

Autorità per l'energia elettrica e il gas

**ANNUAL REPORT ON REGULATORY ACTIVITIES AND  
THE STATE OF SERVICES**

*Introduction by the President*

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President of the Republic  
President of the Chamber  
Deputy President of the Senate  
Ministers  
Authorities, Ladies and Gentlemen

In presenting the eighth “Annual Report by the Authority for Electricity and Gas on the State of the Services and the Activities Carried Out”, I wish, together with my colleague Tullio Fanelli, to express my particular thanks to you, as President of the Republic, for granting us the great honour of your presence, and to the Hon. Casini, the President of the Chamber of Deputies, for offering such distinguished hospitality for this event and for the recent initiative he has taken together with the President of the Senate, Senator Pera, whereby the Authorities’ “reports” will be followed up by more in-depth discussions with the Parliamentary Committees.

## INTRODUCTION

The security of the electricity system, which experienced serious problems throughout much of 2003, has regained a substantial degree of stability that should be consolidated in coming months. In 2004, albeit in the presence of a continuous growth in demand, no signs of risk emerged, thanks to the increased availability of plants as promoted by apt legislative and regulatory measures and by a power exchange that has now successfully completed its initial “run-in” stage.

That said, the electricity market cannot be deemed to be fully up and running; a number of problems are still holding it back from expressing its full potential for the attainment of transparency, competition and security. These include the continuing excessive weight of the dominant operator, imperfections in the role played by active demand, and the incomplete development of the markets for the despatching and reserve services. These problems can be overcome with the cooperation of all actors involved with a view to reducing the current, penalising differences between the Italian and European prices of electricity generation.

Significant improvements have been achieved in the quality of the electricity services, while the trend allows us to envisage further positive developments.

The situation appears more critical for natural gas. Demand that is growing by 4% annually has not yet met with an adequate response on the supply side. The warnings voiced for some time now by the Authority regarding the inadvisability of continuing to fear an excess or “bubble” of gas were confirmed, unfortunately, in the crisis of March this year. At that time, as a result of a tail-end of wintry weather conditions – albeit after a winter that was not particularly cold – a number of emergency procedures had to be called into play, eating into strategic reserves and calling into play the interruptibility clauses in a number of contracts.

Therefore, as already noted, measures will soon need to be adopted to up-grade the infrastructure for the import and storage of natural gas, not just for obvious security-related reasons but also to ensure the supply levels appropriate to a competitive domestic market that is in a position to present its candidacy as a European hub, to the benefit of consumers in Italy and the European Union. To this end, an independent system operator needs to be set up as soon as possible, as has been done for the electricity sector, to engage in transport and storage activities and in the development of systems for the intake of gas at our borders.

### **International scenario**

The international energy scenario has been characterised by strong and systematic increases in the prices of fossil fuels. The progressive rise in oil prices continued throughout 2004 and, in spite of a slight cooling-off in the first part of the year, price levels remain high, at more than double the average for the 1990s. The burden for Italy has recently reached new historic peaks, partly as a result of the changes in the euro/dollar exchange rate. The rise in prices is undoubtedly linked to increased global demand but this increase, which has been particularly marked in the emerging economies, cannot be considered the only source of the strong rises we saw last year. Inadequate investment in the extraction and refining segments of the oil supply chain has translated into constraints that have prevented supply capacity from keeping pace with growing demand. Moreover, to the already high prices of crude oil has been added excessive speculation accompanied by marked volatility.

The strong rise in the oil price, of over 60% since the start of 2004, has in turn exerted an overly strong influence on the natural gas market, notwithstanding the greater balance between international demand and supply in this sector. The extent of the prices rises is not actually directly justified in market terms but is linked to the excessive and inappropriate dependence of the gas price on the price of fuel oil. If we consider the fact that national electricity production will depend increasingly on natural gas, we need to persist in our efforts to ensure that gas price trends become increasingly uncoupled from those of oil.

With respect to coal, a competitive fuel that can be used with technologies that are increasingly respectful of the environment, the strains on demand experienced in the first part of the year seem to be gradually easing off.

In an international context generally characterised by burdensome markets for the supply of fossil fuels, and hydrocarbons in particular, and by challenging objectives with respect to environmental protection and sustainable development, it seems necessary to promote an increasingly rational and efficient use of energy along with a mix of cover that can reduce the strong and persistent national dependency on imports.

This should be done while developing the cost-effective use of renewable sources, for which the Authority has agreed on further incentives.

### **European regulatory framework**

At the European level, the regulatory framework established in 2003 with the second package of Directives for the single energy market is now nearing completion.

However, this appreciable and demanding process should be matched with greater synchronisation in the process of harmonising the different national legislative frameworks (for example the tax, environmental, and economic-industrial frameworks) that after all have a significant influence on the cost, price and competitiveness differentials and comparisons applying to the Italian energy system in the European context.

### Cross-border trade

In 2004, the operational steps for the implementation of the regulation on cross-border electricity trade were initiated. A detailed timescale was then established for the introduction of coordinated market mechanisms to resolve congestions – a significant issue for Italy, as a major electricity importer – in a way that is compatible with the electricity markets already operating and with reasonably priced solutions for Italian consumers. In this respect, timely international agreements should be promoted to enable the allocation of import capacity for Italian customers to be brought forward with respect to previous practice.

Also worthy of note is the regulation on cross-border trading of natural gas. This is intended, *inter alia*, to iron out those disparities in systems of access to the various European transportation networks that are still causing an under-use of interconnection capacity and limited development of the market.

### Kyoto Protocol and emission rights

The instruments and objectives to limit climate-changing emissions have now become effective in compliance with Directive 87 of 2003. The trade in emission rights was deemed to be the most effective mechanism to achieve the goal of reducing greenhouse gases, the objective of the Kyoto Protocol, which entered into force in March 2005 following ratification by the Russian Federation.

In recent weeks the Commission has given a conditional go-ahead to the Italian plan for the allocation of emission rights, while requesting considerable amendments to the original draft. As we have observed, the quota threshold assigned to the electricity sector and the envisaged allocation mechanism both present some thorny issues, including from the point of view of competition. On the one hand, the size of the quotas reserved for the sector and distributed on the basis of the current, strongly concentrated market structure are limited compared with requirements; and on the other, the market in emission rights has risen sharply over the last few months.

To lessen the burdens currently weighing mainly on electricity generation it might also be timely to bring other sectors that are responsible for emissions (for example transport) into these environmental commitments and to enhance the flexible mechanisms that are also envisaged by the Kyoto Protocol, thus providing a global response to a climate change, which is after all a global problem.

## **Italian regulatory framework**

One of last year's most significant new developments in energy matters was the "Marzano" Law (No. 239), a provision that was already discussed in the last report.

Another significant provision was the Prime Minister's Decree for the unification of the ownership and management of the national electricity transmission grid. This Decree also adopted a number of recommendations by the Authority that are intended to guarantee the independence and impartiality of the company with responsibility for developing and managing the grid.

For 2004, the two ministerial decrees designed to promote savings and efficiency in final uses of electricity and natural gas, the implementation of which falls within the Authority's remit, are also worthy of note.

### Implementation of European Directives

One year on from the entry into force of the new European Directives, it would seem timely to speed up the implementation process, which is marking time in other countries also. For this very reason Italy, which has already forged well ahead in the drive to market opening, could issue a signal for a resumption of liberalisation processes in the EU. The risk here, however, is that we might see imbalances becoming more firmly established in the Union itself, imbalances that would definitely not be advantageous to our country. At the same time, the implementing decrees are an extremely useful means of giving a new impetus to national liberalisation processes; to this end we hope that the recommendations already advanced by the Authority will be taken into consideration and that this presentation will to some extent serve as a timely reminder of them.

### Independence of Snam Rete Gas

The Council of Ministers has approved the draft Prime Minister's Decree concerning the criteria and arrangements for the divestment of ENI's holding in Snam Rete Gas.

This provision also considers some aspects of the Authority's observation of January 2005, calling for the neutrality of the operator responsible for the transport of natural gas in line with the solutions already selected for the electricity grid, which guarantee independence, transparency and non-discrimination in the services provided.

### Sanctions

Of particular importance in enhancing the effectiveness of the Authority's action is Law 80/2005, since it eliminates the possibility for sector operators in effect to disregard any penalties they may have incurred, by making derisory payments. In measures that meet with our complete approval, the new law devotes the revenue from penalties imposed by the Authority to consumers, under rules for which we will collaborate fully in the drafting process.

## **Liberalisation, Market and Competition**

### Electricity sector

As of 1 January 2005, the first stage in the launch of the electricity market was completed, thus opening the way to the active participation of demand, albeit still only for certain market segments.

The transition in 2004 to a merit order economic despatching model that uses market criteria to establish the supply price has led to a stronger focus by the Authority on its investigative and control activity.

In February 2005 the fact-finding investigation on the progress of the liberalisation of the electricity sector, jointly conducted in a fruitful collaboration with the Antitrust Authority, was published. This came after a similar investigation of the gas market, on which we reported last year.

The new survey, which concentrated on the wholesale electricity market in 2004, confirmed the serious problems connected with the role of Enel, the dominant operator, which is able to exert a high degree of market power and therefore a strong influence in price setting.

The principal lines of intervention proposed in the conclusions of the investigation concern not just regulatory solutions but also actions to promote: the development of interconnection lines with abroad; the up-grading of the national transmission grid in such a way as to reduce the risks of international congestion; and the activation, by actors other than the dominant operator, of new generating facilities, especially in areas suffering shortages in supply.

Again in February 2005, the preliminary investigations into price-setting dynamics in the power exchange were completed. These concerned a number of days in June 2004 and January 2005 when anomalies were found with respect to the values recorded in the day-ahead market and in transportation capacity usage charges. The aim of the investigation was to evaluate whether market power was exercised – unilaterally or collectively – by one or more operators.

The comparison between critical days and other weeks with comparable characteristics demonstrated that the exceptionally high price level could be traced back not to specific situations such as a demand or cost shock, but solely to the conduct of suppliers Enel and Endesa. As a result of these findings the procedure envisaged by law was activated with the matter being reported to the Antitrust Authority, which then took the appropriate steps.

On the basis of the conclusions reached through this intensive investigative activity, the Authority recently opened a procedure and published a special consultation document with a view to restoring competitive market conditions through actions, some of which temporary and in any case proportionate to requirements, that remove power availability from the dominant operators for certain types of installation.

The actions concerned are structural or, better, regulatory measures which, through contractual constraints or pre-established arrangements to remunerate particular installations, make it possible to reduce the dominant operators' power to set prices in some areas of the country wholly independently of competitors' market conduct. These measures, soon to be issued by the Authority, are needed to anticipate the effects of a fully competitive market that we trust will be able to develop in a few years time once the power stations currently under construction are fully up and running.

Also worthy of mention is the Authority's initiative to promote adequate availability of power over time with a system for the remuneration of generating capacity (in accordance with the provisions of Legislative Decree 379/2004) that replaces the current transitional system.

The Authority's recommendation, which has already been put to open consultation, is intended to delineate a new model for the remuneration of generating capacity that is based on market mechanisms and also takes into account international experience and the structural conditions of the Italian market.

#### Gas sector

As regards the degree of liberalisation of the natural gas market, activities involving the entire supply chain in the sector continue to be strongly concentrated in ENI: production, imports, transport and sale. In effect, the entry of new operators to the market through gas release programmes has not yet resulted in the benefits of competition being passed on to consumers.

The infrastructure for interconnection with abroad is mainly used for import contracts linked to take or pay contracts, many of which were entered into by Eni shortly before the European Directive of 1998 on market opening entered into force. In the short-term, marginal transportation capacity made available by the flexibility of some import contracts also appears difficult to use, since the absence of a European regulatory framework for tariffs and for transparent, non-discriminatory access to international gas pipelines means that its use is still fraught with difficulties.

To encourage initiatives concerning these fundamental issues, the Authority has already produced timely observations, the European aspects of which have also been notified to the European Commission. The aspects relating to the Italian market also include a number of recommendations, which include: the divestment by ENI, under competitive conditions, of a portion of national production and long-term import contracts; and the reformulation and raising of the ceiling on injections, which for ENI is due to expire by the end of 2010.

Another problem specifically affecting our country is the continuing excessive fragmentation of gas distribution, which is still in the hands of about 500 distributors. The reduction of this fragmentation should be further encouraged, thus paving the way for economies of scale and new opportunities to reduce costs and prices.

#### The issue of infrastructure

As mentioned earlier, competition is struggling to gain ground in the Italian natural gas market. New entrants continue to encounter difficulties in arranging imports on their own, because ENI still controls transport rights for the access infrastructure; this is used in full by ENI itself, with partial releases of gas decided, once again, by ENI.

The development of import infrastructure will therefore be a decisive factor in creating an efficient market and transforming our country from an importer to a platform for trade or southern European hub, with the direction of flows being diverted to supply the rest of Europe and with low-cost transits for gas from the rich fields to the south and east of the EU. This transformation should be implemented in a rapid timescale, not least in view of the investments already being promoted for competitive links from North Africa and the Middle East through the Iberian Peninsula and the Balkans.

In the face of a challenge of this nature, new local opposition is now being voiced to plans to construct long-awaited new regassification terminals for liquefied natural gas imports arriving by sea, while ENI has split up and staggered over time the up-grading, by 13 billion cubic metres, of the pipelines already operating with Austria and Tunisia.

The crisis last March that I mentioned earlier, along with the continuing lack of competition and the need for new players, mean that there is no longer time for disputes over gas “bubbles”. What is needed is more rapid action to overcome the infrastructure bottlenecks that we and the Antitrust Authority have already highlighted.

The situation requires a committed effort by all concerned to ensure that the country can rapidly equip itself with a sufficiently abundant import and supply potential to ensure security of supply and provide choice for Italian and European demand in a suitably equipped, efficient and competitive market.

#### Independence of the system operator

The liberalisation process for the gas sector also requires the prompt implementation of the Prime Minister’s Decree mentioned earlier and supplementary provisions to ensure the neutrality of the transport service, in line with the electricity grid, and to gas storage facilities. This can also be done by adopting solutions that limit ownership in Snam Rete Gas and Stogit to holdings of 5%, entrust the management of import transit rights to Snam Rete Gas under fair and non-discriminatory conditions, and promote the grouping of transport and storage under one truly independent system operator.

#### Retail

In the natural gas retail segment, even in the presence of sales permits applicable countrywide, sales companies linked to distribution companies continue to predominate at the local level, sometimes operating through customer communication instruments designed to obstruct transparent competition.

Although all gas service consumers have been free to choose their supplier since January 2003, only recently have we seen competitive commercial strategies being adopted. To support this transition phase, the Authority has drawn up a Code of Commercial Conduct that benefits consumers by enabling them to make informed, aware choices from the various opportunities that are emerging. The Code imposes precise obligations regarding information transparency, the arrangements for presenting offers, price comparability, the breakdown of the different elements making up the final price, and simplicity in the wording of contracts. By establishing uniform rules of conduct throughout the country, the Code paves the way for competition among buyers under equal conditions and in this respect too can be seen as a spur to competition.

#### **Cost effectiveness of services**

In international comparisons energy prices in our country rank amongst the highest in Europe, although the gap is narrowing as a result of the larger increases recorded in other EU countries. This applies both to the captive market for electricity (composed until July 2007 of smaller consumers and households) and to customers who are already free to negotiate directly with sellers or producers.

It should however be noted that the current trend in oil and hydrocarbons prices on the world market (fuels on which our market is highly dependent) is still travelling at



worrying levels. Partly as a result of the changes in the euro/dollar exchange rate, these remain very high, with historic peaks that in the last few days have exceeded €48/barrel.

The fuel costs associated with recent onerous decisions by the Regional Administrative Court (TAR) of Lazio, and with the latest fiscal regulations and the continuing slow pace of competition in energy markets, make the question of containing electricity and gas prices and tariffs a very difficult one indeed.

### Electricity

For industrial users, electricity prices, both net and gross of taxes, continue to be higher in Italy than the European average.

More specifically, for the central categories of industrial consumers, i.e. those using from 2 to 20 million kWh/year, Italian prices net of taxes are over 35% higher. Again net of taxes, in 2004 the electricity used by lower consumption categories increased by more than 3 percentage points with respect to the European average. For high consumption industrial users a fall of 5 percentage points was however recorded. Overall, and with respect to the rises experienced by European countries as a whole, the economic gap between Italian and average European values has begun to narrow slightly.

For the captive market the average national tariff was c€10.67/kWh net of taxes, which account for about 10% of the gross total. In spite of the efforts to contain tariffs, the levels set for the current quarter are in fact 6.3% higher in current terms and 4.6% higher in constant terms than those for the same period of 2004. If we compare the current tariff with the tariff for the equivalent period in 1999, the year in which the liberalisation process began, we find an increase of 20.8% at current values and of 4.6% at constant values, compared with a rise of 260% in oil prices.

If we analyse the tariff for the captive market, we find that the components regulated by the Authority have been falling constantly for some years; indeed the costs for transmission, distribution and sale, which amount to just 21.6% of the tariff, have already reached levels that are better than the European average.

The Authority also devotes particular attention to the semi-fiscal element of system charges (which accounts for 10.7% of the tariff) with a view to containing or reducing it; for this reason a wide-ranging campaign of controls and inspections has been conducted against improper charges, especially those involving the most significant components such as CIP6 incentives (for electricity produced using renewable and assimilated sources) and tariff supplements for smaller electricity firms.

In parallel with this, and without prejudice to initiatives to promote research and development, steps should be taken to avoid further commitments (for example, extensions in terms of either duration or sector of tariff benefits for certain industry segments) or levies (for example, from funds for dismantling nuclear power stations or for ICI (local property tax) on power stations) that increase energy prices.

The main tariff component is the one linked to production prices: it accounts for 67.8% of the net tariff. It is a structural tariff element and is particularly significant in the Italian case, as a result partly of the still insufficient degree of competition but mainly

of the strong exposure to oil prices of Italian electricity generating costs. Nearly 60% of Italian electricity generation depends on natural gas and fuel oil, while if we take the European average (therefore including the Italian figure) the same percentage is represented by coal and nuclear.

We need therefore to devote particular attention to diversifying our production mix and to the growing weight of natural gas in this mix. One estimate that takes into consideration the entry into operation of all planned new power stations places the share occupied by gas at over 50% in just a few years. For this reason, we still need to make every effort to ensure that during the highly desirable uncoupling from the oil market we do not give way to a situation where the gas price is still based too closely on oil.

As mentioned earlier, the high price of electricity generation in Italy can partly be explained by the fact that the market has still to feel the full effects of liberalisation and competition.

However, the entry into operation of new power stations, the consequent improvement in the efficiency of the country's generating capacity, the transparency that is gradually gaining ground (thanks in part to the power exchange) and the regulatory and legislative measures that have been adopted are all beginning to produce positive price signals, at least in some hourly bands in those areas of the country where more generating capacity is concentrated. The Authority fully intends to support these competitive tendencies and initiatives, with the cooperation of all stakeholders in the sector.

Marked differences still remain between the different categories of consumers. For domestic customers there is an indiscriminately progressive tariff structure that is accentuated by the tax element and, in the even more widespread non-time-of-use version, does not provide sufficient encouragement for the rational use of energy. For example, a single person living in Italy, with relatively low consumption (600-1200 kWh/year), pays prices that can be as low as half those prevailing in Europe. A large family, however, with higher consumption (3,500-7,500 kWh), has price levels, net of taxes, that are 42% higher than the European average; the gap has however narrowed compared with last year, by 5 percentage points.

This illustrates the importance of creating a tariff structure that provides better incentives for all consumers to adopt virtuous energy behaviours, while safeguarding those requiring some form of social assistance. On this matter we await the necessary guidelines from the Cabinet and Parliament so that we can begin work on defining the social tariff in the framework of an overall review of the tariff structure.

This review would also make it possible to provide a better base for the development of new, wider and increasingly well-structured time-of-use tariffs, as some distributors have already suggested but which still have only a limited potential impact for medium and small consumers. While we are pleased to note that in the last few months more than 350,000 consumers have chosen two-tier tariffs, we feel that more can and should be done in this area, by taking initiatives that also encompass metering activities.

## Gas

I will spend somewhat less time on the gas sector, because some issues have already been covered in the part of this presentation devoted to the market and because the Authority only sets a benchmark tariff as all consumers are already free to choose their provider. The benchmark tariff, which sellers are required to offer, is c€0.06/cubic metre including taxes; this shows an increase of 6.1% at current values (4.3% at constant values) if we compare the present quarter with the same period in 2004, mainly as a result of the trend in international hydrocarbon prices. Compared with the same period of 2000, the year the liberalisation process began for gas, and against an increase of 70% in the oil price, the current tariff is 2.9% higher at current values and 8% lower at constant values.

Prices, even net of taxes, are generally higher than the European average and show considerable consumption-based differences between one customer category and another. While small domestic users benefit from gas prices that are amongst the lowest in Europe, the cost of consumption for individual or collective heating is about 14% higher than the European average.

Prices for consumption levels of around one million cubic metres per year are, on the other hand, in line with the European average. However, a growing gap once again emerges between Italian and European price levels when higher volumes are considered: for example, a factory that consumes 10 million cubic metres per year pays 11% more for its gas than an EU competitor.

In many situations, the low degree of competition in the market has in effect enabled sellers to avoid transferring to consumers a large enough proportion of the considerable reduction the Authority has gradually brought about in the costs of the regulated infrastructure services, transport and distribution, which account for 19% of the benchmark tariff gross of taxes.

Raw materials account for 25.7% of the tariff. This amount is deemed by the Authority to be disproportionate to the actual costs of supplying gas, which are only partly related to the oil price. For this reason, in its resolution of December 2004 the Authority reduced the cost of supply as allowed in the tariff, but this resolution was subsequently suspended by the TAR pending the hearing that will be taking place in the next week or so. The suspension has led to a tariff increase of 1.6%, which is currently being borne by consumers; we trust that the increase can be recovered, given that the information in the Authority's possession confirms without a shadow of doubt that the average cost of supplying gas in Italy has increased by less than the amount currently allowed in the tariff; this is causing unfair over-remuneration to the sole benefit of operators' profits.

Finally, it should be noted that taxes make up a robust percentage of gas tariffs, higher than is the case for electricity tariffs. Italian prices are affected by a fiscal burden that, for consumption of less than 200,000 m<sup>3</sup>/year, amounts to 45% of the final price.

On this subject, and on the need for a restructuring of the fiscal burden (excise duties, VAT, regional surtax) on gas and electricity prices, the Authority considers further discussion with the Parliament and Cabinet to be timely, including on the basis of previous observations.

### **Service quality and reliability**

### Electricity service continuity

Improvements continued to be made in service continuity in 2004: as a result of the regulatory system (envisaging incentives and penalties) introduced by the Authority with effect from 2000, outages without notice (lasting for more than three minutes and excluding those caused by *force majeure*) continued to see a reduction in terms of both number and duration.

In 2004, and as a national average, the overall duration of outages per customer fell to 91 minutes per year, an improvement of 12.5% on the 104 minutes registered in 2003 and of 51% on the 187 minutes in 2000. The improvement also applies to the number of outages per customer per year, which fell to 2.5 in 2004 (taking all outages into consideration), an improvement of 7.4% on the figure for 2003 and 31% on 2000.

Also to be noted with respect to targets is the marked reduction in the gap between the regions of Northern Italy and those of the Centre-South. In 2000, 244 minutes per year were lost for customers in the south of the country, 257% more than the 95 minutes per customer in Northern Italy. In 2004 the number of minutes lost by southern Italian customers fell to 91 (an improvement of 63% on 2000), with the figure for northern Italy falling to 64 (an improvement of 33%). Essentially, the North-South gap has narrowed by 82% in just 5 years of regulation. The progressive and constant reduction of these regional divides in service continuity is also confirmed when adjustments are made to account for geographical concentration.

### Other types of interruption in the electricity service

Regulation for service continuity excludes, as is the case for many other countries, interruptions caused by *force majeure* (for example black-outs or planned disconnections as part of emergency plans, linked for example to exceptional weather events). In 2004 significant outages coincided with exceptional meteorological events; in such cases, distribution – and sometimes transmission – plants suffered damage caused by stresses exceeding the limits envisaged in their design. The Authority therefore decided to address the question of extended interruptions, and has already presented its recommendations in a consultation document: the intention is to protect customers by introducing automatic compensation mechanisms and to encourage operators to provide the best service possible, even in the case of exceptional events. The Authority has also notified the competent bodies of the need to speed up the process of fully implementing the new European technical regulations on the design criteria for above-ground power lines, which are more vulnerable to exceptional meteorological events.

The problem of micro-outages has also been addressed, by launching a local survey campaign to identify solutions based on detailed case studies.

### Investigation into the September 2003 black-out

After the completion of the fact-finding investigation, whose findings were published in June 2004, into the highly-publicised black-out that was triggered in Switzerland and spread throughout Italy on 28 September 2003, the resulting complex formal inquests by the Authority into the spread of the service failure in Italy and the subsequent resumption of service are now being taken forward. These individual inquests, which involve 45 electricity sector operators, have now reached the stage of ascertaining responsibility and challenging an initial group of 9 companies with failure to comply with certain obligatory technical requirements. These operators are now being provided

with the opportunity to respond to questions before the Authority reaches its final decisions, including with regard to any penalties, by 31 July. In the meantime individual investigations are proceeding for the other companies to decide on whether other such challenges should be made.

Alongside the above-mentioned investigations into the conduct of Italian operators, in 2004 the Authority also instigated an initiative to involve the Swiss operators, and notified the Governments concerned and the European Commission of anomalies found with respect to the initial stages of the black-out.

Naturally, the results of the investigations have been and will be used also to develop directives of a prescriptive nature, with the aim of achieving constant improvement in the instruments and defence and reaction capacities of the Italian electricity system.

### Commercial quality of electricity and gas services

For the electricity sector, since 1 July 2004 the national standards concerning the maximum timescale for hook-ups, quotations, technical inspections, responses to complaints, etc have been up-dated and improved. The maximum periods envisaged for repairs to meters and for the reimbursement of sums wrongly invoiced have also been reduced.

For the gas sector, as was done previously for the electricity sector, the regulation of commercial quality has been up-dated and improved by issuing a Service Quality Code for the regulatory period 2005-2008.

### Rational use of energy

In 2004 the Authority completed the regulatory framework for the entry into play of the mechanism for negotiable energy efficiency certificates (known as white certificates), which was given new impetus through the ministerial decrees of 20 July 2004. The new regulatory procedures, which are innovative in international terms, are designed to ensure that quantitative energy saving objectives are achieved while maintaining the same services ultimately provided to citizens and firms. They also aim for the greatest possible cost-effectiveness in meeting these objectives: the new market mechanism selects the measures with the best cost/energy saving ratios. The new measures have met with an immediate and positive response: more than 100 projects have been implemented by distribution companies or companies specialising in energy services; in the latter case the number registering with the Authority now exceeds 250.

### **Controls, inspections and disputes**

With the fine-tuning and progress of the regulatory framework, the need to monitor and ensure that regulatory procedures are correctly applied is also growing in importance with a view to safeguarding customers and tax-payers, providing operators with an environment of fair competition and identifying needs and requirements as they emerge in the regulated sectors. The growing focus on safety, especially in the gas sector, in the form of monitoring operators' compliance with the standards currently in force, is also worthy of note.

To support this strategy for the development of its supervisory, control and monitoring activities, the Authority has set up a Department specifically dedicated to these duties and is reinforcing its traditional and effective collaborative relationship with the

Guardia di Finanza (Tax Police) Market Protection Unit. To the Guardia di Finanza go our most sincere thanks for the much appreciated commitment and utmost professionalism they have dedicated to us.

On the matter of disputes, in its first eight years (1997-2004) of operation and taking into consideration decisions currently *sub iudice*, only a small proportion of rulings, just over 1%, have been totally or partially quashed; if only those rulings that have been challenged are considered, the rate is 12% at most.

In this context, I would like to express my warmest thanks to the Government Lawyers for the considerable support they have provided.

On the subject of disputes, and naturally without prejudice to the fundamental right of each and every one of us to take any appropriate action to protect our legitimate interests, it seems opportune to draw your attention to the need to avoid a situation developing where excessive numbers of appeals are lodged almost automatically and for purely dilatory ends. This is not good for the system and introduces elements of instability and delay to a regulatory and legislative framework that should on the other hand be becoming increasingly stable, reliable and timely.

To this end it might be useful to reconsider the arrangements for the judicial evaluation of decisions taken by technical bodies such as the Authorities. We are certainly not calling here for a separate judicial system, but rather for specialised arrangements: that is to say, judges, but also the Government Lawyers and perhaps also a division of the Council of State, dedicated to energy-related issues. After all, the numerous bills put forward to equip the legal system with specific instruments for actors who are new with respect to our existing legal framework and most certainly have highly specific characteristics, as is the case with the independent Authorities, indicate a widespread interest in the question.

### **Organisational Developments**

At the end of last year the Authority adopted a new organisational structure to reinforce and increase the efficiency and effectiveness of its operations and internal management systems, as well as its dialogue with all its stakeholders. An arbitration function has also been established, as envisaged by the Authority's founding law, while our activity at the international level and in the EU Council of Regulators has also been intensified with a view to achieving greater harmonisation of national and regional regulatory frameworks and promoting, in the countries of South-East Europe and the Mediterranean Basin, regulatory frameworks that facilitate bilateral or multilateral relations for our country's Institutions and operators.

In fulfilling our operational commitments and achieving these organisational developments the Authority has always been able to count on the strong and highly professional commitment of all our staff, to whom I would like to address, in the name too of my colleague Fanelli, my warmest thanks. We would also like to express our appreciation of the cooperation of the Board of Auditors, the experts, the Cassa Conguaglio per il Settore Elettrico (Electricity Equalization Fund) and the National Consumers' Council.

The indispensable duties and responsibilities with which the Authority is tasked, which have only recently been further extended by law, require the consistent employment of

adequate resources. In this respect, and considering that the Authority's funding is in no way a burden on the national budget, we renew our request that the restrictions imposed by the Financial Law for 2005 be removed in the case of the Authority.

### **Outlook for future action**

The transitional phase that the liberalisation processes of the energy systems and markets of the EU, and our country in particular, are still going through, and their need for support in this process, also require the utmost commitment by the Authority in its activities of regulation, supervision, control, observation and recommendation.

For this reason, this significant commitment, operating "in full autonomy and independence of judgement and evaluation", along with an enhancement of its role in making recommendations to Parliament and its collaboration with the Cabinet and the other Authorities and Institutions, will continue to be the cornerstone of our future activities. Activities whose lines of action were made public through Resolution no. 1 of this year and which will be up-dated on a yearly basis; activities whose aim is to protect consumers and achieve ever more advanced levels of market efficiency, not least with a view to strengthening the competitiveness of Italian companies.

This framework also includes continuity in our actions to ensure that the regulatory framework is made increasingly clear and reliable and to further develop the traditional information processes on the rulings adopted and consultation on those still to be defined, with the increasing and closer involvement of consumers and operators, their associations, and all stakeholders in the sector. Indeed, the Annual Report itself, which we are presenting today, will be subject to a public hearing already convened for next week.

With these same goals in mind, we are already testing an innovative Regulatory Impact Analysis which should soon be up and running; this will cover the most significant provisions, with in-depth studies in which all those involved take part to evaluate the various possible regulatory options and the direct and indirect effects of the Authority's resolutions.

To conclude, after this description of the outlook for our activities and for our collaborative work with the other institutions over the coming months, we wish to confirm our active and convinced participation in our shared commitment to the development of our country: a development that must however also be based, as you, Mr President, have often reminded us in the most authoritative terms, on a recovery of competitiveness by the national energy system while following a course of sustainable development that ensures constant advances in the quality of life.

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*The above translation is provided for informational purposes. In case of conflict between the original text and translation, the original text prevails*