



## Present Status of electricity Power Regulation in Albania

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### **1. Background**

Since 1995, the Albanian Parliament took the first steps toward forming a commercial electricity sector by transforming the Albanian Power Corporation (KESH) - responsible for generating, transmitting and distributing electricity all over Albania, from a state enterprise into a joint stock company. However, the state remained the single shareholder in KESH

In 1995, as a demonstration program designed to show the benefits of privatizing the distribution function of the electricity sector, three pilot distribution companies in Vlore, Elbasan and Shkoder were separated from KESH and 30% of their shares were transferred to private entities and company employees. According to the privatization law, the remaining 70% of the shares of the pilot companies were supposed to be taken by one or more strategic foreign investors with energy sector experience. However, the plan to bring in strategic investors was never implemented. The three pilot companies have performed poorly and the Government has plans to re-merge the companies into KESH

At present, the Ministry of Public Economy and Privatization (MPEP) represents the Government's interest as the owner of KESH and is also Albania's primary energy policy-making institution

Currently KESH is facing a very difficult financial and operational situation due to increasing problems with non-payment and illegal connection. More recently, KESH has faced unusually severe drought conditions that have necessitated cutting electricity service to consumers for 10-12 hours per day.

### **2. Establish of Albanian Electricity Regulation Authority - ERE**

Following the enactment of the Law on Regulation of the Electricity Sector in September 1995, an independent Electricity Regulatory Authority (ERE) was established. According to the Law, ERE is responsible for all regulatory issues in the electricity sector, including licensing procedures, tariff approvals, consumer protection, and the settlement of disputes between participants in the electricity sector.



### **3. *The style of Regulations in power sector.***

The old-style regulation has been the prevailing mode in Albania where state monopolies run the power sector. Typically, it involves extensive control by one or more ministries over the operations and investments of KESH.

Private investors will not participate in a market over which the government maintains undefined, broad and intrusive control. The new, competitive electricity market requires a new form of regulation that is transparent and free from undue political influence. The independent electricity regulator should balance the interests of consumers and investors in accordance with parameters specified in an energy or regulatory law and widely recognized regulatory principles.

### **4. *The " Independence " question ?***

The law gives the ERE strong regulatory authority, but since its creation it has been largely ineffective. Government imposes direct and indirect controls on the actions of state-owned Entities Government controls on prices but "regulation" goes beyond simple price or tariff controls. State-owned power enterprises are commonly required to get government approval for many minor operating and investment decisions.

Under this system, the ministry responsible for energy matters directly controlled the prices and the many day-to-day operating and investment decisions of the state-run electric monopoly. It was not unusual in these cases for the state-run electric monopoly to charge below-cost rates, as has been the case in Albania.

### **5. *Present Action Steps .***

Albanian Government through the assistance of U.S. Agency for International Development - USAID , are preparing a Strategy Action Plan to reform the power sector, comprising the three fundamental objectives as it has developed the Strategic Action Plan :

1. To establish a modern, efficient electricity sector that operates according to sound economic, commercial and market principles.



2. To create conditions that will attract private investment to fund necessary rehabilitation, expansion and improvements to electricity facilities and the participation of strategic investors in the operation of the energy sector.
3. To develop the Albanian electricity market in a manner that is consistent with the European Union's requirements for liberalizing the electricity sector (Directive 96/92/EC) and Albania's commitments under the Thessaloniki agreement regarding the development of a regional electricity market.

These objectives look beyond the immediate electricity crisis and focus on establishing a long-term, sustainable framework for a sound electricity sector. By focusing on these longer term objectives, the USAID believes that Albania will not just overcome the immediate problem of the existing electricity shortages, but will create conditions to ensure that the electricity subsector specifically and the energy sector generally become important assets that boost overall economic growth, rather than liabilities restraining such growth.

**a. Developing a comprehensive energy policy.**

Part of the strategy should include the development of a prioritized list of investment options that considers least cost planning principles and the necessity for fuel diversity in assuring a reliable supply of electric energy. The ERE should review any investment plans developed by KESH and determine whether they are consistent with general government energy policy and least cost planning principles.

**b. Designing tariffs that encourage conservation and liberalizing Electricity Prices.**

Electricity prices should be liberalized over a reasonable period of time so that they can reflect the prudently-incurred actual cost of providing electricity.

The long-time policy of subsidizing electricity prices has proven disastrous. Subsidies have caused major economic distortions by overstimulating electricity demand and discouraging the use of alternative energy sources, particularly in the area of electricity consumption used for space heating. By failing to provide an adequate source of revenues, subsidized prices have



prevented KESH from paying for necessary maintenance of the existing system and from investing in new facilities to serve the growing demand. The lack of adequate revenues has also required the government to partially subsidize the purchase of imported power in crisis conditions. The situation is made worse by the lack of diversity in Albania's generation mix with virtually all generation coming from hydropower facilities. Albania's electricity supply is weather dependent and drought conditions can easily exacerbate any supply shortage. The USAID believes that Albanian household consumers would rather pay a higher but reasonable price for electricity than continue to experience frequent and extended outages.

**c. Reorganizing and unbundling KESH.**

KESH should be unbundled into separate generation, transmission and distribution companies. The reorganization will improve management control, as well as prepare for the development of a commercial market and eventual privatization.

**d. Designing a modern, competitive electricity market.**

Electricity service should be provided by separate companies performing generation, transmission and distribution activities, the Government should set broad policy goals through the ministry responsible for energy matters and the electricity regulator should review tariffs and license market participants.

**e. Developing a regional power market in the Balkans.**

The Government, MPEP and the ERE should continue to participate in the process of building a regional power market that will facilitate the import and export of electricity between countries in the region on an economic and mutually beneficial basis.

**f. Attracting strategic private investment.**

The Government and MPEP, in particular, should review existing laws and prepare legislation that will remove obstacles to attracting strategic private investment in the electricity sector.

**6. Key Issue - Creating a Strong, Independent Electricity Regulatory Authority**



The accomplishment of these objectives will require major changes in the current structure of the Albanian Electricity sector. The centralized, strongly political form of direct government control over the electricity sector that has characterized the sector for decades must be substantially changed. In its place, there must be a strong, independent regulatory authority that operates transparently according to principles embodied by law and the application of well-recognized regulatory principles.

#### 6.1 New status of ERE

The independent electricity regulator will be solely responsible for regulating prices and licensing power market participants.

The independent regulator must balance the rights and obligations of the companies that provide electricity service (and the private investors who may participate in the electricity sector in the future) and the rights and obligations of electricity consumers. The structure of the electricity market must be changed. The existing system in which a single, state-run electric monopoly dominates the market should be replaced by a more open market structure that will encourage competition and economic efficiency and attract much-needed private investment.

The electricity regulator ERE will play a much stronger role in overseeing and implementing energy policy in the future, having full authority to review and approve electricity tariffs during the transition to cost-based pricing.

ERE should be solely responsible for reviewing and approving electric tariffs, protecting consumers, other electricity market participants.

Of course, the ERE' decision-making will always be guided by an appropriate legal framework established by Parliament and the application of internationally-recognized principles of regulation.

The Strategic Action Plan envisions that the electricity regulator will play a much stronger role in overseeing and implementing energy policy in the future. The USAID recommends granting the ERE full authority to review and approve electricity tariffs during the transition to cost-based pricing. Over the next several years, the ERE is also designated as the appropriate entity to lead a series of public,



collaborative proceedings that will develop the rules and structures necessary to implement a modern, commercial electricity market.

This old-style form of regulation is incompatible with the USAID's vision of a modern, commercial electricity sector comprised of investor-owned companies. Private investors will not participate in a market over which the government maintains undefined, broad and intrusive control. The new, competitive electricity market requires a new form of regulation that is transparent and free from undue political influence. The independent electricity regulator balances the interests of consumers and investors in accordance with parameters specified in an energy or regulatory law and widely recognized regulatory principles.

The roles of the ministry responsible for energy matters, the electricity regulator and other government entities under the new style of regulation need to be clearly defined and understood. The ministry responsible for energy matters continues to exercise considerable authority over key policy issues, including in particular matters that may affect energy security such as maintenance of adequate fuel reserves, the diversity of fuel sources and the level of energy imports. On the other hand, the 'independence' of the electricity regulator does not mean that the regulator operates without constraint. The electricity regulator must remain accountable to the ratemaking authority and other standards specified by law. The 'independence' of the regulatory authority refers only to its autonomy to make certain decisions specified by law, such as raising or lowering tariffs, without the approval of political authorities. In other words, the regulatory authority operates with respect to its assigned regulatory functions at arms-length from government interference.



## 6.2 Transparency

A regulatory authority must be seen to be fair to both consumers and investors. This means that the ERE must operate in a manner that is transparent, objective and non-discriminatory. The perceived fairness of the regulatory authority is particularly important in a situation such as that in Albania where it is necessary to raise prices that have been kept artificially low for many years. In order to build public support for the regulatory authority, the USAID recommends that the ERE take formal action at the earliest reasonable opportunity to publish procedural rules that it will follow in all of its proceedings. These rules should provide public notice of all proceedings, allow an opportunity for public participation and comment and require the use of written decisions explaining the basis for the regulatory authority's actions.

## 6.3 Consumer Protection

As the entity responsible for ensuring consumer protection, the ERE will develop formal consumer protection rules, such as standard procedures for processing consumer complaints. In the first instance, consumer complaints should be handled by the licensee. The ERE may specify minimum response times and other performance criteria related to the processing of consumer complaints by licensees. If a licensee ultimately is unable to satisfy a consumer, the complaint should be forwarded to the regulatory authority for further review.

The ERE should have jurisdiction to review investment plans and all major programs initiated by KESH that will impact KESH's ability to provide reliable service to Albanian consumers at reasonable costs, such as KESH's programs to increase collections, reduce technical losses and improve the reliability of the transmission and distribution system.

## 6.4 Service Quality and Standardized Consumer Contracts

ERE will work with licensees to develop standardized consumer contracts that specify the general rights and obligations of both licensees and consumers. The standardized consumer contracts will



address numerous common service issues, such as the minimum technical standards, disconnection procedures and payment obligations. It must be recognized that KESH's ability to provide reliable, high quality level of service is related to its ability to collect revenues from consumers and eliminate electricity theft.

#### 6.5 Regulatory Accounting and Reporting Requirements

In order to fulfill its obligation to review and approve tariffs proposed by KESH and the other licensees, the ERE must have access to adequate technical and cost information in an appropriate format. The Strategic Action Plan emphasizes the right of the ERE to have access to relevant information and the corresponding obligation of the licensees to provide such information. The USAID also recommends that the regulatory authority initiate a formal proceeding in 2002 to prescribe a uniform regulatory accounting and reporting system that will apply to all existing and future licensees and that will facilitate the ratemaking and regulatory process. This accounting and reporting system should reflect the future structure of the electricity market in which transmission, generation and distribution are unbundled.

### 7. CONCLUSION :

In the end, the successful reform of the electricity sector in Albania will depend on the strong commitment of Albania's political leaders and people to implement the Strategic Action Plan.

The ministry responsible for energy matters had to develop broad policy goals, conduct planning and forecasting studies and establish enforceable energy security and reserve guidelines.

The Government may regulate openly and directly through published rules, decrees, and licenses I am sure that Albania will not just overcome the immediate problems of the existing electricity shortages, but will create conditions to ensure that the electricity sector will become economic assets that boost overall economic growth, rather than liabilities restraining such growth.