN No 39/2003), Articles 6,12,13,14 formally state the independence of the regulator. The regulator has to formally report to the Parliament. An annual report must be submitted and financial plan for the following year is sent to the Government and is publicly available. The regulator is perceived to be separate from government institutions and has a positive public image. The Agency's public relations strategy is to introduce publicity on its work and decisions through its web site and press releases.

The regulator is funded by licensing fees. The regulator does not have discretion to allocate its financial resources.

Salaries are established by General Act issued by the Board of the Agency, and recruitment is done by the Director in accordance with general act issued by the Board of the Agency. The salary level of regulator's employees in comparison with other people working in the energy industry is higher.

Social/educational benefits for regulator's employees include housing issues for staff, covering costs for staff education, help the staff in case death of a member of a family.

Funding is an adequate solution and assuming undertakings pay regularly licensing fees; provide normal and regular work of the Agency. Information on regulatory decisions is made available on the public domain. There is a procedure to involve the government institutions and the regulated industry in the regulatory decisions.

## 9.19 Poland

In Poland the regulator is part of the central government administration and its main tasks and duties are specified in the Energy Law and other relevant acts. The energy Law Act obliged the ERO's President to report annually to the Minister of Economy.

There is no fixed term appointment applied to the staff of the regulatory authority. However, provisions exist to prohibit all staff (President, Vice President, General Director, directors of departments) to hold positions in commercial companies or conduct their own business activities as well as hold more than 10% of shares in regulated utilities.

The regulator has to solve disputes between industry and customers on the following issues: grid connection; sales; energy transmission or distribution; natural gas transport; gaseous fuels storage; natural gas liquefaction; supply of gaseous fuels or energy. The decisions of the president of the Energy Regulatory Office (ERO) may be subject to appeals (in the court).

The regulator has a positive public image but there is no clear public relations strategy. The regulator has to follow the current legal requirements in terms of access to public information. With this respect there are two kinds of Bulletins to provide information about ERO's activities and decisions:

- 1) Public Information Bulletin – concerns the structure and organisation of ERO (all administrative bodies should publish their own bulletin), and
- 2) ERO's Bulletin – where the regulator publishes information about its activities and decisions (e.g. the tariffs approved by regulator).

The website is also used to publish important information to the public.

The regulator is funded by state budget (project of budget is prepared by the Ministry of Finance) and has discretion – within a framework of means allowed him in accordance to the State Budget Act - to allocate financial resources. In spite of that, the regulator is obliged to respect rules of financial policy and state's budget discipline. In some exceptional circumstances the regulator has to get previous approval by the Ministry of Finance.

All questions regarding human resources such as staff recruitment, salary and promotion are a sole responsibility of the General Director of ERO. There are some social and educational benefits for regulator's employees. The regulator can concede loans to employees; cover part of holiday's expenses and cover part of educational expenses. In addition, employees have the possibility to participate in different courses. These benefits aren't exceptional, it is a part of state administration's functioning system.

There is no procedure to involve the government institutions and the regulated industry in the regulatory decisions.

## **9.20 Romania (ANRE)**

The Romanian Electricity and Heat Regulatory Authority (ANRE) is managed by a president and a vice-president appointed by order of Prime Minister upon the proposal of the competent minister for a period of 5 years.

According to the law in place the Commission Members and staff are not allowed to exert any trading activities and other civil servant or dignitary functions (exception of academic positions).

The independence of the regulator is formally stated in legislation (Energy Law no.13/2007) and ANRE's operation and organization rules are approved through government decision. In addition, the government or any other institution cannot overrule decisions of the regulator. Any interference of other institutions in determining the legality of an administrative act is prohibited by law.

In Romania the regulator is responsible to establish the procedure for the resolution of pre-contractual disputes and settle possible disputes between industry and customers. However, orders and decisions issued by the president can be appealed in the Administrative Litigation Division with the Bucharest Court of Appeal within 30 days following publication in Romania's Official Gazette (according to Energy Law 13/2007).

The regulator has two main sources of funding: fees obtained for authorizations and other regulatory activities levied upon the regulated companies and funds provided by international organizations. Regarding the allocation of financial resources ANRE's annual budget is subject to approval by the Prime-Minister.

The regulator is perceived in the society as having a positive public image. The regulator cooperates with the media and others institutions and provides information on its work and activities, as well as on regulatory decisions.

The president of ANRE is responsible for staff recruitment; salary and promotion.

The salary level of regulator's employees is higher than the average salaries in the administrative sector but it is equal to the average salaries in the energy industry. Regulator's employees enjoy also from other benefits such as right to receive quarterly bonus, the possibility to attend training courses, etc.

According to the current legislation on transparency of the administrative making decision process, all the public institutions with regulation functions have to make public their legislative projects of national interest. This legal requirement is equivalent to a consultation process.

## **9.21 Romania (ANRSC)**

There is no fixed term appointment for management staff of the National Regulatory Authority for Municipal Services (ANRSC). Formal rules exist that prohibit the regulator staff to have personal interests in regulated utilities and to execute political functions related to the energy industry. This is set out in Article No. 16 paragraph 2 of the Public Municipal Services Law No. 51/2006.

The government cannot overrule or revoke decisions of the regulator. Any conflicts between industry and customers are solved either by understanding between the parties or in court. ANRSC is not involved in this. The independence of the ANRSC is formally stated in legislation - Law No. 51/2006, with amendments and subsequent additions in the Government Decree no. 671/2007. There is a formal legal requirement that ANRSC report to another body. This is in Article No. 7, Government Emergency Ordinance No. 25/2007 (subordinated to M.I.R.A.) Government Decree no. 671/2.

The public image of ANRSC is good and ANRSC is permanently trying to promote transparency and openness towards the media and in the public. ANRSC does not have a specific strategy on public relations, but there is a Communication Media Department, dealing with cooperation with all directions / services / offices at the existing level authority to the media and public. The regulator is funded by licence permits.

ANRSC does not have discretion to allocate its financial resources. The Ministry of Interior and Administrative Reform has to approve the budget. The President of ANRSC is responsible for staff recruitment, salary and promotion. The salary level of ANRSC is equal to the average salaries in the administrative sector and the average salaries in the energy industry. Training courses are provided to employees of ANRSC. Information on regulatory decisions is not made available on the public domain.

Government institutions and the regulated industry are involved in regulatory decisions, for example by transmitting draft regulations on public institutions is concerned.

## 9.22 Russian Federation

The independence of the regulator is formally stated in the following legislative documents: Federal Law of the Russian Federation of 1995 No. 147-FZ “On natural monopolies”; Federal Law of the Russian Federation of 1995 No 41-FZ “On the state regulation of tariffs for electricity and heat in the Russian Federation” and Federal Law of the Russian Federation of 2004 No.35-FZ “On electricity”.

The Federal Law of the Russian Federation of 2004 No. 79-FZ “On the State Civil Service of the Russian federation” sets a wide range of prohibitions related to the civil service but no fixed term is established to the management staff of the regulatory authority.

The Government is allowed to annul acts of federal executive power bodies or to suspend validity of such acts.

The regulator is responsible for settlement of disputes between subjects of natural monopolies, consumers of services of natural monopolies and executive power bodies of constituents of the Russian Federation related to setting and application of regulated prices (tariffs) in accordance with the legislation of the Russian Federation on natural monopolies. The Federal Service for Tariffs of the Russian Federation is the body authorized to handle disagreements arising between executive power bodies in the field of regulation of tariffs.

In general the regulator is seen as having a positive public image. The regulator examines applications and complaints from citizens and organisations as well as petitions to support them in their fields of activities. Information on activities of the FST of Russia and on decisions made is published in the official edition of the FST of Russia and also in the website.

The regulator is funded by state budget and has no discretion to allocate its financial resources. Questions related to recruitment, salary and promotion are a responsibility of the head of the FST of Russia. The salary level of regulator’s employees is equal to the average salaries in the administrative sector but lower than the average salaries in the energy industry.

In Russia there are specific procedures to involve the government institutions and the regulated industry in the field of regulation of electricity and regulation of natural monopolies.

### 9.23 Serbia

The Energy Law (OJ of the Republic of Serbia No.84/2004 – Art.13 Para 1) establishes the formal independence of the regulator from any other government body, all energy entities and consumers and other legal and physical entities.

The first Agency Council in Serbia was elected with a staggered term - two members with a 3-year term, two with a 4-year term, and the President with a 5-year term. Furthermore, Art 24 Para. 1, 2, 4 and 5 of the Energy Law stipulates formal rules that prohibit the regulator to have personal interests in regulated utilities or execute leading political functions.

The Government has no authority to overrule or revoke decisions of the regulator. AERS is the appellate body against decisions of the respective network operators refusing access to their grid or decisions on refusal of connection to their grids.

The regulator is perceived in the society as separate from government institutions. Moreover, an “open door” strategy was the option adopted in terms of public relations. The strategy comprises an offensive approach to media (seminars to journalists and regular news bulletins) and a formulation of the professional identity of the Agency and organisation of internal flow of information as well as cooperation with regulators from the SEE region.

There are two main sources of funding for the regulator: licensing fee and levy incorporate in the regulated tariffs (for usage of grids). In the regulator’s view, financial independence (in particular, independence from the state budget) is crucial for the overall independence of a regulator. Once the financial plan is approved by parliament there is no need for any other approval for the usage of these resources. In Serbia, the President of the Agency Council has all the rights and duties related to human resources. The salary level of regulator’s employees is higher than the average salaries in the administrative sector. In terms of social/educational benefits training courses and exchanges with other regulators are the main benefits in place.

All regulatory decisions are usually available on the public domain but in the regulatory processes no formal procedure is mandatory (although consultations have been conducted). The regulator has to report to the Parliament of the Republic of Serbia at least once a year in accordance with the stipulated in the Energy Law (Art. 21).

### 9.24 Turkey

The term of office for the chairman and members of the Board is six years. Board members may be re-elected after expiry of their terms of office. In most cases, the members of the Board cannot accept any duty in public or private institutions during

their appointment. Within two years from the end of their terms of office they cannot be employed by, or hold shares in any legal entity related to the energy sector.

The regulator is responsible for solving all kinds of disputes in the energy field between market operators and consumers. The disputes between regulators and industry are solved by negotiations and meetings with all the interested parties.

The independence of the regulator is stated in the Electricity Market Law No. 4628. The regulator has the obligation to prepare and submit to the Ministry an annual report and other reports regarding the development of the market.

The regulator has a good reputation in the society. This is reached through an active involvement of the interested parties in the preparation of secondary legislation. In addition, all developments in the regulatory field are announced by a daily press bulletin.

The regulator is funded by different sources and it differs in terms of the type of energy market (electricity or natural gas) considered. For instance, the revenues of the regulator related to the natural gas market are made up of: participation fee; fees collected for license, publications and other revenues and grants provided by international organisations.

The appointment of Authority staff is usually made by the Board among the personnel employed at the Ministry or its affiliated and related organisations upon the approval of the related Authority or institution. The procedures regarding appointment of staff from non-public agencies and the establishment of personnel career system is determined by a regulation to be issued. The remuneration and other financial rights of the Authority staff are determined by the Board upon the proposal of the Board Chairman within the framework of the principles to be established by the Council of Ministers. The salary level of regulator's employees is higher than the average salaries in the administrative sector and lower than the average salaries in the energy industry.

The regulator provides information on its regulatory decisions to the general public. Furthermore, the regulator should take into account the comments and proposals of the market participants when preparing secondary legislation and the interested parties can also be invited to discuss regulatory issues.

## **9.25 UNMIK**

The term of appointment for commissioners is 5 years (Art. 5.6 of the Law on Energy Regulator) and for heads of department the term is 2 years (Art 24.2 of the Statute of Energy Regulatory Office (ERO)). The commissioners shall not be government officials; be politically active; work or be a shareholder of an energy company (the

same applying to direct relatives) or perform any activity subject to rise conflicts of interest. For other staff similar rules are applied as stated in Art 3/b, c of the Code of Ethic and Conduct.

The Government cannot overrule decisions of the regulator. The ERO shall establish procedures for resolving disputes in the energy sector as well as complaints. Eventual disputes between the regulator and the industry are solved by the court of competent jurisdiction depending on the nature of the conflict.

The Law on energy regulator establishes the independence of the regulator. Furthermore, article 10 of the Law on Energy Regulator determines that the Chairman of Energy Regulatory Office shall submit to the Assembly annual report (no later than three months after the end of each year).

Although the way the regulator is perceived in the society as not totally transparent it is recognized that in 2008 the awareness of the public increased considerably. This may be justified by recent decisions on new tariffs and construction of new generation capacities. So far there is no clear public relations strategy but some work is on progress in this area.

The regulator is mainly funded by licensing fees and state budget and the regulator has no autonomy to allocate its financial resources. It has to submit its budget request in accordance with the Law on Financial Management and Accountability. Commissioners' recruitment is usually proposed by the Government and nominated by the Assembly. For all the other staff, decisions on staff recruitment, salary and promotion are a duty of the ERO's board. The salary level of the regulator's employees is higher than the average salaries in the administrative sector and equal to the average salaries in the energy industry. As an indicative level, the monthly salary for members of commissioners shall be higher then the average of five monthly salaries of a public sector official.

In order to enhance transparency the regulator provides information on regulatory decisions and both the government and the regulated industry are involved in the regulatory process. All secondary legislation has been established through consultation processes and public hearings taking into account views and opinions from all interested parties.

## 9.26 Ukraine

The Chairman and members of the National Electricity Regulatory Commission of Ukraine (NERC) are appointed by the President of Ukraine for the period of six years. One person cannot be a Commissioner for more than two successive terms. In addition, Commissioners and employees cannot be involved in entrepreneurial activities, be solicitor of some third persons in affairs of the state body where he/she

works or to perform part-time work (except for scientific, teaching, creative activities and medical practice). The Cabinet of Ministers may revoke decisions of central executive power bodies fully or partially.

Independence of the Commission is stipulated in the Regulation on the NERC approved by Decree of the president of Ukraine of March 14, 1995, No. 213.

The regulator is allowed to solve disputes or conflicts between industry and customers for example, in case consumers complain about actions of suppliers. The disputes between regulator and industry are solved by means of explanations, consultations, examinations at open meetings of the Commission.

Concerning sociological independence, the regulatory authority is separated from government institutions. NERC informs general public about its activities by means of press conferences, briefings, articles, interviews and comments in media.

The regulator is funded by the state budget and the Ministry of Finance shall approve the budget of the Commission for the following year. The procedure for recruitment and promotion for regulator's employees are specified in the Law of Ukraine "On the Civil Service". The Chairman of the Commission deals with issues related to promotion, salaries and recruitment of new employees. The salary of regulator's employees is at the same level of the average salaries in the administrative sector and in the energy sector. In addition, there is a system of training and improvement of qualifications for employees of executive power bodies. Additional vacation days are also allowed for employees with minor children.

There are procedures to involve the government institutions and the regulated industry in the regulatory decisions through e.g. consultation processes. According to law on the Cabinet of Ministers the central executive power bodies are liable to the Cabinet of Ministers, they report and are subordinated to it.

## 10 Conclusions and Recommendations

This section first summarises main results from the questionnaire based on the current situation of the ERRA members. This will follow on with a description of key findings in terms of best practices based on international experience. Based on this analysis we will derive suggestions to ERRA on the role of the regulator with regards to regulatory independence. This chapter will also take into account the results of two additional surveys namely “Regulatory Benchmarking Report for the CIS” and “Regulatory Benchmarking Report for South East Europe” that have been carried out by Pierce Atwood. These two benchmarking studies are briefly summarised in Appendices 1 and 2.

### 10.1 Independence in practice: questionnaire results

Based on the questionnaire (comprising 19 questions) that was prepared and sent out to all ERRA members (see Appendix 3) we can identify some predominant features of the independence of regulatory bodies in the region Central and Eastern Europe and Central Asia. In order to facilitate interpretation of the results Appendix 4 includes some questionnaire responses graphs.

The main findings from the questionnaire are as follows:

- In most ERRA countries there is a fixed term appointment of regulators and staff that usually varies between 4 and 6 years. In a small number of countries (e.g. Serbia) terms are staggered. In 9 out of 26 ERRA members there is no fixed term appointment. These countries are Armenia, Azerbaijan, Estonia, Kazakhstan, Latvia, Macedonia, Poland, Romania (ANRSC) and Russian Federation.
- With the exception of the Kyrgyz Republic and Azerbaijan, in all other countries there are restrictions on ownership of stocks or securities or other direct or indirect financial interests in the energy sector and also from actions which could cause conflicts of interest;
- As a general rule the Government cannot overrule or revoke decisions of the regulator. However, this is not the case in countries like Jordan, Kyrgyz Republic, Russian Federation and Ukraine;
- In almost all the countries considered the regulator is allowed to solve disputes or conflicts between industry and customers and the most common type of disputes relates to the application of tariffs, connection to networks and customer’s complaints;

- Disputes between regulator and industry are normally solved through appeal to the court;
- The independence of the regulator is formally stated in legislation or statute in all the countries (exception of Kyrgyz Republic) and they are required to report to another body (e.g. Parliament, President, Ministry);
- Concerning the way the regulator is perceived in the society the answers are equally distributed among the list of statements. However, it is worth noting that some regulators recognise the need to improve its legitimacy and accountability. In most of the countries there is no clear public relations strategy although provision of information (especially on the regulator's website) seems to be common practice;
- The licensing fees and state budget are the main sources of funding among the regulators; 5 regulators are financed by only licensing fees and 8 regulators are financed by only state budget. In 9 out of 26 regulators are financed by more than one type of source. About half of the regulators considered in this paper have autonomy in allocating its financial resources;
- In the ERRA countries issues such as staff recruitment, salary and promotion are often a responsibility of one entity that may be the chairman of the commission, commissioners, executive director, etc;
- In 14 of the 26 ERRA members the salary level of regulator's employees is higher than the average salaries in the administrative sector but in 13 out of 26 ERRA members the salary level is lower than the average salaries in the energy industry. In Kyrgyz Republic the salary level is lower in both cases (i.e. when compared with salaries in the administrative sector or salaries in the energy industry). On the contrary, in Croatia the salary level is higher. In Abu Dhabi salaries are at the higher end of the regulated sector. In some countries employees may also have social and /or educational benefits;
- In Kyrgyz Republic only decisions related to changes in tariffs are made available. In Jordan information on regulatory decisions is not available on the public domain however; non-confidential decisions are available and shall be published. Information on regulatory decisions is not made available on the public domain by the ANRSC (in Romania). All other ERRA members provide information on regulatory decisions available on the public domain; and
- In addition, there is usually a certain procedure to involve the government institutions and the regulated industry in the regulatory decisions through public hearings and consultation process. This is not the case of Jordan, Kyrgyz Republic, Mongolia; Poland and Serbia.

Some additional results derived from the “Regulatory Benchmarking Report for the CIS” prepared by Pierce Atwood (as summarised in appendix 2) are also relevant herein:

- In the Commonwealth of Independent States (CIS) region there is normally only one regulatory authority which deals with different energy sectors (it might also cover water and telecommunications);
- Often regulatory authorities in the CIS region focus on price setting at the expense of areas such as licensing, dispute resolution, quality of supply and market monitoring;
- Some regulators (such as in Georgia and Mongolia) have issued a separate code of ethics / conduct, distinct from the general civil servant requirements;
- The majority of the regulatory authorities in the CIS region make decisions by majority votes of the Board;
- In many of the countries the role of regulatory bodies versus the role of other institutions is not clear and not explicitly stated in legislation;
- For the majority of the CIS countries the budgets and resources are small and are often not conceded in full by their Governments; and
- Most energy regulators in CIS region lack the explicit legal authority to play a regulatory role on the regional level.

In addition, the “Regulatory Benchmarking Report for South East Europe” (a brief summary is included in Appendix 1) provides also relevant information on regulatory development for South East Europe. It should be noted that this report includes 4 non-ERRA countries (i.e. Austria, Greece, Italy and Slovenia). Nonetheless, we present the main results as follows:

- The degree of control by the regulators over its funds varies. For example Albania, Austria, Greece, Italy, Montenegro and Turkey do not require direct approval for their budgets but each is subject to some form of budget control;
- Regulators in Bosnia & Herzegovina and Bulgaria have experienced financial pressures such as governmental control over its budget or delays in receiving its budget;
- Many regulatory authorities (in particular the old ones) in the South East Europe region share some regulatory responsibilities with other authorities;
- Still there is a gap between high levels of functional autonomy under the law and functional autonomy in practice;

- Most regulatory authorities have the power to issue tariff secondary legislation but a few, such as Bulgaria, Croatia and Slovenia, have limited authority in this area;
- Most regulatory authorities have powers to fix and approve network tariffs and ancillary services and may issue licenses for transmission, distribution supply and generation but fewer may authorise new capacity; and
- All regulatory authorities allow some form of public participation via for example public hearings but this does not mean that the public participates.

## 10.2 Key findings from best practices

On the basis of international experience regarding regulatory instruments and procedures, we summarise a number of points that have been identified with best practice around the world. A number of points will be presented for each dimension of regulatory independence in line with the structure of the paper. We also consider the recommendations from the two aforementioned papers where relevant.

### Political independence

- Staggered terms not coinciding with election cycles;
- Exception from the minister's discretionary powers;
- Restrictions on the number of employees with previous experience in the power industry may be relevant to avoid regulatory capture. On the other hand these restrictions may have negative effects in terms of gaining useful professional knowledge and experience;
- Regulatory staff should only be removed for relevant cause such as criminal behaviour and violation of code of ethics;
- Government interests may be addressed in public hearings;

### Legal independence

- Laws on regulation shall clearly define circumstances under which an employee may be removed as well as the person in charge of do that;
- The regulator shall have full authority over tariff setting;
- The regulator shall have full authority to issue licenses on the long term;
- The regulator should have authority to monitor competitive energy market;
- The regulator should cooperate with the antimonopoly authorities;

- The regulator should also have authority to establish quality of service standards;
- A code of ethics governing staff behaviour should be developed and implemented in order to provide clear basis for action against improper behaviour;
- The logic, data sources and legal basis for decisions should be consistent across market participants and over time;

#### Sociological independence

- A reputation for predictable decisions facilitates planning by suppliers and customers, and reduces risk as perceived by the investment community;
- The regulator should develop and implement a clear and effective public relations strategy;

#### Financial independence

- When possible a licensing fee or / and special regulatory charge shall be preferred as a source of funding;
- The regulator should have full authority to establish (but also held accountable for) a budget that allows to employ and contract out experts / services
- The regulator should have full authority over the recruitment process;
- The recruitment process should be meritocratic and impartial;
- Salary shall be competitive with the private sector and regulated companies;
- An effective human resources program is necessary including on-going training, professional development, access to international practices with adequate budgetary support;

#### Transparency and accountability

- A government or parliamentary budget review would strengthen accountability but may create additional administrative burden and delays if not properly managed;
- Procedures for public hearings, meetings and workshops as well as a public record of submissions and public access to written decisions are necessary;
- An annual report of activities including a financial audit should be required;

- Appeal of tariff and license decisions should only be to the courts whereas issues of market power may be appealed to the anti-monopoly organisation;
- Separate regulatory accounting will increase the transparency of regulatory reporting and tariff setting;
- The regulator should have in place sound organizational and management practices

### 10.3 Application in the ERRA countries

The different dimensions of regulatory independence as explained in this paper are linked together and usually overlap with each other. There is no fine line to separate these factors completely from one another. As explained before regulatory authorities in the ERRA countries face some constraints that influence its ability to function effectively. This typically includes funding limitations, partial lack of legal independence, some cases environment characterised by political instability and absence of stakeholder support, inherited problems from the past. Therefore the best practices presented in the previous chapter should be not mechanically transferred to each of the ERRA countries. Differing conditions within the region require individual approach towards the implementation of the suggestions, providing the countries with the flexibility to incorporate these standards according to the country-specific prevailing conditions.

For example, in the case of newer regulatory authorities the funding source may include government support in the initial period, governmental and donor support. Moreover, although the regulators may have the formal authority to act independently and according to the principles of economic regulation, they can not ignore the political and social environment in the country. In particular, regulatory decisions to eliminate cross-subsidies and introduce cost reflective prices raise usually strong political opposition. Notwithstanding that the political opposition may be mainly driven by electoral and popularity interest, the shock changes in prices may also be economically not desirable.

As perceptions regarding fairness of the regulatory process influence public acceptability of the regulatory system the key is to communicate with various stakeholder groups. This leads to the necessity to design and implement a structured public relations strategy. We acknowledge here that regulators must have the necessary resources i.e. funding, and expertise for an effective strategy which they may not have at their disposal.

In general, competitive level of salaries as well as other social, educational benefits, and good working environment are essential to attract, develop and retain highly

qualified staff. This will enable the regulator to be competitive with the other companies in the energy industry.

In terms of accountability the regulatory authorities need to carry out appropriate reports on performance. The regulator should be exposed to the stakeholders, and held accountable in this for its decision-making. Moreover the regulators should be held accountable before government or parliament for the utilisation of the agreed budget.

Finally the regulators should continue interacting among themselves and with other stakeholders by participating in regional and international organisations and take part in discussions and exchange of information to continue to enhance and support their role as a credible regulatory authority.

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## 12 Appendix 1: “Regulatory Benchmarking Report for South East Europe”

The “Regulatory Benchmarking Report” was prepared for the Council of European Energy Regulators” in November 2005. The objective of the report was to gather information and assess energy regulatory authorities in South East Europe. The Report includes the following countries: Albania, Austria, Bosnia and Herzegovina, Bulgaria, Croatia, Macedonia, Greece, Hungary, Italy, Moldova, Romania, Serbia, Slovenia, Montenegro, Turkey and UNMIK.

In 2004, an initial questionnaire was developed and sent out to participants. Information included in the 2005 report constitutes an update of the 2004 report. The 2005 report includes information from supplemental questionnaire, interviews and analysis of the legislation and practices in each country.

In the 2005 report attention was driven to six main areas where a general consensus was reached. These areas are briefly presented below.

### Unbundling, Third Party Access, Market Design and Implementation

Regulatory authorities should develop guidelines and procedures that support market development such as rules on interconnection capacity, grid codes, market rules, third party access, congestion management and quality of service.

In addition, the regulatory authority has an important role in ensuring effective unbundling, through non-discrimination and absence of cross-subsidies.

### Data Access and Market Monitoring

Regulatory authorities should have the right to request data i.e. technical, financial and operational data. The regulator should have the ability to act when data is not received or received only partially. Even when the regulator has received the data it needs to be processed.

Another issue is how to deal with confidentiality of data and, therefore, how to establish rules to ensure that data is not available to external entities.

### Staffing

All regulatory bodies shall have the appropriate staff members in order to develop their activities. They should have the ability to employ and remove their staff. If the regulator cannot offer salaries in line with those offered in the private energy sector

recruitment and retention will suffer. Furthermore, training opportunities shall be provided to increase staff competencies in market development and implementation.

#### Enforcement

Regulatory rule-making authority is another important area to be enlarged and regulators must have the ability to act as dispute settlement authorities. The use of performance or incentive mechanisms in tariff structures is seen as a method of enforcement and quality assurance that would improve regulatory strength.

#### Accountability versus Intervention

The optimal instruments of accountability are reporting provisions provided for by law, and publication of and public access to regulatory decisions, rules and activities.

Of central importance is the use of safeguards to avoid interferences into the regulatory authority's operations and decision-making processes.

#### Harmonization and International Cooperation

It is also recognized the importance of harmonizing rules and market arrangements among regulatory authorities. This could be done through for example regional initiatives and participation in international institutions.

## 13 Appendix 2: “Regulatory Benchmarking Report for the CIS”

In this appendix we summarize the results of a benchmarking exercise developed for ERRA by Pierce Atwood and supported by USAID. This exercise concerns various aspects of the regulatory experience in seven CIS countries: Armenia, Georgia, Kazakhstan, the Kyrgyz Republic, Mongolia, Russia and Ukraine. All these countries are members of ERRA.

This appendix is not intended to duplicate information on regulatory practices in the above-mentioned countries but rather to provide additional data to supplement the questionnaire developed by KEMA. The methodology used in “Regulatory Benchmarking Report for CIS” (July 2006) was similar to the one used in “SEE Regulatory Benchmarking Report” (see Appendix 1). In particular, an updated version of the previous questionnaire was distributed to CIS countries, including questions on market monitoring and data confidentiality. The report adopted the principles for independent regulatory authorities as presented in a Discussion Paper by the Council of European Energy Regulators (CEER).

Although regulatory authorities in the CIS region show significant differences in their characteristics (e.g. size and resources) and achievements they share the following main aspects:

- Each regulatory authority has strengths to be fostered and international benchmarking can help to improve performance of regulators;
- Most of the CIS regulators are in need of financial and technical resources;
- It is not always clear in the CIS region what is the role of the regulator and the role of other institutions;
- In some of the countries considered there is no stability in the regulatory body;
- Almost all regulatory authorities in the CIS region have limited autonomy in terms of budget, decision-making process, etc; and
- A large set of regulatory and related functions are assigned to regulatory authorities.

For each of the CIS countries we present below a summary of main findings from the “Regulatory Benchmarking Report for CIS”. We will focus on issues not covered in the questionnaire prepared by KEMA on Regulatory Independence.

## Armenia

In Armenia there are two regulatory authorities: PSRC and Armatomenergonadzor. The regulator is in charge of many different sectors such as: electricity, natural gas, industrial and residential district heating, water supply, drainage irrigation and sewage and telecommunications.

Regulatory decisions are taken by majority vote i.e. 3 out of 5 (no deadlock is possible). The regulator has no power to impose fines for infractions however; PSRC has applied sanctions in the form of warnings, reduction of tariffs and suspension and revocation of licenses to market participants.

The amount of budget for 2005 was around 500 thousand Euros being 77% allocated to salaries. Regarding staff selection procedure the staff members shall be civil servants and they are hired through a tender process conducted by the Council on Civil Service of the Republic of Armenia.

The regulator in Armenia has power to issue tariff secondary legislation, to fix tariffs for network and ancillary services and balancing as well as power to set connection charges. In terms of tariff application the regulator's power is restricted only when it refers to removal subsidies. Similarly, the regulator has a wide range of authority with respect to licensing. In addition, the regulator is not allowed to issue rules for new capacity but has the power to issue separate construction and operation licenses. The transmission grid, the distribution code and the market rules are a responsibility of the regulator. The same does not apply to rules regarding interconnection capacity and metering rules and charges.

In Armenia PSRC has authority to set terms of the market opening. The market opening was scheduled to begin in 2006 but this period will be probably extended.

PSRC has a specific division for monitoring licensed activities and investment programs; including review of technical and economic reports of licensed market participants and their investment programs, and monitoring compliance with market conditions.

There is no separate code of ethics/conduct but provisions on these issues can be found under the Law on the Regulatory Body for Public Services.

In general, licensed entities decide for themselves whether information is confidential or not, but the PSRC also has the right to decide whether the information is confidential.

## Georgia

In Georgia there is only one regulatory authority for energy related activities i.e. electricity and gas natural. Regulatory decisions are taken by majority vote i.e. 2 out

of 3. The annual regulatory budget in 2005 was 1.04 million Euros, 59% of which was allocated for salaries, 12% for IT and 0.4% for training. GNERC has difficulty meeting financial costs because payment for regulation is often received late and not in full (for example, in 2005 the actual budget suffered a reduction of around 50%).

The regulator has imposed fines upon a number of organisations and their managers for failure to pay regulatory fees. Other penalties or mechanisms of persuasion available to regulatory authority include revocation of licenses, fines and warnings.

Regarding the staff selection procedure usually preference is given to applicants recommended by colleagues but traditional forms of hiring may also be used.

GNERC has authority to issue tariff secondary legislation and to make decisions on tariffs by decree and individual decisions and to set residential tariffs. In addition, the regulator has power to adjust discriminatory prices and to use incentive rate making (such as performance based rates, including revenue indexing and other innovative tariff methodologies). Furthermore, GNERC has power to issue licensing rules, to issue licenses, to monitor compliance and to modify and revoke licenses. Authorisation for new generation capacity is a responsibility of the Government and the Ministry of Economy. Environmental issues are duties of the Ministry of Environment of Georgia.

Concerning the market opening process, in 1999, wholesale electricity market was established but market is not yet open to independent suppliers.

There is a separate code of ethics/conduct - Decree of GNERC n°2, of 8 April 2005.

There is a press office inside GNERC with 7 employees which communicates with the public through press bureaus and press releases.

The law in place in Georgia has general provisions on confidentiality of information. However, there has been no case where the regulator has not agreed with a company's assessment that certain information should be confidential (in one case, GNERC determination of confidentiality was appealed in court by private party – but court upheld GNERC decision).

### Kazakhstan<sup>8</sup>

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<sup>8</sup> Please note that the “Regulatory Benchmarking Report for the CIS” released in July 2006 and is not up-to-date. At present there are two regulatory authorities in Kazakhstan: 1) Agency for Regulation of Natural Monopolies 2) Agency for Informatization and Communication. Both have their local bodies in the 16 regions of the country, which act as regulators on local level. Agency for Regulation of Natural Monopolies does not only exercise control and regulation in the spheres of natural monopolies related to provision of services in the oil, gas and electricity sectors, but in the sphere of pipeline and water drainage system, as well as railway transportation, civil aviation and ports. From 2008 on the agency is authorized for licensing in the sphere of industry and for licensing control.

In Kazakhstan three institutions have regulatory competencies: the Agency; the local executive bodies and the State Energy Supervisory Committee of the Ministry of Energy and Mineral Resources. The Agency exercises control and regulation in the spheres of natural monopolies related to provision of services in the oil, gas and electricity sectors. The Chairman of the Agency arranges for and manages the work of the Agency and bears personal responsibility for execution of tasks given to the Agency and for fulfilment of all relevant functions. The annual budget for 2005 was approximately 7.3 million Euros. A tendering process is the procedure normally used for staff selection.

The authority regulator as well as the court may both set fines. The Agency sets its own level of fines based on ranges set forth in Code of Administrative Procedures whereas courts follow defined court procedures. Agency often sets fines when for example data is not submitted within a certain deadline.

The Agency has the right to develop and approve by-laws that are binding for state bodies and subjects of natural monopolies and also develop, approve and apply non-discriminatory methods for calculation of tariffs. The regulator has authority for regulated tariffs and cap values the regulator. Conversely, ancillary services and balancing are not regulated.

The regulatory authority has no authority with respect to licensing being instead a responsibility of an authorized body of the Ministry of energy. In a similar way the regulator has a limited role concerning new generation capacity having the right to exercise control over procurements. Between the different technical rules the regulator in Kazakhstan is responsible only for developing market rules.

Functions of the Agency include coordination of investment programs and/or investment projects that are taken into account when setting tariffs or their cap value, tariff estimates and also approval of the procedure for monitoring efficiency of implementation of investment programs by subjects of natural monopolies. Environmental issues are functions of the Ministry of Environment of the Republic of Kazakhstan.

The Agency has no responsibility for compiling information on market dominance, predatory and anti-competitive behaviour. The Competition Authority is the Committee on Protection of Competition of the Ministry of Industry and Trade of the Republic of Kazakhstan and there is cooperation between the Competition Authority and the regulator.

The Code of Ethics/Conduct is not exclusive to the Agency but is part of the Code of Honour of Civil Servants which specifies basic standards for behaviour of civil servants of the Republic of Kazakhstan.

The regulator has to respect all requirements set by legal acts of the Republic of Kazakhstan with respect to disclosure of information that represents commercial or legally protected secrets. According to the civil legislation confidentiality of information is determined by the owner of such information.

Currently, besides ERRA, the Agency participates in the Forum of Electricity Regulatory Agencies of countries that are members of the Organisation of middle Asian Economic Cooperation.

### Kyrgyz Republic

There is only one regulatory authority in the Kyrgyz Republic which deals with energy issues as well as partially other sectors (e.g. water, telecommunications). Regulatory decisions are taken by majority vote i.e. 2 out of 3 and no deadlock is possible.

The annual budget for 2005 was 160.000 Euros which is a common budget for the whole organization and one common settlement account. Around 66% of that budget is allocated to salaries, 2.3% is allocated to IT and only 1% is used in domestic travels. Staff members of the regulator are hired according to the "Regulation on competitive Selection of Civil Servants".

Although the Government defines general tariff methodology, the regulator is allowed to set details and instructions for implementation of the tariff methodology as well as to set connection costs. The new Decree of the President of the Kyrgyz Republic authorizes the National Agency to set tariffs for electricity, heat and natural gas.

The regulator has different powers in relation to tariff application: power to adjust discriminatory prices; power to use incentive rate making (under the law but not used) to reduce rate of return (under the law but not used) and to address needs of vulnerable populations (includes compensations and beneficial prices for energy consumption).

Regarding licensing the regulator does not have enough power to issue licensing rules but, on the contrary, may issue licenses, monitor compliance and or modify and revoke licenses.

Technical rules regarding interconnection, transmission grid and distribution code are a regulator's duty. However, the same is not valid for market rules and metering rules and charges. Market rules shall be drafted by the Government in coordination with the National Agency and subject to approval by the Parliament.

Where competition is possible, the national Agency shall encourage development of energy markets and the emergence of competing producers; create favourable conditions for competition; has authority to monitor the effectiveness of measures

intended to foster competition and notify the competent government entities with respect to violation of the antimonopoly laws. The regulator cooperates with the Antimonopoly Agency.

An internal ethics code for the National Agency exists, but clear ethical standards for all employees are governed by the “Regulation on Basic of Ethics of Civil Servants”. There are no legal consequences for violation of internal code instead in such cases it is used to be a disciplinary reprimand internally by the Chairman for staff members.

Rules of Work with Mass Media, approved by decree of the National Agency contain provisions to protect confidential information. The Executive Board of the National Agency determines whether information is confidential or not.

### Mongolia

In Mongolia there is 1 full-time regulatory authority (ERA) that has jurisdiction across Mongolia and over the main power stations and heat stations and 22 part-time regulatory board authorities in the provinces, which are responsible for regulating small utilities. A 2/3 majority vote is required to any decision-making process. No deadlock is possible as all 3 members must vote.

The annual budget for 2005 was 190.000 Euros being allocated in the following way: 45% salaries; 12% IT and 10% training and travel. The staff selection procedure consists of newspaper announcement and applicants who meet criteria requirements are selected.

ERA has the power to issue tariff secondary legislation as well as fix tariffs for network and ancillary services and balancing. Currently, the connection cost is set by order of executive directors of licensees, transmission and distribution companies. In addition, ERA has the power to require the licensees to eliminate infractions and violations and may impose fines upon executive directors of licensees and companies for non-performance.

In general, ERA has no authority to issue rules for new capacity and to authorize new capacity. Authorization for construction of power plant with capacity over 5 MW can be issued only upon permission of the Ministry of Fuel and Energy. Tendering for construction of new transmission lines and substations and for new generating capacity shall be in accordance with the Mongolian procurement law and procurement rules of international financial institutions.

Regarding technical rules ERA has power to issue rules regarding interconnection capacity; to issue transmission grid and distribution code, to issue market rules and to issue metering rules and charges.

With respect to investment planning / cost recovery the regulator has the right to revise investment plans of licensees only in terms of cost recovery.

ERA requires generation, distribution and construction licensees to submit the environmental impact assessment report with its application for applying the license. The environmental assessment impact report has a detailed plan for environment protection measures.

The market is not yet opened (being planned for 2010) but ERA is responsible for identifying timetable for market opening. ERA shall also determine eligibility of customers based on their electricity and heat load; approve business rules and market regulations and approves power purchase and wholesale prices.

There is a separate Code of Ethics /Conduct and ethical violations can be punished via administrative measures, including possible dismissal.

The regulator has no power to determine confidentiality of information. State law covers this matter and in particular, the State Intelligence Agency makes decisions about confidential information.

ERA is a full-time member of ERRA and enrolled as member of the East Asia & Pacific Infrastructure Regulators Forum in August 2005. The available budget has been insufficient to allow travel for international / regional meetings.

### Russia

In Russia there is one Federal regulatory body – the FTS and 85 Regional regulatory bodies. The FTS covers the oil, gas and electricity sectors. Decisions of the Board are made by majority votes of present members of the Board and the quorum required is 4 persons. If the votes are equal, the Chairman's vote plays decisive role; and the Head of FTS has the right to suspend the decision of the Board for the period of up to 2 months.

The FTS's budget in 2005 was 5.4. Million Euros: 40% of which was allocated to salaries, 12.5% to IT and 1.8% for training and travel. The procedure used to recruit staff for filling vacant positions is the tendering process.

The FTS is authorized to fine citizens, officials and legal entities for violation of the pricing procedures and failure to submit information and for non-execution of instructions on elimination of violations of the legislation.

The FTS of Russia sets tariffs for services relate to organization of functioning of the wholesale electricity market trading system; prices for services related to ensuring system reliability in the power sector; tariffs for services on transmission of electricity and tariffs for services on operational-dispatch control in the power sector.

The FTS has authorities to apply liability measures only for violation of the pricing procedures in terms of over or underestimation of tariffs regulated by the state. In accordance to Law on Electricity, Article 21 (1), Government can adopt measures to

protect certain categories of population to ensure that they receive financial assistance to pay for electricity.

The regulator has no power or very limited role in licensing being a duty of the Government or the Federal Service for Environmental, Technological and Nuclear Supervision. Authorization for new generation capacity is not in the scope of the FTS's activities.

The Ministry of Industry and Energy of Russia has authority to issue rules regarding interconnection capacity, to issue transmission grid and distribution code, to issue market rules and metering rules and charges.

Concerning market opening the FTS participates in elaboration of relevant by-laws and legal documents. The declared market opening is 15% although the effective is around 10%.

In Russia there is no separate Code of Ethics / Conduct applied to the energy regulator. FTS has responsibility to protect information that constitutes a commercial secret in accordance with the federal Law.

### Ukraine

In the energy sector there are three regulatory authorities: NERC, State Nuclear Regulatory Committee of Ukraine and State Energy supervisory Board. These bodies cover the following sectors: electricity, oil, gas and heat.

Decisions are made by majority vote from the total number of Commissioners. If the decision failed to get the necessary number of votes, or in case of a deadlock, the issue is included in the agenda of the next Commission meeting.

The annual budget for 2005 was 1.6 million Euros 55% of which is allocated for salaries.

NERC has the right to impose fines on licensees in the power sector in the amount of up to 13000 Euro. In addition, NERC may draw up acts on license violations; make rulings on elimination of violations; issue warnings, impose fines, appoint temporary management and suspend or revoke licenses.

Regarding human resources selection procedure set in the law on State Service includes passing an exam.

NERC has the right to issue decrees that determine tariff setting methodologies, approves tariffs for licensees involved in transmission of electricity and defines the methodology for calculating connection fees.

In the area of licensing, NERC has a wide range of powers and responsibilities such as issuing licensing rules, issuing licenses, monitor compliance and modifying

licenses. The periods of license validity are set by decrees of the Cabinet of Ministers. The establishment of technical rules regarding interconnection capacity, market rules and metering rules and charges are functions of the NERC. The Grid Code must be approved by the cabinet of Ministers.

The market open is fully previewed in law but not in practice. The regulator develops and approves market rules, exercises control over operations of the wholesale market, approves prices for purchase of electricity and wholesale prices.

There is not a specific Ethics Code to the regulatory authority, but it is part of regulation covering civil servants.

According to the instruction approved by Decree of the Cabinet of Ministers in 1998 information belongs to the state and should be labelled "For Official Use Only". This Decree grants NERC the right to determine the confidentiality of materials, with which it works; the NERC Chairman approves a list of documents that contain confidential information.

## 14 Appendix 3: Questionnaire on Regulatory Independence

### Questionnaire for ERRA Issue Paper: Regulatory Independence

This questionnaire is designed to provide information from ERRA countries on regulatory independence with a particular focus on financial independence. We appreciate if you can complete your answers and send this back to the ERRA secretariat as soon as possible.

#### Political independence

1. Is there a fixed term appointment applied to the management staff of the regulatory authority?

- Yes
- No

If yes, please state what is the term.

2. Are there any formal rules that prohibit the Regulator (i.e. Commission Members and staff) to have interests e.g. hold shares in regulated utilities or execute leading political functions?

- Yes
- No

If yes, please specify separately for Commission Members and staff.

3. Can the Government overrule / revoke decisions of the regulator?

- Yes
- No

If yes, please specify under which conditions?

4. Is the regulator allowed to solve disputes / conflicts between industry and customers?

- Yes
- No

If yes, please specify what type of disputes / conflicts.

5. How are disputes between regulator and industry solved?

#### Legal independence

6. Is the independence of the regulator formally stated in legislation/statute? E.g the tasks and duties of the regulator are specified in legislation.

- Yes
- No

Please, specify which law/decreet/statute.

7. Is any formal legal requirement to report to another body?

- Yes
- No

If yes, please specify.

#### Sociological independence

8. From the list below please choose the statement(s) that applies to the way the regulator is perceived in the society.

- The regulator is separate from government institutions.
- The regulator has a positive public image.
- The regulator needs to improve its legitimacy and accountability.
- Other(s)

If other(s) please specify.

9. Does the regulator have a clear public relations strategy? If so, please describe/comment in detail.

#### Financial Independence

10. How is the regulator funded?

- Licensing fees
- State budget
- Levy incorporated in the regulated tariffs
- Percentage of administrative fines and penalties
- Other(s)

If other(s), please specify.

11. Does the regulator have discretion (e.g. do not have to seek approval from e.g. the government) to allocate its financial resources?

- Yes
- No

If not, please specify from whom the Regulator has to seek approval.

12. Please indicate the job title (e.g. president, Chief of Department) and the respective organization (e.g. regulator, government institution) who is responsible for each of the following functions – staff recruitment, salary and promotion

13. How is the salary level of regulator's employees in comparison with other people working in the administrative sector?

- Higher than the average salaries in the administrative sector
- Equal to the average salaries in the administrative sector
- Lower than the average salaries in the administrative sector

14. How is the salary level of regulator's employees in comparison with other people working in the energy industry?

- Higher than the average salaries in the energy industry
- Equal to the average salaries in the energy industry
- Lower than the average salaries in the energy industry

15. Are there any social/educational benefits for regulator's employees?

- Yes
- No

If yes, please state the most important ones.

16. In your opinion, how does funding affect the performance of the regulator?

**Transparency**

17. Do you provide information on regulatory decisions available on the public domain?

- Yes
- No

18. Is there any procedure to involve the government institutions and the regulated industry in the regulatory decisions (e.g. consultation process)?

- Yes
- No

If yes, please specify.

**Other comments**

19. Any other comments you would like to make with respect to regulatory independence?

## 15 Appendix 4: Questionnaire Responses Graphs

### Questions on Political independence

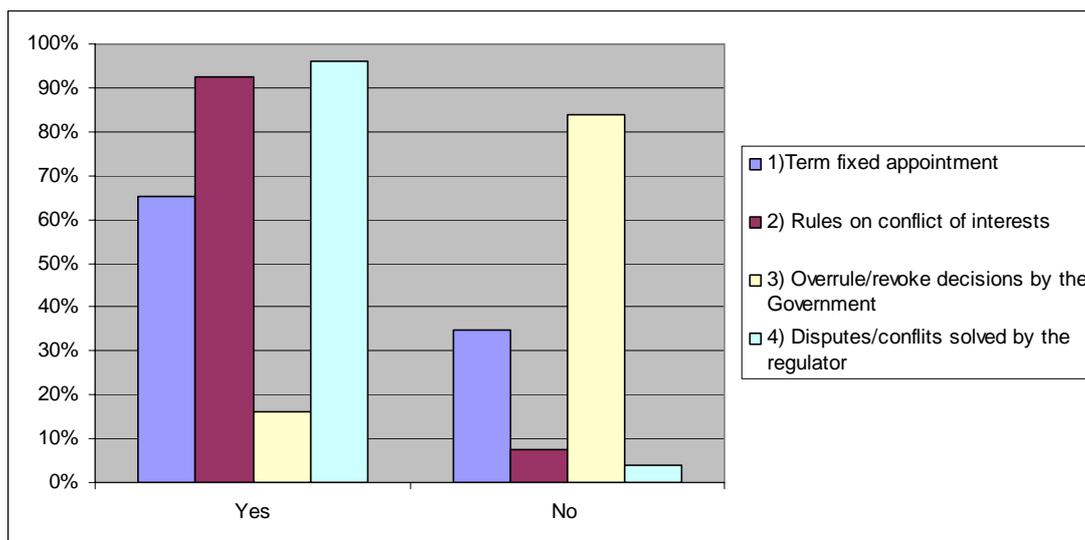


Figure 5: Questions 1 to 4 (Percent of responses)

### Questions on Legal independence

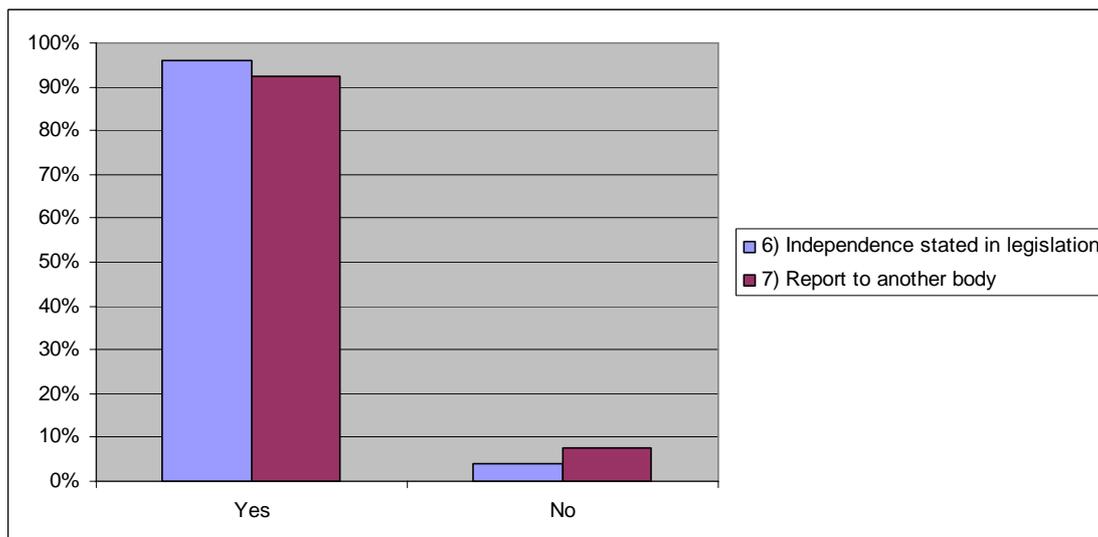


Figure 6: Question 6 and 7 (Percent of responses)

Questions on Sociological independence

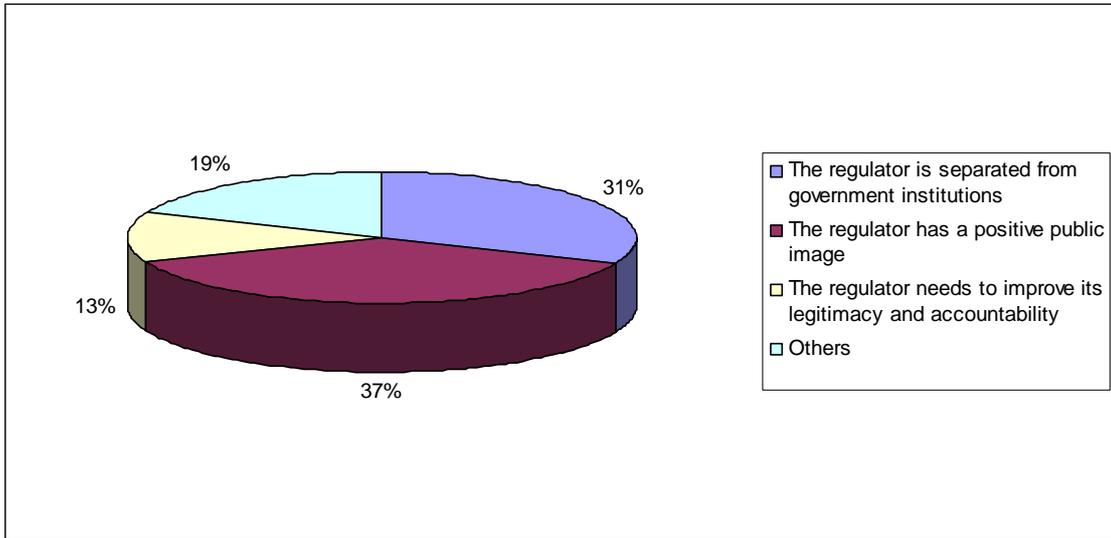


Figure 7: Question 8 – how the regulator is perceived in the society (Percent of responses)

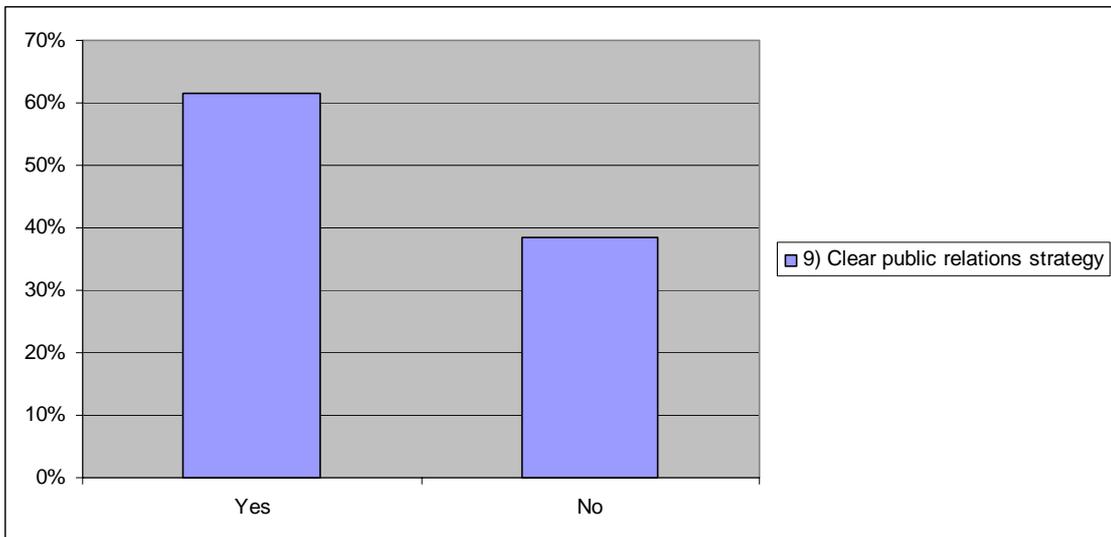


Figure 8: Question 9 (Percent of responses)

Questions on Financial independence

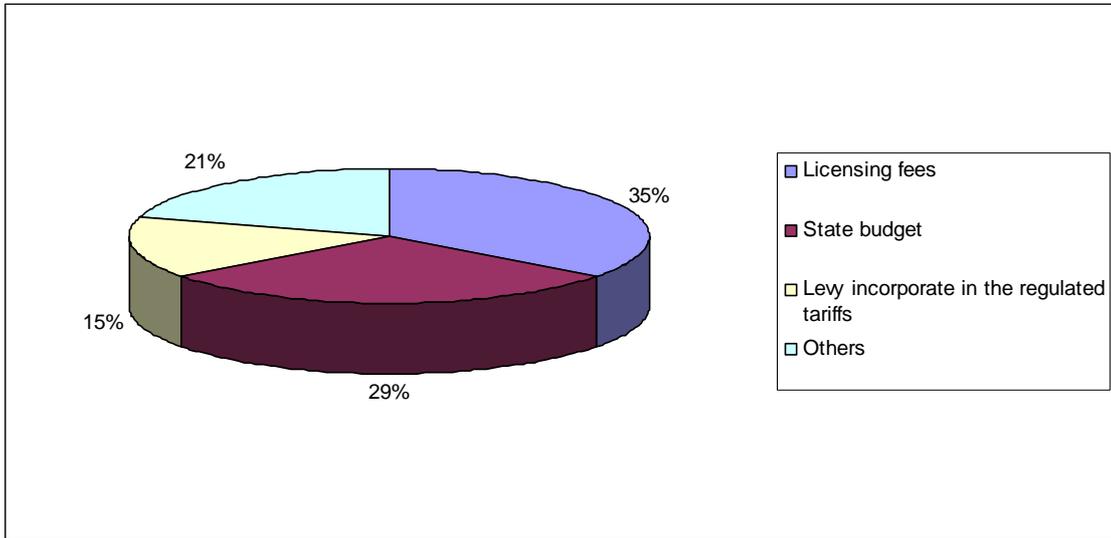


Figure 9: Question 10 – how is the regulator funded (Percent of responses)

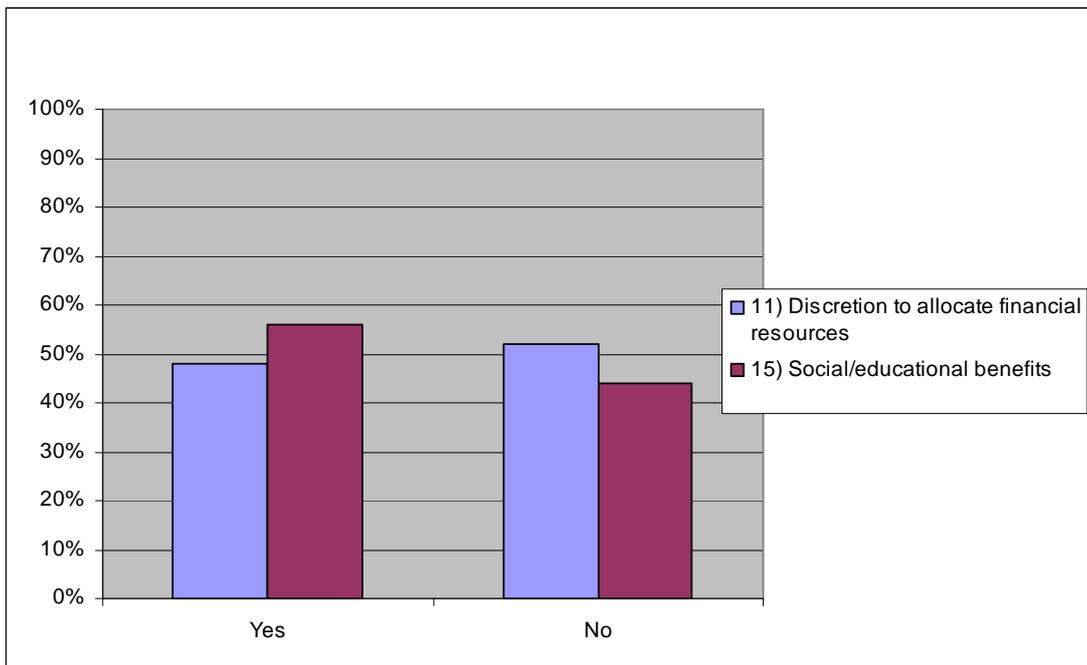


Figure 10: Question 11 and 15 (Percent of responses)

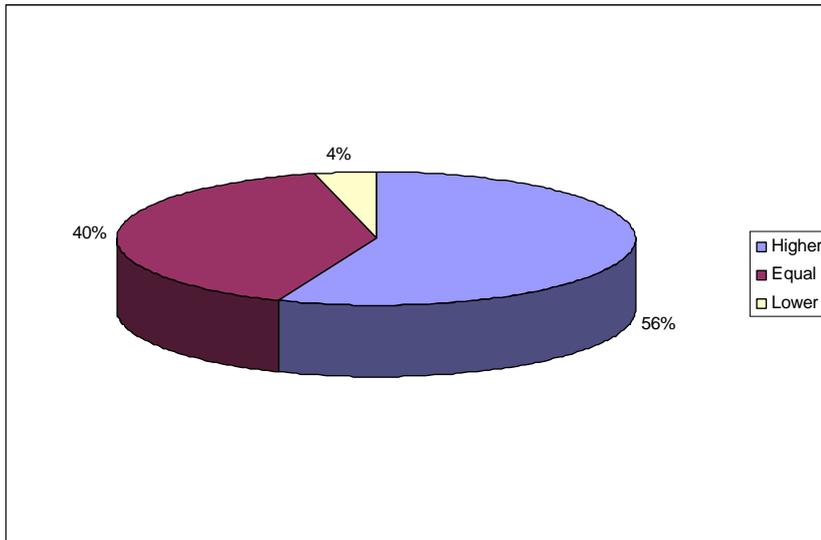


Figure 11: Question 13 – salary level of regulator’s employees in comparison with other people working in the administrative sector (Percent of responses)

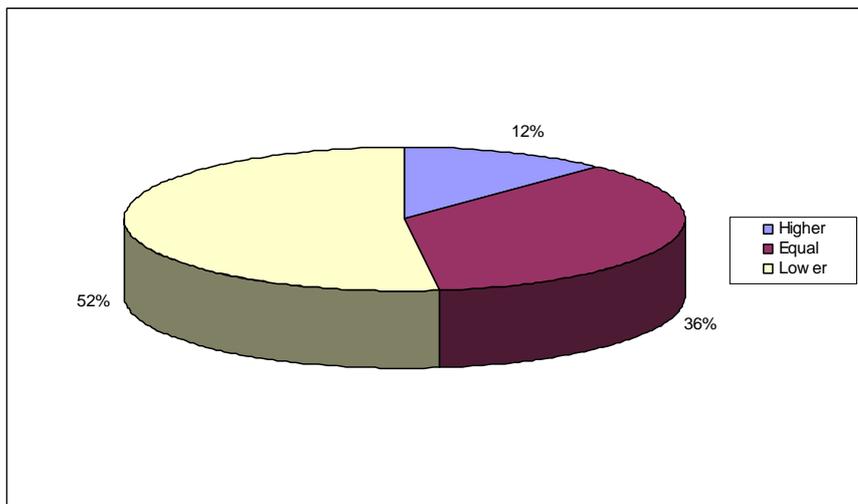


Figure 12: Question 14 – salary level of regulator’s employees in comparison with other people working in the energy industry (Percent of responses)

Questions on Transparency

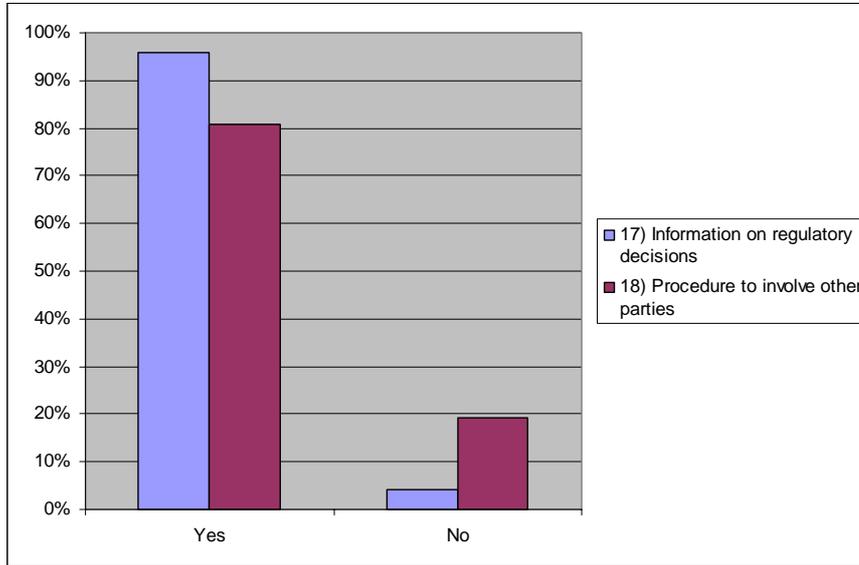


Figure 13: Question 17 and 18 (Percent of responses)

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**16 Appendix 5: Questionnaire Responses (included in a separate document)**