

Panel I V Regulation of the Internal Energy Market: a Policy for Slovakia

Example of gas distribution

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- § distribution of natural gas to consumers in Slovakia
- § marketing and management of access to network capacities
- § operation of the distribution network
- § provision of gas to households in emergency situations
- § connection to the distribution network
- § meter readings

A main contributor to the development of the Slovak economy

SLOVAK DISTRIBUTION NETWORK



2007

- > 31 500 km (incl. ~6 350 km High Pressure)
- 50% polyethylen – 50 % steel
- 77 % of municipalities supplied with gas / 94 % has access to gas / 1,46 millions off-take points
- 5,4 bn.m³ distributed

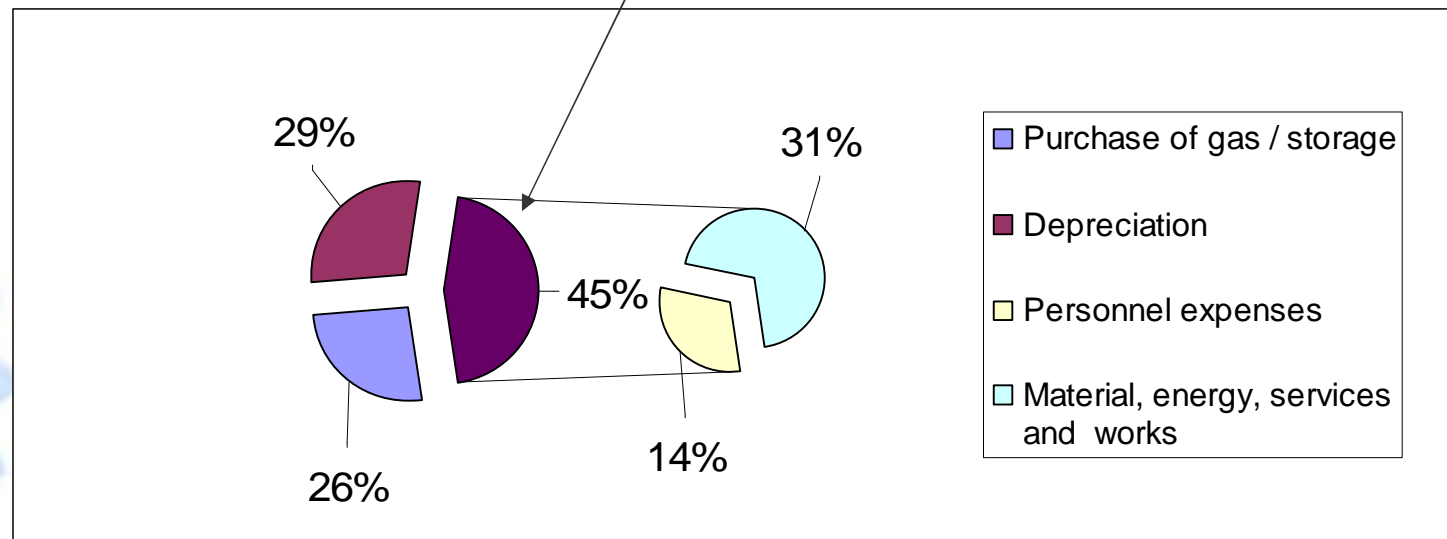
- § Year 2009 is cut from the current regulatory period (2006-2009), which is replaced by a new shorter one 2009-2011
- § *Revenue cap* methodology is replaced by *price cap*
 - | 2009 tariffs derive directly from 2008 ones (risk on new eligible expenses)
 - | price for gas purchase is the only new expense clearly taken into consideration by the methodology
 - | productivity factor of 5% per year (capped by inflation) applies to prices
- § No correction factor (risk if assumptions are not met : volume, price of gas ...)

Budget 2008	bn. SKK
Revenues	12,2
Expenses	7,9
Profit	3,5

ROCE = 4,5 %

(~ 80 bn. SKK assets)

Space for maneuvering



- § Costs for gas purchase or storage are market based and have already grown, making the space for maneuvering even lower
- § It is uncertain how the Regulator will take them into consideration even if
 - | storage costs are eligible (gas market rules - article 29 (3) Decree 409/2007)
 - | price for gas purchase : which price for 2009 ?
- § Amongst controllable costs
 - | salaries should follow the market
 - | materials (steel, plastic ... from oil) are growing
 - | construction prices are growing (Eurostat : +6,7% in 2008)
 - | electricity price is growing (> 10% ?)

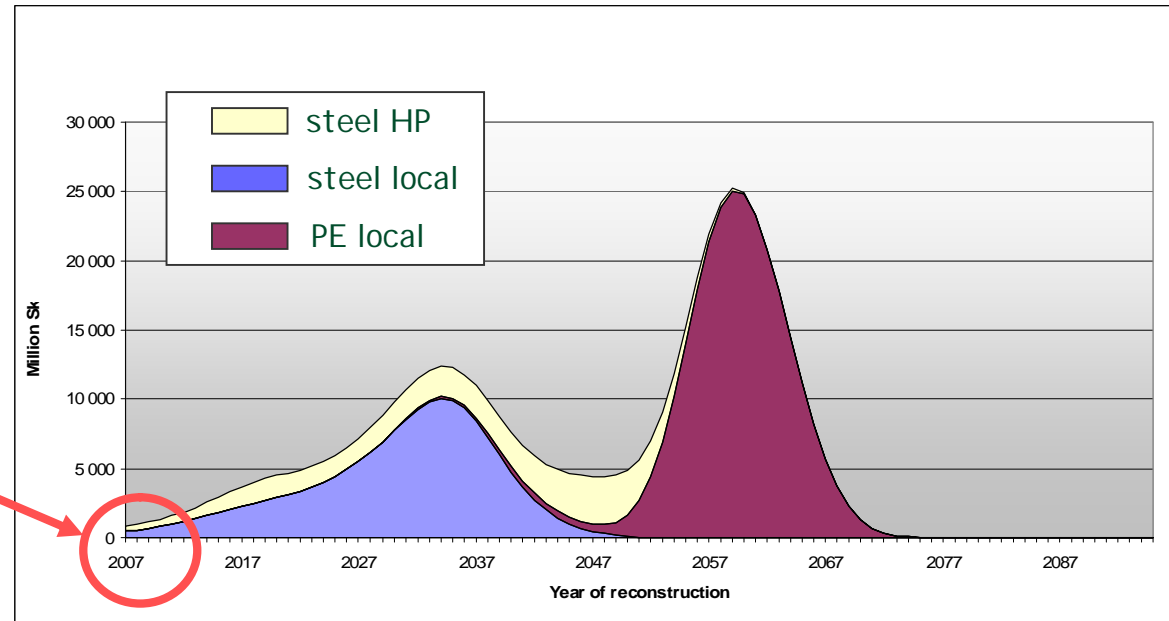
§ A productivity factor of -5% / year

- | it means around -15% when controllable costs and previous developments are considered
- | -33% / year applied to the workforce of SPP-D, which is totally unrealistic

§ Some benchmarks in other countries per year

- | CZ = -2,1 %
- | HUN = -2% (average)
- | UK = -2% (average including -2,5% limited to OPEX)
(after an increase of +2% / previous period)
- | FRA = -1,3% (average including -2,7% limited to OPEX)
(after a +5,6% at the beginning of the regulation period for reconstruction purposes, unbundling and consideration of evolution of volumes)

§ Investment Costs Based on Technical Life Estimation



We are here !

§ Depreciation will inevitably grow despite taken measures

- | optimization of the decision making process and costs (procurement of works and material)
- | increasing the lifetime of the network by cathodic protection and better maintenance

§ SPP-D did not wait to control its costs :

- | optimization of structural costs (-13% between 2007 and 2009)
- | optimization of O&M costs (introduction of mobile technologies to decrease unnecessary travels, reduce reaction times)
- | however the new methodology does not bring any motivation to invest for supporting these changes

§ The new methodology, without taking into consideration development of costs endangers the capacity of the operator to fulfill its missions (safety, reliability, development)

- § The previous methodology, a mix of revenue cap + price cap, including a correction factor, was an advanced methodology, recently adopted by France
- § Price cap approach usually corresponds to a situation where
 - | reserves exist for cost savings
 - | volumes are controllable and may increase (which is unlikely before 2010-2011 in SK)
- § A risk of sub-investment is real when they are not remunerated (it does not mean uncontrolled)
- § UK experienced it and was then obliged to install many motivation tools to correct these shortcomings

§ Price cap is OK in principle, but it should take into consideration eligible costs impossible to control by the operator

§ Our request remains

- | long-term visibility
- | realistic consideration of economical framework /cost-reflective prices
- | awareness of the Regulator about necessary investments to keep the level of safety and reliability

On one hand, the Office has to protect end-user against abuse of the dominant status of the monopoly suppliers of energy, on the other hand it has to ensure such return on investment of the enterprises that enables them to provide safe, quality and reliable supply. Finding the balance between two poles of interests - consumers and suppliers of energy - in a way that the economy works well on both sides, is the task of the Regulatory Office

Source : www.urso.gov.sk

Thank you for your attention !