

**1<sup>st</sup> Energy Regulation & Investment Conference**  
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**KEYNOTE ADDRESS**

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**President Jorge Vasconcelos**  
*Council of European Energy Regulators (CEER)*

Good morning. It is my pleasure to address this first Energy Regulation and Investment Conference and first of all, I would like to thank the Energy Regulators Regional Association [ERRA] for their invitation to be here with you today. I would like to welcome all the colleagues from the ERRA, but also from the United States of America who are here today and who have been extremely supportive of the initiatives in the regulatory field and the energy field in many European countries for the last 10 years.

Let me just briefly introduce the Council of European Energy Regulators. We represent the energy regulators from the European Union and Norway. We have, as our major goal, to contribute in an active way to the achievement of the internal energy market. We are talking about a very huge reality. I will give you just some figures. We are talking about 210 million electricity consumers; about 72 million gas consumers; more than 2,000 companies in the electricity sector; and a little less in the gas sector. We are talking about something like 2,000 terowatt hours electricity delivered and about 100 billion Euros turned over in the electricity sector. This is the energy reality in Western Europe which we are in charge of regulating, together with European institutions and in particular with the European Commission.

We are committed to the development of efficient energy markets, which are truly integrated, which are truly pan-European markets, fair and transparent markets. We have been practicing a model, which is characterized by what I call regulation by corporation, as opposed to regulation by litigation. This is an idea that regulation to be efficient and to be socially responsible has to be open and has to try to achieve a good enough standing and mutual understanding of all the stakeholders and to promote this dialogue on a firm basis.

I will try to be very brief and to share with you some thoughts about the two key concepts of this conference – investment and regulation. Of course, the energy sectors needs both. It needs investment and it needs regulation. I will not talk about how to invest because this is the core business of the banks and the financial institutions. I will, from my personal point of view, say a few words about where and why to invest, and of course, then I will tell you something about how to regulate and I hope these two pieces of information will fit together and will provide some ideas about how the two concepts, the two necessary dimensions of investment and regulation can work together.

Where to invest? To understand the investment possibilities in the energy industry today, it is necessary to keep in mind that we are increasingly dealing with externalities and that these externalities are extremely important in determining the freedom of investment. We have an energy policy in Europe, which has three major goals. One is the competitiveness of the European economy; the other two are security of supply and protection of the environment.

Security of supply is obvious for a continent that imports 50% or more than 50% of the energy its needs, and protection of the environment is also a necessity resulting, among other things, from international commitments of the European Union. And it is important because we want to keep or even to improve the quality of the environment where we live, where we work.

This translates into practical targets and objectives for the energy industry in Europe. The other aspect, which has to be kept in mind, is that the industry is being restructured and there is a legislative process to restructure the industry in Europe. One of the main characteristics of this process is the idea of unbundling, of separation of the different sub-activities within the energy, the electricity or the gas sectors, and mainly separating generation, transmission, distribution and supply. Therefore, I will go through these different elements of the energy chain to discuss very briefly what are the investment possibilities or opportunities in each one of these sub-sectors.

Starting by generation, you should know that in the European Union there is a goal to have about 12% of all the energy consumed in Europe by 2010 produced by renewable sources and this translates in more than 20% of electricity produced in Europe from renewable sources. There is also a goal to support the development of co-generation and the goal is to have about 18% of the electricity produced by 2010 coming from co-generation facilities. So, these are obvious opportunities for investment.

Also, distributed generation is becoming very interesting for many applications and we are seeing, in some countries, the development of very small generating facilities, very close to demand, and this has been stimulated in several member states of the European Union. And, of course, we will need conventional power stations to replace all the old power stations and to cope with electricity growth.

As regards transmission, there is also room for investment. First of all because it's not possible to build an integrated European market if the transmission infrastructure is not available. And this applies both to electricity and natural gas. And, the transmission infrastructure was not planned and was not built for the purpose of cross-border trade. So, if we want to develop a truly integrated European energy market, we must invest on cross-border interconnections, both in electricity and in pipelines for natural gas. So, investment in transmission must enable cross-border trade. It is necessary to enable also the connection of the new generators: renewables and co-generation and decentralized generation. This is a challenge to the owners of the grid. This requires new planning tools. This requires a new approach to investment in transmission. And, investment in transmission is also necessary to improve the way the transmission assets are being used. As you know, electricity has some strange physical laws and electrons tend to behave in a very improper way. So, there are, nowadays, thanks to technological developments, ways of partially controlling the flows of electricity, and this should be done in order to extract the maximum benefit from the existing transmission assets.

For distribution there is also a challenge in terms of planning the networks and investing in order to enable decentralized generation, independent generation to come to the network and to get access to the market, and there is a growing concern with the quality of supply namely because many of the users have increased requirements in terms of quality because an electronic device is being used in both services and industry which requires sometimes extremely reliability and

quality standards. So, this is also a challenge. The quality of supply has to be better quantified and investment in distribution has to take into account in a more objective and quantitative way the aspect of the quality.

As regards energy consumption, there is also room for investment in efficiency, improving efficiency. There is a goal in the European Union to improve the energy efficiency of the energy sector by 1% per year. There is also a goal to improve the demand side management, to improve the attention paid to the management of the energy consumption facilities.

So far about investment, where to invest and why to invest.

Now, about regulation. How should we regulate and how can this have an impact upon investments in the energy sector? Most of the things I'm going to tell you have already been said before. I will, therefore, be very brief and I have a note here, seven characteristics of regulation which I believe are important in the context that we are discussing here. The order is not necessarily the order of importance.

First independence. Regulators must be independent from the industry they regulate and also from political power. Governments and parliaments have their cycles and this is not necessarily positive and this is not necessarily coherent with the investment cycles. Therefore, regulators can and should be a buffer between these two different kinds of cycles and this should ensure some high level of trust and confidence, both from the political decision-makers and from the consumers.

The second characteristic is called "reasons-giving:" regulators should justify and explain all the decisions they take. They should justify their working program. They should justify what they are doing, which decisions they took, why they took those decisions, what were the assumptions, the models they used, the evaluation they did of different alternatives.

The third characteristic is transparency. The procedures used by the regulator have to be fully transparent. Nothing should be hidden and all the internal/external procedures should be known.

The fourth characteristic is stability, predictability of the regulator. I believe this is extremely important for investors. At least this is usually the first priority of investors who visit us regularly. Their major concern is the stability and predictability of the regulator.

Fifth – the regulator should promote and facilitate the fulfillment of general interest objectives, which are set up and defined by the political bodies, by the government, by the parliament. Regulation is not in charge of defining these goals; its task to facilitate the fulfillment of these objectives in terms of security of supply, for instance, complying with the energy policy of the country; in terms of protection of the environment, facilitating, for instance the development of renewables or energy efficiency or energy conservation; and social policy, as has been suggested by the President of the EBRD.

Sixth – regulation should promote efficiency, should promote the efficient allocation of resources, both natural resources and capital.

And, the seventh characteristic – regulation should be fair. It should be fair in the sense that it promotes a fair balance between the legitimate interests of energy consumers and the legitimate interests of the shareholders of the companies. But, it should also be fair in terms of non-discrimination between different companies and different investors. This is something that is becoming difficult in some regions because of the regional dimension, which Mr. Lemierre has mentioned, which is a characteristic of the development of energy markets, not only in Western Europe, but also in the U.S., and Central Europe and South America, and many other regions of the world. We must recognize that there are difficulties because we have a national way of thinking; because in the past electricity and gas were seen as something extremely associated with a national identity, especially in some countries. The energy companies are, or were, part of the national identity and this creates some difficulties. Why? Because we cannot fulfill our objectives in terms of environmental protection or security of supply on a mere national basis. These objectives can only be achieved on a regional, international basis.

Pollution is trans-national; security of supply cannot be achieved by any European country on an individual basis. Therefore, what we need is a strong, large energy market where strong players can play, where strong companies can compete among themselves, and then, of course, we need strong regulation. I was very happy to hear from Mr. Lemierre that he also supports that view. We need strong regulators because otherwise the strong market, with very strong players, will be out of control and this can be something not very good for the energy consumers and therefore, for the European economies.

I believe that by sharing our experiences and by sharing our knowledge, we will be strong and we will be able to better fulfill our duties towards the energy consumers and towards all European citizens.

Thank you very much.