



The Italian Regulatory Authority for Electricity and Gas

# ANNUAL REPORT ON THE STATE OF SERVICES AND REGULATORY ACTIVITIES

*Presentation by the President  
Alessandro Ortis*

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The Italian Regulatory Authority for Electricity & Gas

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**Your Excellencies, Ladies and Gentlemen,**

one year ago, when I presented our *Annual Report on the State of Services and Regulatory Activities*, we were all being hit hard by a *tsunami*-like rise of oil prices. Today, this ceremony takes place while Parliaments and Governments are working in order to find a solution to the current, difficult international crisis, whose origin is partly attributable to such *tsunami*.

The crisis confirmed that energy costs bear an impact on the disposable income of households and the opportunity for companies to compete in a global context. On the other hand, a number of essential, strategic challenges lie ahead, related to the security of energy systems and their impact on the environment and climate, with global issues requiring global solutions.

Given such global interaction of problems, the excessive volatility of oil prices - which are still determined without suitable market rules and in opaque platforms open to aggressive financial speculation - still heavily affects energy systems, especially those that are too dependent on hydrocarbons such as the European and Italian systems in particular.

Such dependence implies significant surges of the end-consumer prices of electricity and gas, although these are alleviated by the mechanisms specifically provided for the protection of the weakest consumers. As a result, after an initial increase in 2008, energy bills have been more recently reduced - and we now have the pleasure to confirm that this downward trend will last until the end of September 2009.

However the need remains to be watchful and concerned in relation to the price of oil and its derivatives, which seem to confirm the overwhelming role of speculation. Speculative practices, which shift from *real to paper barrels* and extend to other

*commodities* and sectors, require *governance* agreements and international rules quashing such practices in favour of greater market transparency, efficiency and reliability, and fostering real energy markets to be better and better regulated and monitored. Only in these markets will the opportunities and advantages of deregulation and competition emerge, the fruits of research, production, infrastructural development, marketing and respect for consumers be better reaped and consumers be given a real power of choice, which in turn will encourage companies to compete and win over their confidence rather than attempt to retain privileged positions.

In the world of sports, for stadium-goers who pay a ticket, to enjoy a big match the following ingredients are needed: a nice stadium; good rules; several champions; scrupulous and impartial referees. Likewise, for the national energy system, much needs to be improved, especially for the gas sector which considerably affects the *energy expenditure* of households and companies alike: the stadium (read: the market) needs to be completed with liberalisation measures and infrastructures; as for rules, further measures are needed to enhance competition; champions need to be more numerous, competitive and not subject to privileges for the happy few in the form of preferential racing tracks or equipment; for referees, it seems fair enough to demand the impartiality and disputability of their decisions, thereby protecting and enhancing their independence and autonomy.

In the words of the Italian economist and politician Luigi Einaudi, competition generates progress. He made the following comparison between the market and a local public fair: *"all those that go to a fair are aware that it would not take place without an additional plus on top of the merchant stalls and purchaser crowds; this added plus, Einaudi argued, was a necessary institutional system of framework rules combined with a monitoring and control activity; rules, he contended, have to be commensurate with the size of the relevant markets or systems, including con-*

tinental and global ones.

This equally pertains to the contribution, responsibility and cooperation (particularly at the EU level) of independent sectoral Authorities and, as far as we are concerned, the commitment to provide Parliament and Government with comments and proposals on the energy sector, based on the tasks entrusted to our institution. We are therefore trying to do our part, in the conviction that the energy sector can develop from a major determinant of the current negative economic cycle to an effective driver leading us out of the crisis and, ultimately, towards economic and social recovery equally in terms of sustainable development.

In our activity, we have given priority to measures aimed at providing consumers with greater awareness, freedom of choice and economic benefits; that is considering on the one hand their immediate expectations and on the other that these are met by the actions of efficient and reliable operators capable of growing in competitive national and international markets.

After all, the competitiveness of a system and of its champions is best rooted and nourished in liberalised and well-regulated environments, rather than in unjustifiable monopolies that are harmful to consumers.

## **REGULATORY AND REPORTING ACTIVITIES**

### **Tariffs, Markets and Prices**

The national energy system continues to be marked by its high dependency on imports (85%) and hydrocarbons (more than 70% being oil and gas); similarly, electricity production is mainly based on natural gas (54%). Energy supplies thus continue to be heavily dependent on oil, far from average European levels of dependence and from other countries with which Italian companies have to compete; the gas and electricity bills of Italian consumers continue to be strongly exposed to

oil price fluctuations.

Given the unfavourable situation, which Parliament and the Government are addressing - also through a '*development and energy*' law adopted last week - we have endeavoured to contribute to mitigate and dilute the effects of high oil price fluctuations through measures favouring competition and supporting investments and mechanisms leading to tariff and price reductions, despite the oil price recovery.

Within the general framework outlined above, it is useful to review the main components contributing to the *energy bills* paid by consumers: i) *tariffs* fixed by the Authority for services provided by technical monopolies (transport, distribution, metering as well as re-gasification and storage, in the case of gas); ii) *energy*, with wholesale and retail market *prices* competitively determined in the context of liberalised production, marketing and sales, which depends on fuel supplies and technologies and on market efficiency; iii) *system charges*, *other costs* and *taxes* provided for by laws.

### *Tariffs for Network Services*

Even in the current international context marked by instability and economic and financial risk, the crucial role of stable and independent regulation is affirming itself on a world wide scale, not just in Italy, in fostering investments in network infrastructures (including smart grids) and in the promotion of efficient costs of related services.

More specifically, the transparency and predictability of tariff systems applied by independent Authorities to remunerate regulated activities have been instrumental in lowering the risk for investors and shareholders alike; as a result, the share prices of network operators have not slumped, loans have invariably been granted, and in-

vestments have continued.

The tariff systems governed by independent Authorities are therefore proving to be an indispensable anti-cyclical instrument favouring investments and, consequently, contributing to overcome the crisis and re-launch the economy.

In particular, as regards our energy infrastructures, a regulatory system based on incentives has been adopted for a long time, based on the conviction that safer and more efficient network services are of primary interest for both households and companies.

Funds from the tariffs that are felt directly by consumers in favour of such developments are available and adequate; however three problems hinder investments.

Problem number one is authorisations. In the electricity sector, for instance, the Authority has already applied a system of incentives with 9.9% return (over 12 years) for new investments intended - among other things - to reduce the costly congestions on transmission networks. The result is that the strong network expansion programmes of the transmission operator Terna, are frequently slowed down by excessively lengthy and uncertain permitting procedures. Further delays at a time when opportunities for other industrial investments are being stifled by the ongoing crisis, would cause even heavier damage in the form of impaired crucial investment and employment opportunities. The Government is rightly intervening to solve this issue with *network-facilitating measures* contemplated in decree-law no. 78/09 of July 1.

Problem number two is the uncertainty in the legislation governing concessions in the hydropower and natural gas distribution.

The situation is particularly serious for these latter concessions, given *inter alia* the excessive fragmentation of the sector comprising nearly 300 distributors, many of which are very small or in any case not justified by special territorial conditions. The

situation is aggravated by the existence of as many as 6400 municipal concessions, which prevents economies of scale and hampers competition, given also the difficulties experienced by suppliers in interacting with such a large number of players.

A choice in favour of efficiency seems therefore necessary based on: termination of in-house provision of services, as recommended also by the Antitrust Authority; significant increase in the size of service areas; compensations encouraging distribution operators to invest up to the last day of their concession; and bidding criteria privileging quality of service and investments rather than overly generous concession fees. Parliament has intervened also on this issue with the "*development and energy*" law which should lead to positive developments.

The third problem is the persistence of vertically integrated companies with dominant market positions, especially in the gas sector. Ever since 2005, the Authority has granted extra returns (for periods of up to 15-16 years) for all investments aiming at increasing gas supplies and diversifying supply sources. New investments in transport, storage and re-gasification are granted average pre-tax returns in the order of 10% or greater in real terms (9.7% for transport, 10.6% for re-gasification and 11.1% for storage). These returns are guaranteed and provide real advantages so that there can be no justification for accumulated delays in infrastructure development (as in the case of gas storage) or for generous (ordinary or exceptional) dividend policies - which are sometimes financed by increased indebtedness. In fact, generally speaking, the interests of shareholders - legitimate as they may be - do not coincide exactly with those of consumers.

The only plausible explanation for the delays and the shortfalls in capacity is the quite rational interest of the incumbent in limiting access to new players in the internal market; economically speaking such an interest can well prevail over any reasonable tariff return for infrastructures and services that are natu-



rally monopolies and whose enhancement is capable of facilitating competitors. It therefore remains urgent to apply the 2003 law and its subsequent amendments, requiring ownership unbundling of Snam Rete Gas in order to provide an effective solution to the conflict of interest that no *Chinese Wall* erected by 'invasive' regulations is able to eliminate, as already undertaken in the electricity sector. In effect, the experience of transferring Terna under the control of *Cassa depositi e prestiti* (Loan and Deposit Fund), which strengthened rather than weakened the international prominence of Enel, and the recent acquisition of significant sections of distribution networks by institutional and other Italian investors, not engaged either upstream or downstream of the networks, demonstrate that strategic energy infrastructures can be transferred to *third-parties* (external to the market) without any risk of losing their control at national level in favour of foreign incumbents.

### *Wholesale Markets*

In the electricity sector, the implementing guidelines for wholesale market reform and rationalisation based on law 2/09, were defined by the Ministry for Economic Development on the basis a constructive method of participation. The Authority supported such reform measures by contributing, among other things, to the definition of the rules for dispatching *indispensable plants* for the security of the power system with the primary objective of containing their costs and limiting unjustified rents coming from lack of competition in some areas of the country.

In 2008, the Authority further adopted a *consolidated text* reforming and rationalising the monitoring of wholesale electricity markets and dispatching.

In the gas sector, as provided for by law 2/09, we proposed a number of possible pro-competition measures which also considered other market opening experiences, which underscored the possible need for powerful and decisive measures

to overcome obsolete forms of organisation.

Among these are gas release and (as reported in a recent *Investigation* jointly conducted with the Antitrust Authority) divestment of gas-storage facilities by the dominant operator ENI. These proposals, which are also aimed at promoting investments to increase security of supply, were partially accepted in the aforementioned decree-law. Regarding gas release, it is hoped that the new law will envisage a significant increase in the volume released and extension of the period in order to favour medium to small consumers and suitably promote competition. As for storage, while we appreciate that ENI seems to be voluntarily preparing itself for divestments (whose adequacy will need to be assessed), it is important to underscore that regulatory measures alone are not sufficient to overcome obstacles arising out of an ownership structure in which a single entity controls the vast majority of existing storage units as well as of gas fields that can be converted to storage.

These measures need to be accompanied by the commissioning of new LNG plants and gas import pipelines leading to greater diversification of suppliers and supply areas; a number of Italian projects were included among those eligible for EU financing, but others are progressing according to a different logic and strategy, and consequently thwarting Italy's future role as gas hub for Europe; potentially also a hub for electricity with interconnections in the Mediterranean basin for additional production capacity, especially from renewable sources.

In order to contribute to such goals and create a real regulated wholesale gas market (an exchange), the Authority has long ago launched a procedure aiming at the definition of a balancing system based on market criteria and at solving the criticalities observed in the measurement and assignment of withdrawals. Such a need was confirmed in the recent decree-law no. 78/09, and certainly the Authority will fulfil the tasks entrusted to it by legislation in a timely way. However, a criti-

cal issue remains which cannot be overcome by regulatory instruments alone - namely the absence of an independent dispatcher, that is a *third-party* (such as Terna in electricity) which can ensure the impartial implementation of market outcomes and provide the necessary services without even a minimum suspicion of discriminatory practices.

Finally, we wish to underline our concern for the failure to extend the antitrust ceilings in the gas sector by law; hopefully, the foreseen application of normative measures will provide solutions that prevent the current practice of dodging the ceilings and that different operators - already present in large numbers in the market but still dependent on ENI's gas imports - will be enabled to act as effective competitors.

### *Retail Markets*

In the current phase, while efforts are being made to complete the transition of the freedom of choice of consumers from theoretical to real (only in a market with plenty of supply and competing suppliers can it be considered real), two contractual opportunities are available to safeguard consumers: the offers of suppliers on the free market and the regulated offers that have to be made by them based on the reference conditions defined by the Authority for the protected market (small customers that still have to decide whether or not to switch to free market).

In the electricity sector, the number of households and small-sized companies that choose offers on the free market continues to increase.

In only two years of liberalisation, more than 3 million 200 thousand consumers decided to change supplier, that is over 2 million households (7.1% of total) and more than one million 200 thousand small-sized companies (15.6% of total). The national average *switching* rate has therefore reached 8.9%, which is in line

with best experience in other European countries.

In the gas sector, the results are less encouraging.

After seven years of complete opening of the market on the demand side, less than 7% of consumers changed supplier, down to just a little over 4% for households. In 2008, the percentage of consumers switching to free the market has been modest (1.2%).

Even so, we are nevertheless continuing in our endeavour to ensure increasingly equal opportunities for all competing suppliers, in terms of availability of information, ease of *switching*, accessibility to networks and related costs.

As contribution to providing an increasingly real possibility of consumer choice, in addition to the *toll-free number* at the Single Buyer (which I thank for its fruitful collaboration), the Authority has already made available on its website a "*trova-offerte*" (*offer finder*), a user-friendly search engine for finding and comparing the various commercial offers available in the electricity market, as well as the *consumers' window* ("*finestra del consumatore*"), a useful guide for consumers providing information on opportunities, services and rights originating from liberalisation.

To further improve transparency in the interest of consumer protection, the Authority has continued to exert its powers in the field of metering devices. In the electricity sector, the diffusion of electronic meters is close to completion, unprecedented worldwide. Starting from 2010, the diffusion of these new devices, will allow gradual large scale extension of the two-tier tariff to domestic customers, ensuring better cost allocation and, more importantly, encouraging more virtuous and efficient behaviour for the benefit of all consumers and the equity of the system as a whole.

In the field of gas metering, the Authority has strengthened its regulatory activities

with reference to: the immediate replacement of faulty meters, free of charge; the identification of consumption profiles; and gradual modernisation of the stock of meters with innovative electronic equipment. The latter programme is also a world *premiere*.

### *Charges, System Contributions and Taxes*

We have made an effort to keep under control the *general system charges*, which are incorporated in the electricity bill, for example by introducing a new mechanism motivating the reduction of nuclear decommissioning times and costs, which Sogin has satisfactorily implemented. The Authority further intervened on the CIP6 charge (introduced in the early 1990s to finance electricity generation from renewable resources but also favouring efficient CHP generation from fossil fuels) reducing it by nearly 600 million Euro per year.

On the other hand, strong increases are expected for *general charges* in support of renewable resources, which are certainly essential to foster truly sustainable development; based on the current mechanisms these are estimated to double from the present 1.6 billion Euro by 2010 and grow to an estimated 7 billion Euro by 2020, changing in scope from largely CIP6 fossil generation to predominantly renewable generation. We have already pointed to the need to review the sustainability of such large charges as well as the incentive mechanisms over time, taking account of the specific characteristics of each energy resource in terms of efficiency, costs, technological maturity and the expected impacts on national industries; in parallel, the Authority is nevertheless working to facilitate network access and reduce the costs of network services thus contributing to the successful accomplishment of renewable energy promotion.

The mechanism currently in place for extracting *system charges* takes the form of an administrative levy (further burdened by VAT applied in the bill),

presents problems of distributional equity. In particular, electricity consumption is not proportional to personal income or to company profit. For instance, a low-income family with high consumption (a large family) pays higher *system charges* than a well-off single; likewise, a business with high power consumption but modest profits pays higher contributions than a high-profit business with low consumption. We therefore deem it appropriate to think over ways and means of transferring such costs, either in full or in part, to the more equitable general taxation system.

Other charges or contributions included in the *electricity bill* are those in support of *research* and *energy savings* as well as *solidarity surcharges* for disadvantaged consumers.

Consumers contribute around 60 million Euro/year in support of *research*.

The availability of these resources allowed us to grant 107 million Euro to research institutes in 2008. Moreover, in accordance with the three-year plan 2009-2011, we expect to issue calls for tenders for a further 264 million Euro.

As regards *energy savings* and *rational use of energy*, the mechanism of *white certificates* is providing benefits that are well above the costs.

Starting from 2005, the first year of application, thanks also to the valuable collaboration with ENEA (the National Agency for New Technologies, Energy and the Environment), our Authority assessed nearly 4,800 applications and certified savings worth more than 3.6 million toe, a result which is above the statutorily required level and is equal to the annual domestic consumption of a city of 4.8 million inhabitants. Such good performance will however need to be increasingly supported by a growing commitment commensurate with increasingly demanding future targets.

On the matter of solidarity contributions between consumers, in accordance with statutory provisions introducing forms of support for large or economically disadvantaged families and for patients using a life-support equipment, the Authority is

currently applying the *electricity bonus* mechanism and has also put in place the *gas bonus mechanism*, which grants benefits retroactively from the beginning of this year. With reference to the *electricity bonus* mechanism, thanks to the collaboration and commitment of the Italian Municipalities Association ANCI and its member Municipalities, the backing of central Government and the media, more than one million applications have already been filed; non-eligible applications are less than 2%; applications that are currently being assessed are nearly 380,000; those already judged eligible to receive the bonus on their bill are more than 600,000 and are of course expected to increase.

Beneficiaries who have filed an application within June 30th last will also be eligible for a retroactive reduction from the beginning of 2008. The current mechanism entitles beneficiaries to an average reduction of about 20% on their electricity bills, to be financed by all other consumers (including companies) through a very small solidarity contribution.

While focussing on *solidarity* and disadvantaged customers, it also seems appropriate to recall the suspension and reduction of energy bills provided for by a recent *ordinance* of the Italian Prime minister in favour of the earthquake-stricken residents of Abruzzo. As we dedicate our full commitment and collaboration to the implementation of the ordinance, I hereby would like to express, in the name of the Authority, our full and sincere solidarity in favour of the unfortunate population of that region.

### *Prices*

National prices are indisputably higher than the European average, although the gap has been gradually narrowing, especially in the electricity sector, partly due to a higher competition.

In 2008, wholesale prices of energy in the main European power exchanges

increased by 60% to 110% compared to the same period of the previous year, with the exception of the Italian exchange which experienced a more moderate dynamic (+28%). Throughout 2009, prices in all major European exchanges decreased drastically following the slump in crude oil price and reduction in demand. Italian price differentials compared to the French and German markets, which were in excess of 30 Euro/MWh during the early months of the year, came down to nearly 20 Euro/MWh.

Beginning with November 2008, trading on forward markets started also in Italy allowing greater flexibility in the management of energy portfolios.

Despite the small volumes traded, the introduction of this form of trading in Italy is an important innovation. In the first half of 2009, the spread on the annual contract expiring in 2010 between IDEX (Italian Derivatives Energy Exchange) and the French and German Exchanges fluctuated around 14 to 16 Euro/MWh. Even lower values were recorded on OTC markets, thereby raising expectations of a more competitive Italian wholesale market.

Further significant improvements could be achieved through the market reforms recalled in the above, specifically regarding of the derivatives markets, initiated by law 2/09.

Prices in European hubs did not closely follow oil price trends during most of 2008 - partially as a consequence of international tensions. The price behaviour at the Italian Virtual Trading Point (PSV) was more or less in line with those of other European hubs but exhibited much higher values owing to a lower degree of competition.

In the retail market, based on the data published by Eurostat for 2008, it can be estimated that 60% of Italian households with annual consumptions below 2.500 kWh pay lower electricity prices than the European average. As in the past, households with higher consumption show unfavourable deviations even greater



than 45%. In the same period, Italian companies have paid energy prices above the European average for all consumption classes, with deviations in excess of 25%.

Italian gas prices for the lowest class of consumption (cooking and hot water) were lower than European averages; while for the higher classes (use of gas for heating and other uses), the price was in line with the European average, net of taxes, and higher than the average, gross of taxes (15% greater). Italian companies (excluding non-energy users and electricity generation companies) paid prices around the European average. However, a comparison with countries where liberalisation is more advanced shows that Italian prices, net of taxes, were higher by more than 20%.

As already mentioned, the Authority has the task of defining the *reference prices for the protected market* and the conditions for *guaranteeing* supplies of *last resort*, which services are assigned through bidding procedures between operators qualified for such purpose.

In the electricity sector, reference prices for the *protected market* are determined based on the actual and forecast costs of the Single Buyer, a publicly owned company in charge of procurement to meet such demand.

In the gas sector, after considerable consultation, the methodology for calculating the *reference prices for protected* customers has been changed giving particular attention to the transfer of correct price signals in order to promote competition and rationalisation of consumption. However, the Authority is aware that these consumer protection measures are hardly sufficient to effectively combat the exercise of the market power in the wholesale market.

The oil price variation of 2008 was not followed by a simultaneous gas and electricity price variation largely owing to the effect of internationally applied indexation mechanisms linking gas to oil prices that are based on the averages of previous periods (including the record peaks of July 2008). Additionally, in the Ital-

ian *protected market*, the Authority has for a long time adopted quarterly updating procedures which mitigate the effects of excessive (upward or downward) volatility of international hydrocarbon prices. During periods of increase, these mechanisms dampen and dilute the increase; since January of 2009, the mechanism results in consecutive reductions lasting at least up to September of this year despite the current price rally. Since the beginning of the year, the price of electricity has come down by 8%; that of gas by 15.4%.

The economic crisis combined with high energy prices have made the above described electricity and gas *bonuses* particularly welcome to less well-off consumers - however, they have at the same time determined a rise in default of payments. In order to counter this problem, the Authority has already started consultations on possible corrective measures.

## **Quality of Services**

In assessing the overall *cost-effectiveness* of supplies, reference should be made not merely to prices, whose levels are still unfavourable in comparison with the European average, but also to the technical and commercial *quality* of services, whose conditions for the Italian consumer are however among the most favourable at the EU level. This is the result of regulatory mechanisms that are proving to be effective, more specifically: establishment of increasingly demanding standards/targets linked to an automatic system of bonuses or penalties for operators and automatic compensations for consumers.

### *Technical Quality*

In 2008, the average duration of power outages attributable to distributors remained stable (50 minutes/year per customer, among the lowest in Europe). The gap between Central and Northern Italy on the one hand and Southern Italy on the other has been reduced. In the South, the duration of outages recorded an all-time

low of 73 minutes/year per customer. Regulatory procedures have also been enhanced: including brief outages (for the first time in Europe), expanding the group of consumers who benefit from compensations; applying compensations also for long lasting blackouts.

As far as the gas sector is concerned, safety conditions have progressively improved as a result of our incentive-based mechanisms and monitoring activity; the rate of network inspection increased to more than 45% of the minimum required level and the national average response time following calls for emergency intervention (calculated on the arrival of support staff on site) is now at a satisfactory level (33 minutes).

### *Commercial Quality*

Over the last ten years, owing to the failure to observe specific regulations introduced by the Authority, consumers received over 650,000 compensations, of which 50,000 in 2008, corresponding to a payment of nearly 3.5 million Euro. Aiming at a general overhaul and strengthening of quality of sales regulation, the Authority has published a Service quality code ("*consolidated text*") which covers, among other thing the speed and quality of response to complaints; the accuracy of invoicing; the quality of suppliers' call centres, for which we have published a preliminary classification based on waiting time, quality of replies and degree of customer satisfaction. Such classification will be updated and published on a half-yearly basis.

After renewing the existing Memorandum of Understanding between the Authority and the National Council of Consumers and Customers with a view to promoting further initiatives for the protection of citizens/consumers, we have launched a *Forum of Consumers* for periodical review meetings and financed 16 training seminars; the latter initiatives involved more than 350 representatives of Consumer

Associations in various Italian cities in order to develop conciliation procedures between Consumer Associations and suppliers. Recently, the Authority has initiated a consultation procedure on new proposals to improve the readability, transparency and simplicity of bills, in any case without penalising the necessary completeness of information. Proposals include a single bill for both electricity and gas so as to respond to the growing diffusion of joint or *dual-fuel* offers.

## **Reports, Consultations and Resolutions**

In line with our ongoing commitment to and keen interest in intensifying our dialogue with the Italian Parliament and Government, we have made available 3 advisory reports and 3 briefings for as many parliamentary hearings.

In 2008 we confirmed our constant commitment in favour of exchange of ideas with other stakeholders by publishing 38 consultation documents; by promoting seminars or subject-specific meetings with operators and consumers; by strengthening the application of *Regulatory Impact Analysis* (RIA) to the more far-reaching decisions.

As confirmation of the importance we attach to transparent dialogue, next week we will be holding our traditional public consultation on the Three-Year Plan; the relevant document was published as first resolution of the year so that every stakeholder would be informed in time of our planned activities and have the possibility of formulating appropriate comments and remarks.

The success of the consultation processes is in any case evident from the value given to them as measured by the keen participation of consumers, operators, companies and their respective Associations; I sincerely thank them for the observations and proposals they never fail to submit.

Last year, 444 resolutions have been approved (vs. 359 in 2007). Of these 206 (vs. 179 in 2007) were rulings of regulatory nature and 115 (vs. 66 in 2007) rulings

in the sphere of monitoring and application of penalties. In parallel, in the interest of clarity and transparency, we are proceeding in our effort to simplify the regulatory framework and process by identifying 500 resolutions that are no longer in force. In addition *Consolidated Texts* have been published on the most salient regulatory interventions implemented in the past.

## **Disputes**

The rulings of Administrative Judges on our rulings are extremely significant for the effective fulfilment of our institutional functions and further provide useful guidance for future choices. That is why we are following closely legal review, in the awareness that it can be a useful instrument to improve our capacity of intervention.

No doubt, the review of our rulings, if carried out within times that are compatible with the needs of the market and in ways that are reasonable and rational, can contribute significantly to the certainty of the regulatory framework.

An analysis of rulings confirms the high degree of solidity of the Authority's actions to jurisdictional review, with 98.4% of our resolutions being recognised as legally valid. Among the pronouncements of Administrative Judges, it suffices to make reference to a recent ruling which states that the independence of the Regulator is an essential factor in the governance of energy markets.

I hereby thank State Lawyers for their precious assistance in every stage of dispute resolution.

## **MONITORING AND CONTROL**

The correct enforcement of regulations is particularly important for protecting the interests of households, companies and investors; therefore, increasing importance has been attached to monitoring and control activities and to the infliction of

penalties for non-compliance.

## **Controls and Inspections**

In the reference period, 113 inspections were performed on: quality of service, safety, network access, tariffs, tariff integration, production incentives, etc.

The controls were also extended to new forms of investigation such as: compliance of gas distributors with emergency response obligations; effective qualification of retail electricity supply companies listed in the *Suppliers List* of the free electricity market; compliance with the Suppliers' *Code of Conduct*, and conformity of energy saving projects.

A total of 111 inspections on CIP6 plants have been carried out since 2005 for an overall capacity of 8,850 MW. As a result of these, more than 156 million Euro will be reclaimed in the form of incentives received without entitlement; of this amount, 73 million Euro has already been paid, thus contributing to reduce the largest of the general system charges (the A3 component) in the electricity bill. Another activity worthy of note is the monitoring task entrusted to the Authority on the so called *Robin Tax* on energy companies, which consists of a regular review of the behaviour of operators in response to price changes and has recently received legal confirmation. At the end of the first cycle of analysis of accounting documents filed by operators, the Authority will inform the Government and the Parliament on possible irregularities.

In our steady commitment to our monitoring and control functions, and in our preparation of related plans and instruments, we have relied on the intense, growing and professional cooperation of the Special Units of the Italian Tax Police (*Guardia di Finanza*), whom we sincerely thank. Key appreciable contributions were also received from University Institutes, the Fuel Experimental Station and

the Electric Sector Compensation Fund (CCSE) (*Cassa Conguaglio per il Settore Elettrico*), which is also active for the management of funds related to *tariff equalization* and the *system charges* mentioned above.

## **Investigations and Penalties**

Investigations to ensure compliance with regulatory provisions has increasingly intensified. Enquiries have increased to 194 from 168 in 2007; penalties inflicted have increased from 56 to 64, for a total of 9.5 million Euro which will be used for initiatives and projects in favour of consumers.

In order to ensure the maximum degree of transparency in, *inter alia*, its decisions for the infliction of penalties, the Authority has introduced *guidelines* on the quantification of penalties; such guidelines are intended to provide more clarity in the exercise of discretionary powers in a clear, non-discriminatory framework intended for the fulfilment of the objectives provided for by the law.

In compliance with the current administrative practice and with case law, a cap has been introduced equal to 10% of turnover; moreover, to favour the collaboration of companies in autonomously amending their conduct, specific rules have been introduced to enable assessing the value of initiatives designed to improve market conditions.

Penalties were inflicted, first and foremost, for breaches related to safety of gas supplies and continuity of gas and electricity supplies. Other investigations carried out by the Authority focused on infringements related to the commercial protection of consumers and were extended to include compliance with: tariff regulations; network access obligations; purchase of green certificates in support of renewable sources; and communication of data required from companies. Further, the Authority continued its investigations started last year on the numerous infringements of gas metering correction coefficients, which emerged following our fact-finding survey in 2007 and the investigations of public prosecutors.

## **ORGANISATION AND OPERATIONS**

Institutional activities have intensely involved our workforce, whose numbers have remained unchanged over the past few years, despite the new duties and functions assigned to us over time. Indeed, such new functions and the need to develop further services in favour of consumers, consolidate our monitoring and control functions, and support the European and international commitments referred to below, all require an increase in personnel. This can be achieved without burdening the State budget since the Authority funds its operations exclusively through a system of self financing based on contributions from energy sector operators. Over the last few years, thanks to continuous improvements in internal efficiency, it has been possible to limit such contributions to just 0.3 per thousand of operators' revenues, well below the one per thousand contribution envisaged by the law. This self-financing system lies at the foundation of our financial and economic management, which undergoes accurate control by our Board of Auditors, to whom I owe a grateful acknowledgement. As regards the qualitative development of our human resources, we have continued to invest significantly in training and updating activities, reaching 70% of the staff in 2008. I hereby take the opportunity to extend my warmest thanks to all of our Personnel and collaborators for work, devotion and professionalism, on my personal behalf and on behalf of my colleague Mr. Fanelli, who also deserves our utmost gratitude for his unwavering commitment and experienced collaboration.

This intense commitment was favoured also by the Guarantor of our Code of Conduct and supported by our valuable dialogue with the Union representatives and increasing collaboration with CNEL (National Council for the Economy and Labour) and colleagues from other Authorities, whom I sincerely thank.

While dwelling on operations, it seems appropriate to recall activities developed at European and international level.



Energy exchanges, cross-border flows and interconnections, binding European legislation oblige us and provide us with the opportunity to develop suitable international cooperation and exchanges between Regulators and Institutions of the EU. As a result, we have increased our commitment within the CEER/Ergeg (Council of European Energy Regulators), also in view of the imminent launch of the new European Agency of National Regulators which envisages harmonisation towards increased levels of responsibility and independence similar to those fixed by the law instituting the Authority.

Among other initiatives, we are participating in the *Board of Regulators* for the Balkan area (established by the Athens Treaty); we are managing *Twinning* projects promoted by the European Commission with our Colleagues from Ukraine and Albania, as well as a Central and South Eastern Europe *Regional Initiative* facilitating integration in gas and electricity markets of the area and towards a single continental market; we are supporting *MEDREG* (the Mediterranean Working Group on Electricity and Natural Gas Regulation based in Rome) and the *Florence School of Regulation*, which draws together personnel from Regulators and operators of many countries of interest for Italy (for training, research and exchange of experience).

As a whole, such international relations are dedicated to the regulatory cooperation within the EU or for cross-border interconnections and energy exchanges of major national interest. Our commitment has in fact focused on themes and areas of key interest for Italy (the EU, Eastern Europe and the Mediterranean Basin) so as to contribute to building increasingly transparent, integrated and stable markets with regulatory frameworks operating in harmony with Italian and EU legislation; all of which also facilitates the necessary investments and role of Italian companies.

## **OUTLOOK FOR FUTURE ACTION**

Looking at the international economic crisis and at the strategies enacted towards its solution bearing on the energy sectors, the continuity of regulatory contributions promoting investments and increasingly secure and cost-effective resources and energy services, becomes increasingly important. This future commitment is favoured by the international convergence we have contributed to create. More specifically, upon conclusion of the *G8 Energy* meeting held in Rome a few weeks ago, together with the representatives of Regulators from all continents, we have drafted a document which envisages larger forms of collaboration designed to make regulatory frameworks increasingly solid, transparent and globally harmonised; this ultimately translates into a more effective, gradual improvement of energy systems security, cost-effectiveness and sustainability.

For these very purposes and with regard to oil products, on which energy/gas bills and national security are still highly dependent, we have welcomed with considerable interest the invitation received from the Italian Ministry of Economic Development to jointly investigate a proposal for an initiative that needs to be promptly embarked upon at the EU level; it aims at not passively accepting the high oil price volatility and related speculation but rather at suppressing them with the single, loud voice of 500 million European consumers; such proposal for an early, pragmatic and timely European initiative is just a first step pending the conclusion of future, more complex global agreements.

The proposal - to be further investigated and improved - will involve experts in the sector and consists in the establishment of a regulated *European Oil Exchange* open to selected operators who will trade in standardised long and very long term products, to be physically delivered in Europe and guaranteed by a reliable European central counterparty. Such a system would provide a degree of certainty for

price containment and reasonable returns on long-term investments, which will ultimately contribute to promoting a more suitable level of spare capacity and dampening price volatility.

As regards our future activity, we will attempt to meet the commitments arising out of decisions recently taken at the EU level on *sustainable development* (energy savings; role of renewable sources; greenhouse gas emissions) and on the internal market of electricity and gas (network unbundling; integration of national markets; establishment of the European Agency of National Regulators and increased cooperation between them).

To cope with the challenges posed by the development and competitiveness of the Italian system, the Authority's special dedication and efforts will remain constant along the lines, objectives and themes already outlined and published in its three-year work programme. In so doing, we intend to ensure the maximum degree of institutional cooperation, commitment to public communication, increasing dialogue with all stakeholders and continuous focus on the two key issues of our institutional mission, promotion of competition and consumer protection.