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ROUNDTABLE ON COMPETITION ISSUES IN THE ELECTRICITY SECTOR

-- Republic of Lithuania --

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ROUNDTABLE ON COMPETITION ISSUES IN THE ELECTRICITY SECTOR

Lithuania

Overview of Regulatory Framework

1. Until recently, the Lithuanian electricity sector was characterized as having monopolistic entities with prevailing state ownership, providing no grounds for competition, running huge overcapacities, and obsolete technologies. The major participants in electricity supply and distribution were: state – owned Ignalina nuclear power plant (NPP, a generator producing around 80% of today's electricity need in Lithuania), Lietuvos Energija (a state monopoly for electricity transmission and distribution in Lithuania, however, it also included within its organizational structure two thermo-electric power plants plus a hydro-accumulative power plant and a hydro-electric power plant), and three thermo-electric power plants in major cities owned by local municipalities. The primary fuels used are nuclear fuel (cassettes) and natural gas.

2. The Lithuanian government recently has initiated the implementation of a new policy in the main objective of which is to abandon monopoly in the sector and to create conditions for freer market and competition to exist.

3. Two laws were adopted creating the legal basis for the opening-up of the electricity market for competition. First, **Law on the Restructuring of Lietuvos energija (2000)** provided for the division of this huge state monopoly into three independent structures: generation, transmission and distribution. Now, after restructuring LE, it no longer combines all these three functions – it is only a regulated transmission monopoly, and all electric power plants have been separated from LE and are independent electricity producers. The distribution network was also divided resulting in two separate distributors operating in two different parts of the territory.

4. So at this moment there are several major producers of electricity: Ignalina NPP and five local thermo-electric power plants located in major cities, apart from numerous smaller local electricity producers. However, Ignalina nuclear power plant will be gradually shut-down, responding to the requirements of the European Commission in the pre-accession negotiations. The first reactor will be decommissioned by 2005, and the second – by 2009. At least until 2005 there are very few incentives to build any new power plants. Even following 2005, the still operating second reactor will make any significant new entry into the market very unlikely. There is still a lot of uncertainty as to the situation following 2009 after the second nuclear reactor is decommissioned.

5. **The Electricity Law (2000)** provides for the opening of energy market in Lithuania and the creation of possibilities for competition, primarily among generators and to a lesser extent among distributors.

6. A transmission company (the operator of the transmission network – higher voltage lines) is providing the services of energy transportation via transmission lines, and is also acting as a dispatcher of energy flows and as a balancing unit. Two distribution companies (the operators of the distribution networks – lower voltage lines) are in charge of supplying energy to end-users.

7. The new law provides for that at the initial stage of the market creation only some major users ('free users', i.e. those which annually consume over 20 million KWH of electricity) are able to choose

among electricity suppliers. These major users are free to choose their suppliers at their discretion, and can buy electricity directly from producers or other suppliers, which in their own turn conclude agreements with networks operators to transport energy through their power lines (third party access). However, free users and suppliers can import energy only with the permission of the Government or an institution authorized thereby. Later on the number of free users will be gradually expanded to include smaller users, and starting from 2010 all users will be free to select their own suppliers.

8. There are also plans to develop the common electricity market for all three Baltic states – Estonia, Latvia, Lithuania to be implemented prior to the EU accession. Technically this is achievable at reasonable costs due to the transmission lines that have been linking the three nations since the Soviet era, and are relatively modern.

9. An electricity regulator – the independent Energy Commission appointed by the President of the Republic – regulates electricity prices (indirectly – by establishing price calculation methodology and formulas) of those producers and suppliers which account for more than 25 % of the market. However, free users can buy electricity from whatever supplier at an agreed price. Other users (‘non-free users’) have to buy electricity at “public prices” from a public supplier – the distributor obliged to supply energy to non-free users in the respective territory. Maximum “public prices” are established by the Energy Commission, however, concrete prices below the established maximum ceiling are not regulated.

10. The transmission company maintains the monopoly position, however, maximum prices for transmission services, as well as for distribution services by the two separate distributors are established by the Energy Commission, based on the costs of the relevant companies.

11. The vertical integration between generation and transmission has been dissolved, and it seems that separation of power generation from its transmission and distribution up to now has proven quite successful. The transmission company and both distributors operate at a profit, as well as major generation companies, while the electricity prices remaining stable.

Market Structure and Market Rules

12. The total generation capacity in Lithuania is 6500 MW, and it is the double of the domestic demand for power. The transmission network, as well as major generating capacities, have been built up in Soviet times and today Lithuania runs power generation capacities by far exceeding national demand. Therefore there are no congestion problems and no need to expand capacities any further. However, any necessary expansion of the generation or transmission capacities is possible only upon the receipt of the licence from the Ministry of Economy

13. The main power generator is the Ignalina nuclear power plant with around 80% of the market share. The remaining 20% of the market are shared among five thermo-electric power plants and other smaller local power suppliers. Power transmission and distribution are separated from power generation activities. There is one transmission firm and two distributors.

14. There are actually no commercial imports. Imports are restricted by the law, and only the government or its authorized institution can issue the permission to import, provided that the exporting country has authorized the import of the same volumes of power from Lithuania. Exports destinations are mainly Belarus, Latvia, Russia and Estonia.

15. A market in wholesale electricity is now in the process of development. The law provides for a market operator which will be organizing a kind of electricity auctions. The market operator will also publicly announce the market-determined power price. However, the market operator (i.e. an electricity

auction organizer) has not yet been selected.. Also, up to this time, the secondary regulations defining rules by which energy trade is to be organized are still in the stage of drafting and deliberations, i.e. have not yet been adopted. It is not yet decided whether the participation in the spot market will be mandatory or voluntary. So the electricity exchange is in the early stage of its development.

16. Competition authorities have not dealt with any merger, or established collusive behaviour or abuse of a dominant position in this market, possibly, mainly because the separation of functions and establishment of independent business entities are very recent decisions, and, although there are several operators, in monopolistic sectors a rather extensive regulation of firms' activities remains in place.