



THE ROMANIAN ENERGY REGULATOR (ANRE)

- A DETAILED ASSESSMENT -

Bucharest, Romania, 2010

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Ana Otilia Nuțu

Introduction: Romania's energy sector in a nutshell

Context:

A decade ago, a major change in EU's vision for the European energy sector took place. Before, it seemed acceptable that national energy markets are virtually segregated and dominated by national champions, vertically integrated state monopolies. But this is in contradiction with the goal to have an Internal EU market, and with the consumer's interests, deprived of choice. The new plan was to introduce in both electricity and gas as much "market" as possible: separate monopolies from competitive activities, enhance competition in wholesale and retail markets, including cross-border connections, with the ultimate goal to give the consumer a choice and improve security of supply. But the new roles of energy sector players required also a new regulatory framework: independent national regulators were set up to ensure suppliers and networks operate correctly and provide services promised to customers.

An aspiring EU member at that time, Romania quickly became a leader in such reforms and started in the late '90s an aggressive, but successful energy sector liberalization program, way ahead of old EU member states like France. Romania's reforms meant a break up of national vertically integrated companies (electricity, gas) into producers, independent transmission grids, suppliers and distributors, in 1998-2000. Energy regulators (initially separate for gas and electricity) were set up; in its early days, ANRE, the electricity regulator, became a good practice model, copied by regulators in older EU member states (France, Germany). The fact that Romania was negotiating EU accession, including a chapter on Energy, "pushed" the Romanian political leadership to embrace reforms and prepare ambitious strategies following EU's liberalization thrust (such as the "Energy Road Map" of 2003).

Romania's reforms had two major benefits, in addition to improved consumer choice:

- they improved sector governance, by increasing the transparency of energy producers, separating loss-making entities from viable ones, and reducing cross-subsidies. This was a huge improvement, considering the soft budget constraints existing in the sector and widespread perception of corruption; and
- they created the prerequisites to attract much-needed private investments in the sector, where major units are falling apart because of obsolescence (and the state simply does not have enough money for upgrades). Indeed, privatizations were started in 2004-2005 (one gas + oil producer, 5 electricity distributors and suppliers).

After Romania's EU accession, and even earlier, after the accession negotiations were closed, there remained little external anchors to finalize the reforms in the energy sector. Privatizations were stopped, because of partly real, partly misperceived problems; but budget constraints also do not allow the state to make major investments in units that are too old to be profitable or too polluting to meet

EU's environmental conditions. A major setback to the reform is the fact that the government even considers the return to integrated energy champions, against the EU trend. First, they proposed to create one national power champion containing state owned electricity producers, distribution and supply; then two integrated companies, containing electricity plus loss-making mines, with or without distribution. This idea discouraged private investments in the electricity sector, such as PPPs, which are practically stalling since 2007-2008.

The regulator ANRE (electricity, then merged with gas in 2007) experienced a dramatic decline in the public perception after 2005, when the EU negotiations were finalized. ANRE has been involved in several public scandals in recent years, being accused in the media for politicization, departure of key staff, nepotism, and waste of public money. ANRE received a final blow in 2009, when it was transferred under the subordination of the General Secretariat of the Government, lost its own budget, and cut the salaries of key personnel by about 70%.

Politicization and clientelism are a key concern across the Romanian public administration and the energy sector (in which a lot of money is involved) has not been spared. The management of state-owned companies and the leadership of the regulator have been changed at each change in government, sometimes even more often, with no connection to actual performance. This practice intensified after 2005-2006.

In the meanwhile, liberalization reforms are ongoing in the EU, even in very reluctant countries like France; this widens the gap between Romania and older EU states, and has increased the likelihood for infringement actions against Romania (one was initiated in 2009, another one will follow in 2011). EU energy regulators have gained much more strength and capacity and their role is continuously evolving: from tariff setting and access to networks, to enhancing competition, protection of consumer rights, support for environment and renewables by market instruments etc. ANRE's focus continues to remain tariff setting (networks, captive consumers and "social tariffs"). What is worse, some of its regulations are barriers against competition in the energy markets, both wholesale and retail.

Who's who in the Romanian energy markets:

1. Companies:

Much of the Romanian energy sector remains in state hands. Apart from the transmission grids for gas and electricity, the state owns all major electricity generators (cca. 6); half of the domestic gas production (1 of the 2 big gas companies) and all gas storage; and 3 out of 5 electricity distributors. All state shares in these companies are managed by the Ministry of Economy, through its department OPSPI. OPSPI is not very effective in managing the companies as a holding, which has proven actually beneficial for some competition in the state-owned generation sector (some state-owned companies "compete" on the market, e.g. the three energy complexes Turceni, Rovinari and Craiova).

In the past years, some of the state-owned generation companies have been involved in media scandals (eg, non-competitive and non-transparent sales of cheap electricity or gas to favoured private partners).

Transmission operators (particularly Transelectrica in the power sector) remained independent from generation and ensure non-discriminatory third party access.

Transelectrica remains a company with strong corporate governance, but this could be under threat if the management is further politicized.

There are many suppliers in both electricity (about 60) and gas (over 100).

Romania is a net exporter of electricity (about 5% of production) and imports gas from Gazprom (usually around 30% of consumption); it is thus relatively energy independent.

2. Regulator:

Since 2007, ANRE is in charge with the regulation of gas and electricity. Its regulatory focus is mainly on setting tariffs for networks and regulated consumers (captive or social). ANRE is led by a President, has 3 Vicepresidents, a regulatory committee with 5 members (directors of different departments in ANRE) and a Consultative Council with 7 members (Ministry of Economy, associations of businesses in energy, trade unions in energy, local administration etc.), which debates on major regulatory items and positions in the EC or international associations of regulators. All are appointed by the Prime Minister. Though in its early days ANRE was considered a good practice in the EU, in recent years ANRE has had serious governance issues – the reason why we initiated the project.

Also, ANRE's technical capacity is declining because of loss of key staff. The Commercial Code is well developed, but ANRE lags behind the de facto liberalization of gas and electricity markets. For technical regulations it relies – sometimes excessively – on transmission sector operators (Transelectrica and Transgaz). This practice is however currently acceptable given the serious governance issues in ANRE, and the fact that the TSOs are relatively better performing on the technical matters and well-governed (particularly Transelectrica).

3. Markets:

Romania's gas and electricity market models are competition on both wholesale and retail markets. While in principle fully liberalized in 2007, the actual market opening is around 50% in both electricity and gas. That is, about 50% of the gas and electricity consumed in the country are sold to “captive” consumers.

3.1. Wholesale markets:

Wholesale markets are markets where suppliers buy from producers or other suppliers.

In electricity, there are several wholesale markets:

- long term bilateral contracts: about 20% of the electricity sold long-term is sold competitively, in the power exchange OPCOM, in forward or futures contracts. The remaining cca 80% is sold on bilaterally negotiated contracts outside the competitive market. Since all generation is state-owned, the fact that a large share of electricity

sales is done without selecting competitively the private partner is a source of suspicions of corruption (e.g., undervalued sales).

- day-ahead market, on OPCOM: a voluntary, competitive spot market for electricity

- balancing and ancillary system services markets: As electricity cannot be stored, supply must exactly meet demand. This balance is achieved by having enough generation or demand side participation. Demand side is when large energy users sell back the electricity they would have used during periods of high demand. In the short-term, wholesale markets achieve an approximate balance. Fine tuning and outage compensation is done by the TSO which ensures the security of supply on a second to second basis. To this aim, Transelectrica administrates a day – ahead and (quite recently) intra – day balancing energy markets having a share between 4 and 14% of electricity produced to balance the system. On the ancillary system services the buys and sells are structured in such a way as to mimic the trading on a competitive market (with TSO as a “broker” between buyers and sellers). This particular market is largely dominated by the hydro producing company; the regulator sets a price cap for ancillary services to mitigate the monopoly position. In addition, 5-10% of electricity consumption and production are traded cross-border. The allocation of cross-border interconnection capacity is done competitively by Transelectrica and neighboring TSOs on a bilateral basis, by auction.

OPCOM is a well-functioning power exchange, ranking 8th in Europe, and has the prospects to become a regional market (to include Hungary and Austria by 2011-2012, and possibly Serbia-Bulgaria-Greece in the future).

50% of the electricity market is liberalized. The other 50% consists of regulated contracts: 8 implicit suppliers, which own also distribution networks, buy a regulated “basket” of energy from several producers. ANRE regulates the quantity and price of the basket. The 8 suppliers sell on the retail market to “captive” consumers electricity at the regulated basket price plus transmission tariff plus distribution tariff. The competitive market trades what remains outside of the “basket” consumption.

The gas wholesale market could be similar (with the difference that gas can be stored, so there is no need for balancing or ancillary services, but there is a market for storage capacity). However, so far the wholesale gas market lacks centralized trading platforms like day – ahead and “forwards” being exclusively based on bilateral deals, either regulated or negotiated. Again, 50% of the market is “captive”; two suppliers, which manage separately also distribution networks, buy a regulated basket of domestic and import gas, and ANRE keeps the domestic prices low to control the end-user price. Captive consumers pay the gas plus regulated tariffs of storage, transmission, and distribution.

3.2. Retail markets:

On retail markets, suppliers sell gas or electricity to end-users. They consist of a competitive part (where users choose their supplier) and a “captive” part (where users remain with their existing supplier). ANRE’s tariff policy (low prices for captive end-users) is a barrier to full market liberalization.

Methodology

An effective regulatory framework is one that supports good sector performance. To have a complete image of how the energy sector regulator performs, two dimensions of regulation need to be assessed: **regulatory governance** (institutional and legal framework based on which the regulator makes decisions) and **regulatory substance** (the quality of actual decisions, implicit or explicit, made by regulatory body). We look at specific elements of regulation relating to governance and substance and assess whether they help or hinder energy sector performance; these specific areas were determined also based on discussions with our board of experts. The main focus of the current assessment is thus on regulatory governance (80%) with a test of several key aspects of regulatory substance (20%), meaning assessment of the actual decisions (e.g., such as the effects of proposed market and monitoring rules, tariff structures or licensing methods, where an ex-post evaluation is possible; and test on whether the regulator's policy is consistent or not with the best legal and economic thinking). The focus on regulatory governance is caused by the following:

- it is relatively easy to understand by a non-specialist and will increase the understanding of the general public that a regulatory body, no matter how technical, must still be accountable to the general public.
- while regulatory governance is not enough for good quality regulation, experience shows that poor governance always leads to poor quality regulation.
- ANRE's technical capacity (market rules, methodologies for tariffs levels and structures, licensing regulations, quality standards, network access conditions etc.) has been increased through various consultancies, and ANRE used to be among the top regulators in Europe until the early 2000s. Various scandals in the media regarding ANRE concern political appointments at top levels, political interference in regulation, excessive salaries, increase in budget and number of personnel, non-transparency of tariff-setting procedures, leave of key personnel etc. If the best practice methodologies in the consultancies are currently not applied properly, this is both the result of poor governance and lack of knowledge, due to replacement of specialists with political appointees.

On the regulatory substance, we selected a sample of key decisions of ANRE on licensing, market monitoring and tariff setting in electricity and gas, and checked whether these decisions meet the prerequisites for good regulation.

External constraints:

A well-functioning regulatory framework that is consistent with good sector outcomes would also require good practices in the following areas, which are not directly under the influence and control of ANRE. We treated them as external constraints and therefore the report does not contain an in-depth assessment or provide specific recommendations on these matters.

- a **strong corporate governance framework for state-owned companies**, so that all companies operate on hard budget constraints, and key players, public and private, play by the same rules (no favored actors). For state-owned companies in the energy sector, this includes: avoiding cross subsidies; ensuring maximization of profits by selling competitively (on the same principle why there are rules for competitive tendering in public procurement); willingness to grant managerial freedom to companies (instead of political appointments at Director level). Thus, the Ministry of Economy should control companies only through the General Shareholders' Assembly, not on the day-to-day operations of the companies. Also, the government and the Ministry of Economy should refrain from using political influence on the regulator (regulatory independence), either by political appointments of key staff in the regulator or by controlling the funding of the regulator;
- a **well-functioning judicial system**, so that consumers and investors have legal means of redress against uncompetitive practices or abuse from other companies or state organizations. This means that both courts and prosecutors' offices function properly and are virtually free of corruption;
- **general rules for public sector transparency**, so that the state-owned companies, the Ministry of Economy and the regulator are accountable to the public opinion for their actions, and framework laws concerning the disclosure of assets and interests of key politicians, civil servants, and other public sector employees with decision making powers in the sector. On a broader scale, the governance depends on the maturity of civil society and on the understanding from the public opinion that all state organizations are accountable to the citizen;
- **strong regulatory framework in general**, for example a well-performing Competition Council to deal with uncompetitive practices and avoid market concentration; good regulation of other utilities such as local energy (heating), to avoid cross-subsidies or market distortions; Consumer Protection; public procurement etc. **Romania is currently the laggard in Europe in terms of regulatory framework**, as illustrated by the World Bank's Governance Indicators (Kraay – Haufmann);
- a **good technical capacity in the Ministry of Economy**, who is responsible for the general energy policy, security of supply and also the major shareholder of state-owned companies in energy (electricity, 50% of the gas). The Ministry should understand its role in terms of managing the complex issues of energy security and policy, meeting environment standards, proposing legislation to support investments in renewables etc. The protection of vulnerable consumers should be done exclusively through social policies managed by the Ministry of Labor;

- the **impact of EU regulations and benchmarks**. EU has played an important role before accession as an external anchor for the governance reforms, and continues to promote rules that support regulatory quality. The extent to which the EU rules have “teeth” is questionable after accession, considering there are little leverage instruments for good behavior. However, the energy regulation continues to be subject to constraints from the EU within the common energy policy (Third EU package). In addition, ANRE is subject to an infringement from the EU on policies for the regulated energy market.
- **Government interference with market structure**, meaning the impact that the proposed restructuring of the power sector (re-grouping the power and mining in two large dominant companies) would have on the regulation of these companies and on the market.

Benchmarking:

Where appropriate, we compared ANRE with regulators from other countries, using also the information from existing benchmarking exercises (EU, ERGEG, IERN etc.). There are however strong limitations in such benchmarks. Most importantly, such evaluations are self-assessments of regulatory bodies within associations of regulators, so some of the results can be biased – even with good intentions – or different agencies understand differently the same question or indicator (an issue raised also for Romania by our key specialists interviewed). Also, most evaluations are based on the powers and responsibilities in the law, whereas the practice might however be very different. Also, conditions vary among countries in terms of energy sector structure and role of regulator. Last but not least, the main benchmarking exercise we propose (a comparison in time of ANRE, the present report being the first evaluation of a series) has the advantage that it focuses on items that are relevant to the evaluated body and provides incentives for change within ANRE. However, there are some items of regulatory governance for which benchmarking with other countries is relevant and provides useful insights, and we also recommend ANRE to do self-assessments on these areas in the future. We selected 1-2 good practice regulators with which ANRE could be compared on transparency (e.g., completeness of website information) or substance (focus in regulatory activity). We used mostly the case of Ofgem (the UK regulator), because we found it a best practice model in terms of adaptability to challenges, quality of services provided to its stakeholders, public perception, and transparency.

Data collection methods:

The main sources for data and issues consist of:

- desktop research of legislation, articles in the media, reports written by specialists and benchmarking exercises done by regulatory agencies in Europe, data from statistical sources (national, Eurostat, World Bank database).
- structured interviews with key national and international specialists in the energy sector, from our Board and stakeholders. Interviews are based on a questionnaire developed with inputs from the Board and are adapted from

World Bank¹ and Inogate². The questionnaire is presented in the Annex to this report.

- tests on transparency – requests for information sent on FOIA (L544). In the detailed assessment – Transparency we detailed the list of information requested, with explanations on why those particular items were selected.

Definition and testing of indicators:

We used mostly qualitative indicators, which were adapted from World Bank and Inogate handbooks. They are used to fill in the Scorecard table at the beginning of the report and assess the relative performance of ANRE now, with its own performance in 2004 and a performance target. The items below are the “ideals” for ANRE, considering the existing energy sector environment in Romania.

A. Regulatory governance:

This part assesses the governance rules and procedures on which ANRE operates. This concerns the legal framework (ANRE's statutory documents, secondary legislation, laws regarding the energy sector etc.), but also the application of these rules in practice. We define several governance indicators, which will form part of the scorecard to evaluate and monitor improvements / changes in the way ANRE operates, during the project and in future evaluations. Some of these indicators are overlapping (e.g., an appeals process to the regulator's decisions is important also for independence – as an external safeguard that regulatory decisions are independent from regulated industry, the regulator being penalized otherwise; and for accountability – the regulator is accountable for poor decisions to those on which it enforces them).

Key indicators (target level – best practice considering “external constraints” – market structure, definition of roles in law etc):

- **Independence**

The target (benchmark) level is:

- the regulator has a distinct legal mandate fully applicable in practice, there are good prerequisites to keep the regulator free from political (ministerial) pressures and pressures from the regulated sector; it makes final decisions within its authority domain
- the regulator must not be subordinated (formally or informally) to one single person in the Executive or to the ministry owning energy companies, and the subordination and accountability of regulator must be clearly defined
- Regulator must have the possibility to fully control market rules and price setting for regulated market components without pressures from ministerial level (including informal pressures, such as “guidelines” for pricing); also, licensing and monitoring of market must be free from outside pressures
- must have budgetary authority (from own revenue sources)

¹ http://rru.worldbank.org/Documents/Toolkits/infra_regulation/FullToolkit.pdf

² http://www.inogate.org/inogate_programme/inogate_resource_center/training-materials/Training_Handbook_engl.pdf

- there must be an appeals process to create pressures on the regulator to make decisions that would not be reversed, e.g. to make sure the regulator is not influenced by one company from the regulated industry
- Executive leadership must be fixed-term, technical staff to be selected on competitive terms, appointments and removals of staff to be based on objective criteria – competence, interest etc.
- Regulatory Board and Consultative Council must be appointed by clear rules that ensure independence of individuals from regulated sector and political pressures
- The regulator must have highly trained staff in appropriate numbers to perform its functions and avoid contestations
- The organization structure and resources are adequate to perform its functions without pressures from government (but also without excessive expenditure).
- **accountability of the regulator**

The benchmark level:

- the regulator must prepare periodic (annual) reports of activity (in addition to energy market monitoring), to be discussed and approved in Parliament, and available to the stakeholders in due time. Alternatively (second best practice) the report can be approved by the Cabinet of Ministers, but NOT by one person in the executive, such as the PM
- there must be clear, legal rules according to which regulator must respond to requests and inquiries from the general public and stakeholders in energy, and these rules must be enforced in practice
- if judicial courts overrule decisions systematically, the regulator must take action to correct decisions, regulations etc. In the particular case of Romania, this must however be considered critically (the courts apparently tend to rule in favor of public institutions in most cases, the judicial system is not well functioning)
- responsibilities must be clearly defined among various regulatory bodies (ANRE, Competition Council, Consumer Protection, ANRSC etc.) and clear, structured and formalized relationships must be established among these bodies on issues needing coordinated approach (e.g. tariffs and competition on electricity market etc); there are no areas that remain not regulated when they should be (regulatory gap). The regulator is preventing the market dominance (e.g., is properly informed and consulted when Government attempts restructuring of state-owned energy companies that might have an effect on regulatory effectiveness)
- the regulator must give proper accounts of money spent, and have its financial accounts externally audited
- regulator must be accountable for performance (preferably audited externally), according to clear performance indicators, based on which the management can be reappointed and / or removed, and these rules apply without exception
- the regulator must have an ethics code, which must be applied in practice (e.g., avoidance of conflicts of interest, transparency of assets and wealth for

dignitaries beyond the normal requirements for any public institution, rules of conduct in sensitive situations etc)

- the regulator and staff must not exercise their powers with discretion, but only within approved rules and good practices (a quality assurance system should be in place)
- the processes by which the regulator makes decisions must be clear and consistent in time, both those formally in law and informal processes, to avoid decisions that discriminate in favor of one market player (this item is also under regulatory predictability)
- the regulator must be able in practice to enforce its rules and decisions and effectively supervises investment programs, service quality standards etc (e.g., the penalties on companies must be proportional to faults, there must be adequate remedies, and good responses to requests for clarifications from regulated sector. These items also contribute to ensure decisions are not arbitrary)

- **transparency of decision-making by regulator**

Benchmark level:

- all decisions of ANRE are publicly disclosed, including with justification, to be accessible to the public and stakeholders; in case of “emergency” decisions or frequent amendments to previous regulations, the “emergency”/amendment must be clearly justified and reviewed ex post. This includes also the information on the items discussed in Consultative Council and Regulatory Committee
- rules are applicable to all in the same category (no discrimination), and rules are published ahead of time
- stakeholders are properly consulted on decisions, not only informed ex-post, and there are no exceptions to the consultation / transparency rules
- regulator publishes reports on activity and performance, and on the energy market as well, on the website, to be publicly available to stakeholders and public in general (to be benchmarked with another EU regulator)
- Regulator answers promptly and adequately on requests for information based on FOIA (L544), on even sensitive issues (tariff structure; eligibility of consumers, access to networks, regulated market tariffs and “pool” structure; financial statements, auditing etc.)

- **predictability of regulatory decision-making**

Benchmark level:

- regulatory decisions must be consistent in time, and there are periodic revisions of tariffs and responses to changes in environment
- regulatory decisions are properly explained and justified (e.g. in good “substantiation notes”, which have to be of proper quality and publicly disclosed)
- Regulator learns from past experience (e.g. if decisions are systematically challenged, regulator must review them; the regulator monitors the impact of regulation in time, adapts in a flexible manner to changes in environment, ensures that regulations are not overburdening). However, amendments to

previous legislation must not be extremely frequent and must be justified by a feedback from the environment.

B. Regulatory substance:

This section examines the performance of ANRE in a selected number of decisions and orders issued in 2010. We chose 3 decisions for licensing, 3 significant Orders on tariffs for regulated consumers, 2 Orders on change of methodology for network pricing (transit tariff for transmission grid and amendment mid-term in the regulatory period of methodology for distribution tariff).

- Tariff design

Benchmark (target) level:

- The tariff setting mechanisms must not endanger financial viability of regulated companies (e.g. tariffs are cost recovery)
- Tariffs must direct company operations towards increasing economic efficiency and quality standards levels (tariff levels, tariff structures, automatic and non-automatic cost pass-through mechanisms; tariffs avoid cross-subsidization. Economic prices must be separated from social policies.) Prices and tariffs must be non-discriminatory (no favoritism) and with no cross-subsidies.
- Prices structures to remain stable and predictable, published in due time, consulted with regulated industry and policy makers
- Limit regulatory intervention to minimum, not to overburden the industry (“proportionality” principle: costs of intervention do not exceed benefits, regulations are proposed where there are market failures, for consumer protection, energy security etc.)
- Tariffs must be consistent with clear strategic goals, defined in advance (such as energy efficiency; social tariffs should gradually be replaced by social assistance systems for access to energy)
- Regulator must perform periodic reassessments of costs / regulatory review to check whether the base for approved tariffs remains the same
- Regulator benchmarks itself to “best practices” in similar countries to check consistency and appropriateness of regulation

- Monitoring & licensing

Benchmarking (target) level:

- Regulator receives systematic data from the energy market and information on request from regulated companies, and demands most information in standardized formats
- Regulator enforces always its rules, decisions, orders on the market players (eg penalties, revocation of licenses etc)
- Regulator criteria for licensing and authorizations is transparent, non-discriminatory, allows quality of supply, does not overburden companies
- Third party access to networks, including cross – border interconnectors, is non-discriminatory, in law and practice

- Revocation of licenses and authorizations is based on clear, objective criteria (e.g. poor quality, interruptions, financial bankruptcy), without undue interferences from political level / pressures from regulated sector
- Regulator has clear formalized rules to handle consumer complaints and observe them adequately (e.g. how many complaints and are they resolved quickly in comparison with other countries)
- Regulator monitors and enforces the implementation of criteria in privatization contracts (e.g. ENEL), monitoring in due time investment and maintenance programs, and quality standards that were committed at privatization
- Regulator monitors quality of service standards (are they comparable with EU standards – e.g. interruptions?)
- Regulator issues / monitors clear rules for investment programs and connection obligations of the network companies (regulated TPA)
- Horizontal coordination – regulator coordinates in a formalized, structured manner with other regulators on consumer protection, market competition on OPCOM / gas markets, environment policy
- Regulations respect property rights, do not restrict investments / access on the market to a company, do not unduly affect one company

Scorecard – Benchmarking ANRE to itself

	2004	2010	2011*	2013*	Immediate measures (by 2011, to reach target)	Mid term measures (by 2013, to reach target)
GOVERNANCE						
Independence					Govt: no direct control on ANRE; only approval of ANRE's report	Govt: control only through approval of ANRE's Report in Cabinet
Budget and subordination					Govt: repeal HG 1428 (budget, subordination to GSG)	Govt: check financial statements in Report
Change in leadership					Govt: amend and implement Law 13, leadership changed only for performance	Govt: replace leadership if Report is rejected
Informal political pressures					Govt: abstain from statements on prices, integrated cos	Govt: social protection, if any, completely outside prices
Relations with regulated sector					ANRE: no inappropriate relations to cos (shares, nepotism)	ANRE: no inappropriate relations to cos (shares, nepotism)
Accountability					ANRE: report on activity at 2004 level and full audited report on finances	ANRE: performance and financial reporting
Reporting and confirmation of leadership					Govt: change management only by Cabinet decision, on performance	Govt: change management only by Cabinet decision, on performance
Accountability to consumers, industry, public					ANRE: respond adequately to complaints, accusations in media	ANRE: full reporting on activities targeted to different audiences
Financial and auditing					ANRE: publish audited financial statements	ANRE: publish audited financial statements
Ethics and enforcement					ANRE: reinstate Code of Conduct, adapt, enforce, publish	ANRE: continue to publish results on ethics enforcement
Transparency					ANRE: publish and consult on all major decisions; 2004 level reports on website	ANRE: full performance reporting on website (Ofgem target)
Publish decisions (regulations + decision-making process)					ANRE: publish reg committee decisions and link decisions to objectives	ANRE: all decisions on objectives, monitor deadlines, explain delays
Proper consultation					ANRE: public hearings or e-comments on all major decisions	ANRE: launch e-debates on all major decisions, publish all comments
FOIA responses		TBD			ANRE: respond in full to all FOIA requests	ANRE: respond in full to all FOIA requests
Predictability					ANRE: maintain consistency on regulatory periods	ANRE: link decisions to sustainable goals & objectives
Consistency and justified amendments					ANRE: publish justifications for all amendments to Orders; work program on objectives	ANRE: full work program on objectives, explain deviations or changes
Adaptability to environment changes					ANRE: full debates on changes (tariffs, impact on regulatory framework of changes of sector structure)	ANRE: identify and launch debates on changes in environment, e.g. private participation in generation
SUBSTANCE						
Tariffs					ANRE: eliminate distortions on tariffs	ANRE: revise tariff policy to enhance competition, eliminate regulated prices for producers & consumers
Economically sound					ANRE: review tariffs for regulated consumers; abandon social tariff	ANRE: review tariffs for networks (transmission - tranzit, zonal tariff)
Periodic reassessments					ANRE: change of tariffs only on fundamental changes in environment, not as crisis response (ENEL)	ANRE: announce in time reassessment of tariffs and debate
Monitoring markets and licensing					ANRE: clarify and enforce regulations	ANRE: refocus its activity on markets, not tariffs
Enforceability of decisions					ANRE: better sanctions, do not replace with change in approved tariffs	ANRE: Enforcement code with full procedures
Transparent criteria for licensing/withdrawal					ANRE: start work to streamline Enforcement guidelines	ANRE: Enforcement guidelines
Consumer protection, management of complaints against industry					ANRE: respond to complaints with clear justifications, enforce sanctions on suppliers in breach	ANRE: Definition of vulnerable consumers; consumer rights

*	Achievable target
	Unsatisfactory
	Moderately satisfactory
	Good
	Best practice
	N/A or no evidence

Explanations for changes in scores between 2004 and 2009 (full explanations in Detailed Assessment):

- 1. Independence:** ANRE lost budgetary autonomy and was subordinated to GSG; presidents were changed mid-term despite the provisions of the laws. There were increased political pressures on prices before elections and on silent approval of the two integrated companies (without a published impact assessment of the new challenges to regulate a market with two dominant companies).
- 2. Accountability:** The quality of reporting has decreased, currently the annual reports do not provide enough details on the performance of the regulator. Strong negative image in the media in recent years. Conduct Code prepared in 2004-2005 abandoned.
- 3. Transparency:** Poorer annual reports on website, less information on regulatory performance, less connection between regulatory activities and broad objectives.
- 4. Predictability:** Consistency of regulation was enforced by external conditionality and PRG project of the World Bank (expired in 2009); discussions in 2010 to amend tariffs on distribution in the middle of the regulatory period as response to ENEL debate.
- 5. Tariffs:** Methodologies were set in place in 2004, before the end of the negotiations on Chapter 14 Energy with the EU for Romania's accession. Agreements reached then (to phase out social tariffs by 2007, to reach import parity for domestic gas prices) were not complied with. Tariffs allow cross-subsidization despite the explicit interdiction in the energy laws in 2007.
- 6. Monitoring markets and licensing:** evidence Romania is not in compliance with consumer protection guidelines, breach of ANRE's own orders. ANRE has not been able to enforce the regulations agreed upon in the privatization contract with ENEL.

DETAILED ASSESSMENT OF ANRE

PART I. REGULATORY GOVERNANCE

In this part we focused on the key aspects of a regulator's governance: independence, accountability, transparency and predictability. A regulator must be free from interference from government or regulated industry, accountable to consumers, investors and the general public, its activities need to be transparent to a large range of stakeholders, and regulatory framework must be predictable and credible.

The main findings and recommendations of our analysis are that serious governance improvements are needed:

1. ANRE needs to recover its independence from the Executive, which it has lost in the past 5 years (first in practice, recently also in law). In the current conditions, ANRE is in breach of EU Directives and does not meet the requirements of the Third Energy Package, which will trigger an infringement in 2011 if corrective actions are not undertaken immediately
2. To reinstate the credibility of ANRE, the regulator must respond adequately to media accusations of nepotism and relationships with regulated industry, by firm actions. This requires the preparation and effective enforcement of ethics rules for its management and key staff, and the publication of ethics monitoring, to mitigate the agency's negative public perception in recent years. Additionally, the regulator should react timely to the market needs (new regulation or updates requested by Opcom, Transelectrica etc) and EU regulations, including Romania's commitments
3. A serious threat to both regulatory independence and quality is the loss of key, competent staff because of salary cuts and politicization of top positions
4. ANRE must report adequately on its performance and use of resources / powers, to consumers, regulated industry and citizens. It must implement adequate internal controls to mitigate fiduciary risks and have an effective external audit with published results

1. Regulatory independence:

1.1. Laws used to be fairly good, but not fully applied; recent laws formalize the bad practices from before

1.1.1. In law...

The role and powers of ANRE are defined in several pieces of legislation³. The main legal framework (Energy Law 13/2007, Gas Law 351/2004 and their subsequent amendments before 2009) is largely in line with good international practices and EU Directives. It sets many of the prerequisites for a regulator that is free from both political and industry pressures. A series of amendments in 2007 to the main law have actually improved the agency's **independence from political pressures**, e.g. by eliminating the Ministry of Economy's role in nominating the president, vicepresidents, regulatory board and Consultative Council. The number of vicepresidents also increased from 1 to 3 and of the other members of the regulatory committee from 3 to 7, which matches the new responsibilities of ANRE (resulting from the merger of electricity and gas regulators).

According to the legislation before 2009, the president, vicepresidents and the other members of the regulatory committee have a fixed term mandate (there is no similar requirement for the Consultative Council, however). The members are appointed for 5 years, and cannot be revoked unless they decease, resign, their mandate expires, are condemned for criminal activities, become incompatible or fail to do their tasks. Before 2009, the agency had own revenues from license fees and was de jure an autonomous body (as we see below, the practice was however different).

But new amendments to the law in 2009-2010 are a new and serious threat to the agency's independence even in law. Following some scandals in the media regarding the high salaries in ANRE and other agencies in 2008-2009⁴, and in an attempt to rationalize budget wages, the Government issued a Law (**329/2009**) by which several agencies were streamlined and transferred under the General Secretariat of the Government. The agencies in the Law, including ANRE, are not allowed to have own revenues, such as from license fees. The revenues are collected as general budget revenues, and ANRE receives financing from the budget expenditures. Even more, ANRE currently does not have own budget, but is included in the budget of the General Secretariat of the Government (GSG).

The Government Decision **1428/2009** that regulates the new functioning of ANRE reiterates that ANRE will no longer have own revenues (**no budgetary**

³ Law 13/2007 (electricity) and Law 351/2004 (gas), amended by Govt Emergency Ordinance 33/2007, Emergency Ordinance 172/2008, Emergency Ordinance 1/2010, Government Decision 1428/2009, Emergency Ordinance 43/2010, Govt Decision 410/2007 (revoked)

⁴ For example, in late 2008 there was a huge scandal related to salaries in ANRE alone:
<http://www.hotnews.ro/stiri-esential-4796745-secretarele-soferii-anre-salarii-3-700-lei-lunar-prime-sarbatori-3-000-lei.htm>

independence) and specifies that the agency is coordinated by the Deputy Prime Minister. It mentions fixed term appointments of 5 years for president and vicepresidents, **but does not limit the situations in which the leadership can be removed**, mentioning only that leadership can be changed by the PM. Vicepresidents have now a **political rank** (state secretary, meaning deputy minister). There is **no fixed term appointment for the regulatory committee**, unlike in the previous legislation. The Agency was merged with another agency for energy efficiency – a merger that makes little sense, since the latter had nothing to do with regulation, but with managing some programs on energy efficiency.

There is some (rather faint) hope that some of these new legal provisions will be reversed, or at least so the PM promises to the EC. The European Commission has issued in mid June a very tough reaction to the Government Decision and practically threatens Romanian authorities with an infringement unless ANRE regains its statutory independence (see Box). While the Government has assured the EC in writing that ANRE would regain legal independence, in July the president of ANRE was changed again, “swapping” positions with one of the vicepresidents. In July, a commission organized by DEA and comprising ANRE, Ministry of Finance, Ministry of Economy and General Secretariat of the Government met to prepare an Emergency Ordinance that would have subordinated ANRE to the PM, given ANRE back its own revenues, allowed ANRE autonomy in spending as main credit ordinator and the budget of ANRE to be approved by Government Decision. However, the Minister of Finance insists that ANRE's budget be an annex to GSG budget, and GSG to remain main credit ordinator for ANRE. GSG opposes the idea, arguing it cannot continue to be main credit ordinator without being able to control its own budget. Regarding the payment of ANRE's staff and the applicability of Law 330/2009 (Unitary Pay Law), the decision would have to be made by the Government. No other changes had been operated at the time of this report, to bring ANRE in line with the EC's recommendations.

Box 1: Letter from the European Commission

The letter responds to a complaint regarding the reorganization of ANRE and concerns the legal changes that affect the statutory independence of ANRE. It focuses on the following issues:

- ANRE does not have own budget any more, its budget is managed by the GSG
- staff of ANRE was reclassified as general budget personnel and will be paid under the newly enacted Unitary Pay Law – which means a cut of 50% of wages expenditures; while some agencies were exempted from the Unitary Pay Law, ANRE was not among them; specific concerns are raised about best staff leaving the Agency
- the EC is worried also about the frequent changes in ANRE's presidents
- overall ANRE will not be prepared for the implementation of EU's Third Energy Package. It fails to meet the requirements of the old Directives 2003/54/EC and 2003/55/EC, which requires national regulators to be “wholly independent of the interests of electricity and gas industries” and able to carry out their tasks efficiently and expeditiously. The new Directives in the Third Energy Package, applicable from March 2011, are even stricter on the independence of regulators. They require regulators to be “legally distinct and functionally independent” and capable to make “autonomous decisions independently from any political body”, while having “separate budget allocations, autonomy in the implementation of the allocated budget, and adequate financial and human resources to carry out its duties”. The EC threatens directly with possible infringement.
- ANRE used to be a good regulator before and after accession and EU spent money for its capacity improvements, but Government measures undermine the Agency
- The letter requests a formal position from the Government within 3 weeks on whether ANRE would be able to meet its obligations under the new Directives, and on the steps that the Government would make to bring ANRE in line with its EU obligations.

But even if the Government Decision 1428/2009 were cancelled, there are several problems affecting independence that arise from the previous legislative framework.

1. PM has the final decision in changing management. In the initial laws, the Minister of Economy was nominating the leadership, and the Prime Minister approved them. After changes in 2007, the president of ANRE was submitting the nominations, but the PM continued to make the final decision. This is not a good practice as it leads to a potential conflict of interest (e.g., the PM has the interest to support profitability of state owned assets).

Box 2: How to ensure regulatory independence

In theory, there are two legal options to ensure the regulator's independence from political interference:

- best practice: the regulator reports yearly to the Parliament on its activity. The Parliament approves or rejects the report; leadership of the regulator is dismissed if the report is rejected. This is applied for other regulatory bodies, such as CNVM (the Romanian SEC).
- acceptable practice: the regulator reports yearly to the Cabinet of Ministers, leadership can be changed if the report is rejected.

In the second case, the regulator is accountable to the Executive. A part of the Executive has interest in the energy sector (e.g. state owned energy companies, under Ministry of Economy). However, this option is acceptable provided the agency reports to the entire Cabinet, and not only to one person (PM, deputy PM etc.). By having a vote in the Cabinet on the report, the interests of the Minister of Economy (the shareholder of state energy companies) and of the Prime Minister (who appoints Minister of Economy and is overall responsible for the profitability of state owned assets, including energy companies) are dissipated through the larger vote of all members of the Cabinet. It is not advisable to have the final decision on the management and assessment of performance in the hands of one person, the Prime Minister or deputy Prime Minister.

2. **“Separation of powers”**. A problem is also the fact that the **members of the regulatory committee consist of Directors of various departments in the agency:** electricity market and tariffs, licensing, gas market and tariffs, energy efficiency, external relations, control and consumer protection, renewables and co-generation. This situation could cause in practice several problems, and potential conflicts of interest:

2.1. **Those who propose regulations also approve them.** It would be advisable for directors to propose regulations that are approved by a regulatory committee independent from the departments in ANRE. This would ensure that regulations are double-checked independently.

2.2. **“Collegial protection”**. Since members are Directors from different departments, there is a natural temptation of the regulatory committee members to “negotiate” regulations (or, put in other words, “I vote your proposal, if you vote mine”). The temptation to do so is greater considering the different backgrounds of the committee members: for example, it is unclear to what extent a Director on the gas sector could judge the quality of a regulation in electricity. It is very likely the members simply rely on the fact that each director knows his sector and how to regulate it, which could turn the approval process into a mere formality.

An immediate solution to this conflict of interest problem (before the amendment of legislation and change in structure of the regulatory committee and consultative council) would be for **ANRE's management to decide never to contradict regulations as discussed by the consultative council.**

1.1.2. And practice...

The introduction of the new legislation actually formalizes some of the problems that were in the system even before.

a. **Frequent changes in management.** Despite the restrictive situations in law under which the management could be removed, in practice the management of ANRE was

changed in a non-transparent manner, mid-term, and without clear explanations on the reasons why the change was necessary, which indicates the de facto politicization of the leadership of ANRE. **Between 2005 and 2010, ANRE had 5 (five) different presidents.** The changes of VPs and other members of the regulatory committee were also frequent.

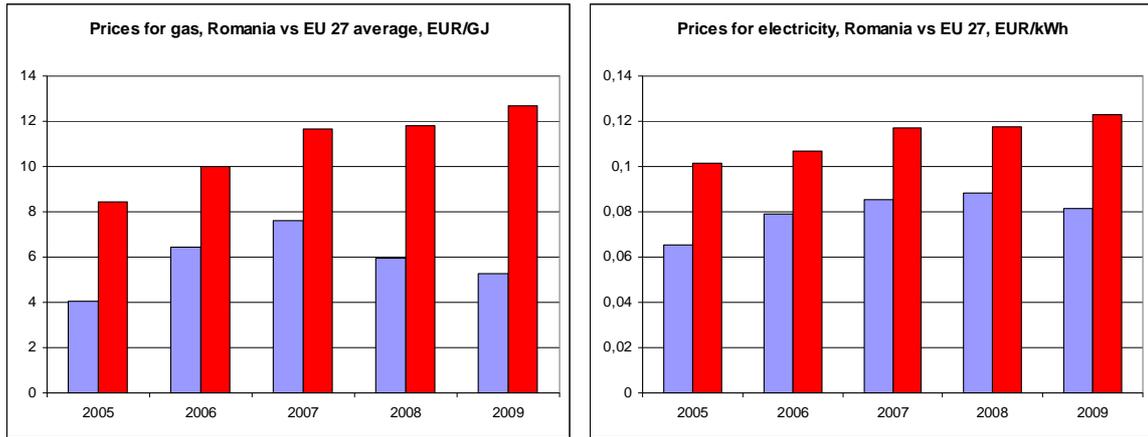
The politicization of the leadership is enhanced by the fact that there are **no clear criteria for the selection of the members of the management or regulatory committee, nor for the consultative council.** The laws do not specify a minimum set of criteria of competence, such as number of years of experience in the energy sector or in regulation, which leaves room for discretion in the appointments. Many of the previous presidents' and vicepresidents' background consisted mainly of political backing from the parties in power (see Box 3).

Box 3: Leadership is politicized

The technical nature of energy regulation would require professional qualifications at the top, and this is the reason why management must be appointed fixed-term with clear, limited criteria for mid-term removal. However, ANRE's presidents and vicepresidents since 2005 have leaned on political support rather than on technical qualifications. Thus, one vicepresident even remained political member of a local city council while VP in ANRE. Others have had political positions before or after their position in ANRE, as political appointees in sectors not connected to energy. One of ANRE's presidents had formerly been a minister of environment and then a deputy minister of agriculture; another former president, with no background on energy or regulation before his appointment as president of gas and then energy regulator, became afterwards deputy in Parliament and his family consists of career politicians, at both central and local levels, etc. Leaders of ANRE in past 5 years have been promoted by the parties in power (PSD, PNL, UDMR, PDL, PRM), political affiliation being more important than qualifications for the job. The current president of ANRE, a former car dealer, also does not have an energy background except several months during which he has served as a vicepresident of ANRE. This could explain why CVs of top management cannot be found on ANRE's website.

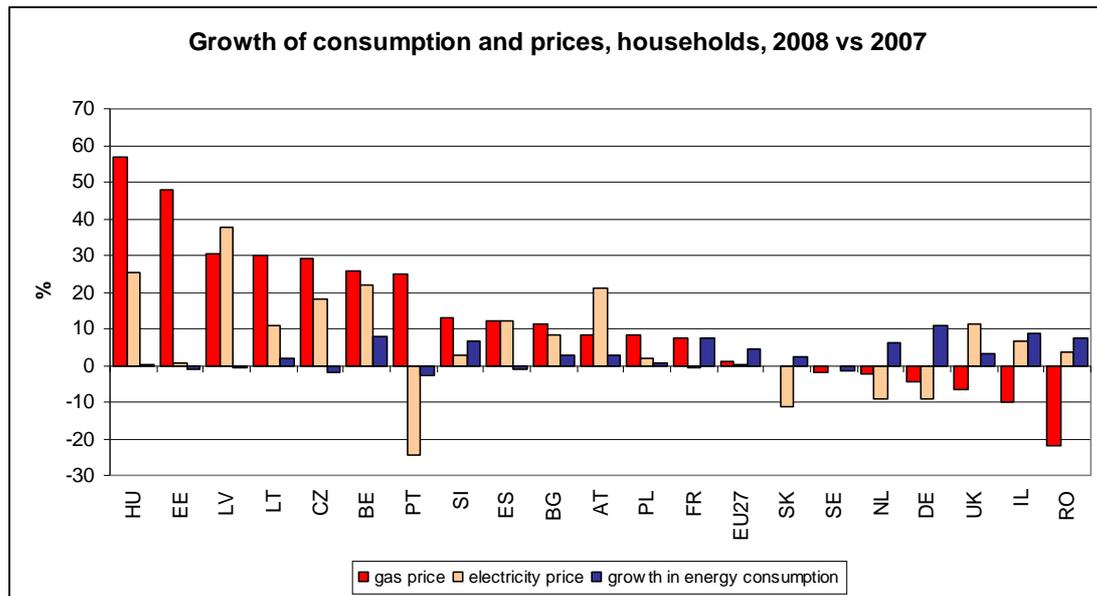
As an immediate effect, there is evidence of **at least informal political pressures** on ANRE's decisions, if we look at prices for the regulated customers. During 2009, but also before, the Prime Minister and the Minister of Economy issued statements that "prices would not be increased during the crisis" for gas and electricity. This is in effect an informal pressure on the regulator to keep prices in line with "political directives" (see Figures 1 and 2).

Figure 1. Price evolution, gas and electricity, Romania vs EU 27



Source: Eurostat. Electricity and gas prices for medium size households were kept low in 2008-2009 (electoral years), despite Romania's commitment to continue market liberalization which puts upward pressures on prices. Keeping prices low for households was justified "by the crisis", in statements of Minister of Economy, PM and the president of ANRE at the time. This had little to do with the economic reality: in 2009, residential electricity consumption grew by 8% and gas consumption by about 5%!

Figure 2:



Political influence on prices for households. In 2008, an electoral year, despite the growth of household energy consumption, prices dropped substantially from an already low level in the EU; this happens while at the same time domestic gas prices are kept well below import parity. Source: Eurostat, 2010.

Also, the Ministry of Economy is preparing a major restructuring in the energy sector that would have important implications on the regulation. Namely, the Ministry wants to consolidate the energy (electricity and mining) sectors in two large integrated companies, which would become monopolies in various segments of the electricity market. Thus, one of them contains the companies that predominantly sell

electricity in long-term contracts in the power exchange OPCOM, whereas the other concentrates almost the entire supply on the balancing and ancillary services markets (at least until an additional hydro unit under rehabilitation is finalized).

Despite the obvious implications for energy regulation, as regards market functionality particularly, **ANRE has not issued publicly any official position with solid arguments for or against the measure.** While the Ministry is not required by law to obtain an endorsement from ANRE to go ahead with the restructuring, ANRE would have to regulate a totally different sector and its opinion should be crucial in the decision to undertake or abandon such restructuring ideas. The Agency should publish a detailed impact assessment of the restructuring on the challenges for regulation; in our opinion, that would be a strong test of actual independence. The report could be for or against the restructuring, but must contain strong arguments for the position for which ANRE assumes responsibility. Otherwise, ANRE's *silenzio stampa* fuels suspicions that it is pressured by politicians in the Government / Ministry of Economy.

1.2. Independence from regulated industry

In this matter there are several issues of concern.

1.2.1. Holding shares in regulated industry: some members of the regulatory committee (and the same time directors on the sector regulation) own shares in the companies they are supposed to regulate (see Box 4). While the value of these shares is not very large, forbidding regulators to own shares in regulated industry should be common sense and must be part of a clear set of rules (legal or institutionalized practice, such as internal ethics rules).

1.2.2. Hiring relatives of managers of companies from the regulated industry. This is another practice that should be explicitly forbidden, to avoid both influence of the regulated industry on the regulation and the risk that the regulator loses its credibility. However, there is anecdotal evidence that this occurs in practice (Box 4).

Box 4: Independence from regulated industry: what NOT to do

According to his statement of wealth published on ANRE's website in 2009, the director for access to networks of gas and electricity and member of the regulatory committee owns 38,000 shares (8778 RON) in Petrom, a company that accounts for half of the domestic gas production, and 269 shares in GDF (7069 EUR), a company that owns half of the distribution and supply market on gas in Romania. The director on energy efficiency and also member of the regulatory committee owns shares in Transgaz, gas transmission network (69 shares, 11972 RON) and Transelectrica, the electricity transmission grid, 250 shares (3375 RON).

A scandal in 2009 in the media revealed an arrangement between the president of ANRE at that time and the general manager of Nuclearelectrica, a large state-owned nuclear power plant. The manager of Nuclearelectrica promised to hire the daughter of the president of ANRE in the shareholder's assembly of Energonuclear (a joint venture between Nuclearelectrica and private companies to build 2 reactors), in exchange for his own daughter to be promoted director for communication in ANRE. Following the scandal, both daughters renounced their controversial positions.

3. **Staff and resources must be adequate.** The selection and training of staff seems to be a problem in ANRE (also highlighted in the EC letter, which signals the high turnover of qualified staff). This is in line with the public accusations of politicization (removal and appointment of people on political criteria, even at lower, technical management level) and with the cut of salaries. In 2009-2010, following the application of the Unitary Pay Law for public sector employees (affecting ANRE as well), and an additional 25% pay cut across the board in July 2010 for all budget-paid employees, top salaries have decreased by about **70%**. Qualified people are finding jobs in the private sector or even in public companies (Transelectrica). Training is not given proper attention.

However, the budget of ANRE had increased substantially in recent years (doubled over 5 years, between 2004-2009). About 90% of the total budget represented direct staff costs. **It should be explored if other perks (training, educational trips, in a coherent training strategy) could be effective in retaining qualified and motivated staff.**

2. Accountability:

As explained above, a regulator must be accountable for its decisions to a political body, Parliament or entire Executive. It must also be responsible to a constituency of stakeholders (consumers, investors, citizens) to which it has to report on its activity, in order to justify the use of resources and powers entrusted to the regulator.

2.1. **Reporting obligation.** To justify whether the regulator has acted in accordance to its mandate, the regulator must prepare an annual report of activity, available to the stakeholders in due time. ANRE prepares such reports, which are published on the website.

The annual report however is **not formally approved or rejected by the Executive**, nor is the dismissal of management related to the agency's results in practice, as we saw before. The fact that there is no such mechanism for approval or rejection means no political check on whether the regulatory quality in the past year rose to expectations.

As a consequence of the fact that reports are not given their proper importance, there is a **marked deterioration in the quality of information contained in the annual reports of ANRE since 2004**. While at that time they still missed some critical items to be a best practice (see Box 5 for a model), initial reports focused more on the regulatory activity and performance of ANRE and provided a clearer image on what the regulator does and what it should do. For example, the 2004 report contained:

- program of regulations for the past year, proposed vs achieved
- clear performance indicators
- monitoring of ANRE's transparency
- correlation between existing programs and objectives of the agency

- presentation in simple terms of the regulatory activities (licensing, market regulations, market monitoring, technical regulations, prices and tariffs, together with justifications for each measure)
- consumer protection, including complaints and management, and average time to solve each type of complaint
- decisions contested in Courts and how they were solved by the judicial system
- international cooperation programs
- next year's regulatory program on broad headings
- market monitoring results in annexes, in graphs
- budget (only execution)

By comparison, the 2009 report is mainly an account of how electricity and gas markets work in Romania and **offers precious little details on the activity of the regulator itself**. While the information contained in the reports is important and useful, it mainly repeats/duplicates the monthly market monitoring reports, the content of some of the regulations and laws etc. The report lists the Orders issued by ANRE and their content in brief, but without providing qualitative explanations, such as how these fit into an overall program contributing to the regulator's broad objectives. It continues to present rather detailed information on consumer protection (petitions structured on types of petition), but this time without offering information on how these were solved and average response times. It has some details on the control activity (types of control, sanctions), but without linking the controls with the reasons behind the control program (consumer complaints? Other?). The report also presents the execution of the budget. The report provides details about types of contestations in courts, but not the results (final court decision).

The following items would be crucial to determine whether the management can stay in office or should be removed. **Next reports must contain, at a minimum:**

- Details on how resources are used:
 - o Complete financial statements, including balance sheet, cash flow, notes and a breakdown of revenues, current vs previous year, e.g. to understand how much ANRE gained from license fees, its (previously) main source of revenue. Financial statements must be audited externally. A brief description of proposed measures to rationalize resources could improve ANRE's chances to regain its budgetary independence;
 - o Staffing: some details on the number of staff, technical skills available, and training, staff attraction and retention policies to fill in the capacity gaps. As signaled by the EC letter, this is a major capacity constraint in ANRE.
- The elements existing in 2004 reports that are not available in recent reports, on performance, regulatory program on broad items, match between resources and objectives

- Brief impact assessments of past regulations, which **must** be available to justify the frequent amendments of Orders in the next year (see Predictability chapter)

Introducing the above information is a **quick win**, as it requires little additional work from what ANRE does currently. Moreover, reporting on activities is not only a formal requirement, but also an opportunity to promote the Agency and improve its credibility to the stakeholders. The agency can better control its public (not so good) image by being proactive and focusing its reports on achievements.

Box 5: Best practice reporting – the UK regulator OFGEM

The UK regulator issues a very brief annual report containing information on:

- key achievements in the year based on clear stated objectives (controls, consumer protection measures, investigations and enforcement, measures to control market abuse etc.; reviews of regulatory regime, such as transmission network tariffs and access; social tariffs and dealing with poor consumer protection)
- rationalization of own resources – finding ways to reduce costs, staffing, optimize resources, staff development; budget compared to previous year, but also a complete simplified set of financial statements (balance sheet, cash flow, recognized gains and losses)
- actual vs planned performance, including meeting deadlines for the work program
- impact assessments on past regulations
- assessments of former regulations and feedback to improve them
- better regulation and simplification of procedures, so that regulations are kept to a minimum and do not overburden the regulated industry.

2.2. Accountability to regulated industry, consumers and the general public. As any public organization, ANRE falls under the provisions of the Freedom of Information Act (Law 544/2001) and is required to provide within 10 days (30 days with explanations for delays) information of public interest, such as budgets, justification for regulations, including justification for setting the regulated prices, contracts using public money etc.

ANRE publishes on its website a very useful guide on how to request public information, who is responsible for FOIA requests, a program of public audiences with the president and 3 vicepresidents, and a list of documents that can be requested on FOIA (see also Transparency chapter).

Indeed, ANRE responds to requests, but the quality of the responses is not always adequate (see Box 6).

Box 6: Request to reexamine an Order issued by ANRE on gas sector

Mr. Mihail Biolan has sent an official request to ANRE to reexamine an Order (82/2008, on gas prices for regulated consumers, GDF - Distrigaz Sud). The main reasons for the reexamination request are the conflict with:

- previous legislation issued by ANRE (ANRGN Decision 1078/2003) and Law 296/2004 (abusive clauses)
- EU Gas Directive 55 (on consumer protection)

Among several items in conflict: end-user prices approved in Order 82 do not follow binomial formula, as specified by ANRE's Decision 1078. For the second regulatory period the approved rate of energy efficiency improvement is negative, -6.36%; as per Decision 1078, efficiency improvements can be transferred to the consumer, in our case the losses (This is contrary to the idea that the second regulatory period should provide incentives for efficiency improvements). ANRE's response to this request was simply "ANRE considers the Order legal and justified and cannot approve the request for reexamination".

An accountable regulator must respond with arguments, particularly when its position is contrary to that of the plaintiff. In this case, ANRE should have explained how the Order avoids the conflicts with previous legislation (or indeed reexamine Order 82 and improve it).

2.3. Means of redress. The Orders and decisions made by ANRE can be in principle contested in courts, but in practice contestations have not led to substantial results, such as overhaul revisions of regulations. So far, the contestations are mostly related to particular items such as withdrawal of licenses, sanctions, but also tariffs for networks for gas and electricity distribution, or complaints from consumers⁵.

To monitor the results of high profile lawsuits, we have looked at the website of the Romanian High Court of Cassation and Justice⁶ (the equivalent of Supreme Court, or the instance of last resort in our case). We chose this Court as its decisions are final. Between 2005 and 2010 ANRE had 14 final decisions in the High Court. These consisted of:

- 8 contestations of regulations (ANRE won 6, lost 1 with another public institution – the Ministry of Transport, and one has to be judged again),
- one for material damages (ANRE lost),
- one labor conflict,
- 3 suspensions of administrative decisions (of which ANRE won 2), and
- one contestation of a Government Decision to which ANRE was part (again, ANRE won).

Among the lawsuits to cancel regulations, 4 which ANRE won were with very large private companies (EON, ENEL, CEZ).

Per discussions with our panel of experts, the large proportion of lawsuits won by ANRE could be also because the courts tend to decide in favor of the public institution in a conflict between a public body and a private entity, particularly when the lawsuit concerns canceling regulations. The number of final decisions monitored

⁵ http://www.antena3.ro/economic/news/eon-gaz-distributie-da-in-judecata-anre-pentru-ca-a-redus-tariful-la-gazele-naturale_74563.html

http://www.cronicavip.ro/cronicavip/article.php?article_id=52887

<http://www.scj.ro/SCA%20rezumate%202008/SCA%20r%203851%202008.htm>

⁶ www.scj.ro

is not large enough to lead to the conclusion that this indeed systematic, but our findings do not rule out this hypothesis.

Lawsuits (an expensive undertaking anywhere) generally do not cover issues on overall regulation principles or methodologies, but narrower items that affect individual interests. But this does not mean that principles behind methodologies used by ANRE are necessarily correct or good practice. On the contrary, **for two major regulatory items (liberalization of gas and electricity markets, stalled by price regulation distortions) Romania has received an infringement from the EC in June 2009**. We explain in the Regulatory substance part some of the possible causes behind the failure to liberalize gas and electricity markets.

Another possible explanation for the relatively small number of contestations could be a preference for individual or side arrangements. Companies prefer to “bargain” directly for their individual interest with a public institution (that does not necessarily mean corruption, but also informal pressures by means like public statements). For example, in March 2010 EON announced it would have to lay off 23% of its employees if the gas regulator does not approve an increase in the prices for its regulated consumers by 17%⁷. In other cases, the regulator might issue bad regulations that work both ways (e.g., the company loses on one regulation, but wins on another more than it has lost on the first); or a regulated company is not in compliance with another regulation and decides not to sue and be at risk to be exposed. We have no direct evidence for this in the energy sector. However, as explained in the Regulatory substance section, there is evidence of price regulation distortions that cause electricity suppliers to lose money on regulated consumers. Unless they manage to make a better gain from another regulation, there is no explanation why they wouldn't complain, at least publicly, that they are required to subsidize losses from the captive market.

While the judicial complaint is more expensive and costly, in theory, there is a possibility to complain to an administrative body – the Ombudsman. However, the Romanian Ombudsman, which deals with complaints against public institutions and seeks to mediate between the two parties, does not have a reputation to be very effective and, of course, it is not specialized. Complaints against the regulator are therefore addressed directly to Courts.

2.4. Clarity of regulatory roles. Accountability is clear also when the institutional framework is clear on who does what. There are several regulatory bodies that regulate items related to energy markets or consumers, e.g. Competition Council, Consumer Protection, the regulator for local utilities ANRSC etc. Their responsibilities are clear in law, however there are some items for which it is necessary to have collaboration Protocols, to undertake joint controls or reviews and benefit from each other's expertise.

⁷ <http://www.citynews.ro/maramures/economic-25/disponibilizari-e-on-ar-putea-renunta-la-23-din-salariati-77101/>

For example, the Competition Council can look at market abuses generally when it is notified. Because of technical constraints that may affect competition, ANRE has the technical knowledge to monitor the markets on electricity and gas, and its departments for market monitoring calculate indicators of concentration. It may signal possible abuses to the Competition Council, which then enforces the competition law. There has been a Protocol signed in 2005 between the Competition Council and ANRE to facilitate a collaboration and speed up enforcement of market regulations, but apparently the Protocol has simply fallen into oblivion. Such a protocol could contain ways of cooperation that would improve market conditions, e.g. a review of regulatory framework to propose reforms to promote competition or increase quality of service.

A collaboration protocol would have been particularly useful in the current issue on the power sector restructuring in two integrated companies, which the Government has approved in principle in mid 2009. The legislation requires a formal endorsement from the Competition Council before the companies are set up, but the opinion of ANRE is not required officially. A Protocol on monitoring and enforcement of competition rules in energy markets jointly by ANRE and Competition Council would have ensured that the move does not go ahead without a formal opinion of ANRE as well.

Regarding an effective consumer protection, the situation is much worse, and there is no collaboration protocol with the Consumer Protection agency (also see Regulatory substance section).

2.5. Proper accountability on use of resources. This means the regulator must prepare and publish financial statements, cash flows, revenues and expenditures, balance sheets with inventory of assets, and be checked by an external auditor. The legislation however is also **weak in terms of fiduciary controls.**

ANRE publishes only a balance of revenues and expenditures in the Annual Report, a list of investments and another on contracts concluded on its website. However, it does not disclose assets or the results of an independent audit. The Court of Accounts (Romanian public institution auditor) should verify the accounts of the agency, but we understand it has never done so except one case in which it has responded to a call for investigation from within ANRE.

Unlike Ofgem, for example, which makes all the financial information publicly available on website and presents means to reduce expenditure, ANRE does not publish such information or seek ways to improve efficiency of spending. There have been public concerns on how ANRE manages its financial resources (mainly, scandals about high wages in ANRE mentioned before). The media scandals on this topic have been actually one of the political reasons why ANRE was transferred under the GSG and its budget became revenue to the state budget. The Government felt it had more control on the financial resources if ANRE became financed from the state budget than if it remained autonomous with own revenues.

Box 7: Missing budgetary controls, but limited financial autonomy and flexibility even before 2009

According to the legislation in place in 2008¹, the budget of revenues and expenditures was proposed by ANRE, by July 15, for the following year, to the Minister of Finance. The budget was (formally) approved by two ministers (labor, finance) and ANRE's management, by a common Order. The budget approval for 2008 was however published in April 2008, well after the beginning of the year. According to the provisions of the legislation, before the approval ANRE could spend each month 1/12 from the budget of previous year. To avoid risks of overspending before they could be certain on the budget for the year, ANRE was paying only salaries in the first quarter, and any investments were left for the following months of the year. Savings could be reallocated without an additional approval like for the initial budget.

While ANRE is reporting to the Ministry of Finance quarterly on budget execution (and financial statements, including balance sheet, cash flow etc.), the execution is not actually checked by MOPF. There is also no statutory obligation for the financial statements to be externally audited, at least by the Court of Accounts. Regarding the internal audit, ANRE has a department in the organization chart, but we understand it has no filled positions. Before 2006 it had only one person, instead of a recommended 3 (uneven number, but more than one, for independent checking).

It would have made more sense to have a more streamlined budget approval process, to ensure timely approval of budgets and predictability, but a monitoring of execution, strong internal audit and independent verification by an external auditor, Court of Accounts or a credible auditor (Big 4). ANRE should also be required to publish all financial statements and audits on its website. To reduce the risk of waste of public funds and minimize other fiduciary risks, ANRE could have been required to do also a performance audit and an audit of key processes (e.g. licensing activity/invoicing).

1. Methodological Norms of Ministry of Finance. Ordinance 1/2007

Table 1: Budgets and staff doubled between 2004 and 2009, exceeding even Western regulators

	2004	ANRE 2009	OFGEM (UK) 2009	CRE (FR) 2009
Staff	86 (ANRE) + 112 (ANRGN) = 198 6,92 mn RON (ANRE) + 8,34 mn	262 (ANRE) + 65 (ARCE) = 327	310	125
Budget (expenses)	RON (ANRGN) = 15,26 mn RON	31,72 mn RON	200 mn RON (40 mn GBP)	80 mn RON (19.9 mn EUR)
Of which employee costs			87,50%	48%
				60%

In the regulator's case, there are several **areas of risk**, for both governance and management of assets. The main "business" of ANRE is licensing; given the particular interests in the energy sector, this could be a major risk area for possible corruption (or at least suspicions that would affect the regulator's credibility and must be proactively mitigated).

Box 8: Media scandal on licensing a bankrupt supplier¹

The liberalization of the electricity market led to the emergence of private suppliers, which buy electricity from producers on the wholesale market and sell to consumers on the retail market. In 2005, as the market liberalization had just started, a company obtained a supply license and bought electricity from Hidroelectrica, a state-owned electricity producer, to sell to a steel producing plant (ArcelorMittal – Sidex Galati). The value of the contract was 400 mn RON (100 mn EUR), as the supplier was covering half of the electricity consumption of the steel company. There were two major issues with the deal. First, the supplier obtained electricity from a state owned company without a tender (this is however not under the control of ANRE). Second, and under the control of ANRE, according to a media investigation the supplier was at then an **officially bankrupt company, under judicial liquidation, with a fictitious headquarters**. Under these circumstances, the supply license could not normally be granted. Having a good control system on the licensing activity is crucial to ensure non-discrimination among suppliers, but also to provide credibility to the regulator that it would never engage in illegal practices.

1. <http://www.hotnews.ro/stiri-arhiva-1241722-combinatul-mittal-steel-sidex-galati-cumpara-curent-mii-miliarde-srl-falimentar-sediu-fictiv.htm>

Having an independent, external audit is critical, to ensure both good use of resources and external credibility. An audit would look not only at financial matters, but overall at business processes and controls (cash management, invoicing, licensing, separation of invoicing from cash collections for double checking etc.). In addition, a good financial and processes audit could go as far as suggesting possible improvements in the organizational chart looking at the match between departments and functions of the regulatory agency.

Box 9: What questions would an auditor ask on the licensing process?

1. who prints the licenses? If there are no effective controls, there is a potential risk, e.g. unauthorized issuing of licenses or with a previous date. Recommended: licenses must be printed at an external official institution, with serial numbers, to have an external control of the exact number and dates when the licenses were issued. Second best option: if issued in house, clear records of all licenses must be kept, (duplicate border with serial number, stored safely, available to auditor upon request).
2. are invoicing and licensing separated? This allows cross-checking of the activity of people employed in these departments and an additional safeguard on the cash and licenses. (The directions that issue the licenses on electricity and gas are located under the departments for access to networks and authorizations in the electricity and gas, respectively. Per our understanding, the chief accountant prepares the invoices for the licenses.)
3. are invoicing, cash collection and accounting separate? This would ensure checking of invoices with other accounts, such as money receipts.
4. is the accounting system not allowing changes to be made retroactively (automatic controls)? This would ensure completeness of records on revenues, invoices, and cash.

Etc.

2.6. Performance auditing (examining the quality of outputs compared to the inputs) is also essential to identify whether the regulator's resources have been adequately used to meet the organization's objectives; this must be the **only** criterion for the mid-term removal of management. Examining previous ANRE reports, the agency had in the past some capacity to self-assess and justify to the public its performance and achievements. **This practice must be renewed immediately.** In time,

performance auditing must go well beyond the 2004 reporting, and ANRE should learn and compare itself with other EU regulators.

2.7. Ethics code. Having an ethics code is important for a regulatory authority to enhance credibility to the stakeholders in the sector. Such a document defines what is acceptable or not in terms of actions, potential conflicts of interest, and requires transparency of interests and wealth for dignitaries to prove that key staff from the regulatory agency do not use their powers in a manner not suited to the legitimate interests of the regulated sector and consumers. Given the special responsibilities of regulatory agencies, it is highly recommended that they prepare such documents that go beyond the requirements for general public agencies. While other energy regulators in the EU do not necessarily publish such documents or internal investigations on ethics (mainly because their credibility is well established), **in the case of ANRE this is highly recommended to make public such efforts in order to improve the agency's credibility in light of recent media scandals.**

Currently, ANRE has indeed a “code of conduct”, prepared in 2005⁸, but to our understanding it remained a paper document that was never applied. ANRE has no Ethics committee to monitor staff behavior, and the agency did not publish results of possible internal investigations as result of public accusations in the media (e.g., the scandals about nepotism⁹). The Agency published several press releases in response to some of the accusations.

There are however general integrity arrangements which operate for all Romanian public institutions, such as the National Integrity Agency and the obligation to publish statements of wealth and interests, and these are quite effective. For example, the information in Box 4 on the shares owned by members of the regulatory committee is available in the documents published as required by these regulations. The National Integrity Agency (which monitors the conflicts of interest or the discrepancy between changes in wealth and legal income) has highlighted some issues in ANRE in recent years. For example, one of the presidents of ANRE was accused by the National Integrity Agency for incompatibility by being at the same time in 2010 deputy in Parliament and manager of a private company; and for being simultaneously in 2007 president of ANRE and manager at the National Uranium Company.

A problem with these general arrangements is that a regulatory agency also needs additional safeguards, such as being forbidden to own shares in regulated industry, or other rules of conduct that are not necessarily legally binding (being irrelevant for other public bodies), but their breach affects the credibility of the regulator. In addition, the National Integrity Agency was subject to a lot of political pressure, being rendered ineffective in May by the Constitutional Court, and for several months the dignitaries (management, key personnel) were not obliged to post on

⁸ <http://www.anre.ro/index.php?id=368>

⁹ For example, in 2010 the president of ANRE was accused of having hired two nephews in the agency, and a nephew of the Minister of Economy: <http://www.revista22.ro/a-href--anre-cuibusor-de-nepoti-cum-si-au-pus-videanu-si-lificiu-nepot-8268.html>

websites statements of wealth of interest. While the agency was given back its powers in August and the dignitaries will be again required to publish detailed statements of wealth and interests on website, the statements of ANRE's management were not updated since 2009 (on ANRE's website these have not been updated even after the expiry of the new legal deadline, October 1, 2010). ANRE must go beyond what the law requires and promote its own integrity in a proactive manner: **publish detailed statements even if not required, take immediate measures for those who are incompatible before the National Integrity Agency enforces its administrative decision** etc.

In addition, **ANRE must have a functioning ethics committee, with published investigations and findings**, and several actions must be explicitly forbidden in its own internal rules. Some possible items to be included should concern the main accusations appeared in public:

- to avoid conflicts of interest: interdiction to own shares in regulated industry or have close relatives in companies in the sector, interdiction to be related to management of companies involved in ANRE's procurement, interdiction to provide consultancy services to private sector companies; interdiction to hire as collaborators employees of companies from the regulated industry
- a description of gifts that could be received and from whom, in what amounts
- what happens if a criminal investigation is started on a key person (the Energy law 13/2007 specifies the management could be revoked only in case of a final court decision)
- interdiction to be employed by a company in the energy sector for a period of 2 years (e.g. not to disclose sensitive information on the competition). In exchange, proper compensation for this interdiction must be granted if the person is made redundant
- confidentiality clauses – employees must handle personal or company information with special care not to affect their interests
- rules to handle pressures, real or perceived, affecting independence (political pressures, pressures from industry) – e.g., where to report
- a professional image – certain behaviors that are inadmissible (e.g. rudeness in response to public inquiry etc.)
- proper use of agency's resources and assets
- no discretionary use of powers.

A quality assurance system would consist of enforcement and publication of results, including sanctioning of those in breach (and, possibly, rewards for good behavior). For a period of several years (at least 3-4) the **enforcement** of this code of conduct should be disclosed in ANRE's annual report, to reinforce the agency's public credibility.

2.8. Capacity to enforce its decisions and to provide a clear, consistent regulatory framework is essential for the accountability of the regulator, because it increases the credibility of the regulator in front of consumers that they are effectively protected against abuses and investors that regulation ensures level play. The total

amounts of sanctions (600 K RON in 2009) look quite small, and most cases involve relatively small penalties. In 2010, ANRE made an investigation on an electricity distribution company which it sanctioned with a 355 K fine; the other penalties for the same company affect however the predictability of distribution tariffs (see Box 18 Regulatory substance part).

Regarding level play, the media has raised suspicions that some of the regulations are discriminatory, favoring some players to the disadvantage of others (see Box 10 for an example). ANRE must respond publicly to such allegations, with arguments, immediately after the accusations appear in the press.

Box 10: Private company PETROM allegedly benefits better conditions than state owned company Romgaz

In 2008, a media investigation showed that PETROM is allowed to charge more than Romgaz for the gas sold to the captive consumers. According to the existing practice, domestic gas price is kept low, and the captive consumer receives a “basket” price, consisting of a weighted average of prices for domestic and import gas.

The main domestic gas producers are Romgaz and PETROM (about 45% of domestic gas production each). They are required to contribute to the basket all gas except “own technological consumption”. However, while Romgaz contributes 99% of its gas to the basket, PETROM manages to put in the basket only just above **30%** (1.8 bn m³ being exempted, of which the gas transmission operator recognizes as technological consumption only 753 mn m³ in 2007). The remaining 1.07 bn m³ is “sold” by PETROM to one of its subsidiaries, a chemical plant (which otherwise would have had to purchase at the higher, “basket” price). If PETROM had to sell the gas at “domestic” prices in the basket, in 2007 it would have gained 180 USD/1000 m³; by using the gas in chemical industry, where gas cost is 90% of total cost, it obtained the same profit as by selling the same quantity of gas at 320 USD/1000 m³.¹

1. <http://www.evz.ro/detalii/stiri/petrom-ne-arde-la-gaz-804702.html>

3. Transparency:

3.1. Transparency on rules and regulations. ANRE publishes indeed decisions and orders on the website; its Orders are also published in the Official Gazette. The orders contain some information on the reasons behind the Order.

For some major items ANRE organizes public debates and the announcement for participation is published on the website, together with the relevant documents to be discussed. The minutes of the debates are also published. However, it is not clear whether debates are organized for all major Orders. Currently on the website there are documents for public comments (Legislation → documents for discussion Natural gas and Legislation → Documents for discussion electricity), as well as announcements for public debates (2 in 2010). For those with public debates there are also minutes (one in 2010).

The sheer number of regulatory items (in the published work plan of the agency and the actual Orders and Decisions) is overwhelming. While much information is there, it is **very difficult to access** for the regular reader. A reader needs to understand in simple terms, for example, how the gas market works, what are the consumer rights

and obligations, what are the issues with competition, competition in metering services etc. As will be explained in the Regulatory substance chapter below, it is also visible from the way in which ANRE presents itself that **ANRE focuses more on legal aspects of regulation (licensing, tariffs, regulated prices) than on the promotion of a well-functioning market (analysis, investigations, deregulation, consumer protection against abuse etc.)**.

Box 11: How Ofgem publishes information on regulations:

Existing regulations are published under different headings, on different areas of regulation (e.g. Markets → Retail markets → Retail competition). Sub-pages under each heading have a short description of the different sector under Ofgem's monitoring, and what Ofgem actually does on that particular matter. The last sub-page contains also the relevant documents (analyses, reports, regulations), newest first. There is more reliance on actual market and sector analysis than on rules, decisions, orders of Ofgem (reflecting also the focus of the regulatory activity, which is less legalistic, and more policy- and vision-oriented).

This means of presentation is much more accessible, transparent and easy to search into than if all orders, decisions and reports were published in the same page. The links to broader objectives of the regulatory activity are easier to spot and one can identify promptly for which objective a regulation was introduced.

Documents under debate are available in a separate tag, Live consultations, where one can find all the documents under discussion and awaiting comments, but also older documents for which the debate is closed (including the comments received). Most of the consultations are related to impact assessments or principles of regulation, and only very few (below 5%) on regulations.

In the annual report Ofgem presents its work plan (performance vs deliverables), structured on main activities and subsectors (e.g., Competition → market monitoring, or Regulating networks effectively → Transmission)

3.2. Transparency on activity:

There is precious little information on the activity of the regulatory committee and the consultative council, though they are the main drivers of the regulator's activity and performance. For example, the only information available in a systematic way is the Regulatory program, which contains regulations to be discussed at the meetings of the regulatory committee, in a chronological order.

ANRE does not publish minutes of their meetings, and meetings of the regulatory committee are also not open to the public.

Box 12: Ofgem report

Publishing a good report is not a challenge, but an opportunity. The agency controls the messages and tone, and the impact on the public can be tremendous. For example, the report issued by Ofgem focuses on achievements vs objectives and uses buzz-words such as "leading voice in Europe", performance, simplification and better regulation, consumer first, people development, regulating effectively, progress, new, "continued to outperform our self-imposed cost regime" etc. The overall impression of the reader is that Ofgem knows what it does, who are its clients (consumers, investors, citizens) and that what it does is excellent.

We tested the actual implementation in practice of the FOIA provisions. Specifically, we sent by fax a letter asking information on items that are sensitive or simply not publicly available on the website. We requested the information by fax, e-mail and proposed that this information could also be made available on ANRE's website:

1. Personnel data (numbers of approved positions and actual staff), for ANRE overall and for several Departments, including the Internal Audit.
2. Financial information (2009 balance sheet and copy of the audit report, if any; if there was no audit in 2009 we asked them to confirm)
3. Information on how energy prices are determined for electricity captive consumers. We asked for the:
 - a. regulated quantities of energy from producers that make up the 8 “pools” of electricity;
 - b. prices generated automatically by PowerSym software run by the planning department of Transelectrica;
 - c. prices used by ANRE to see whether they are different than those generated by PowerSym (an automated system used by the TSO for setting up generation regulated prices for electricity); and
 - d. technological consumption approved for each implicit supplier. If we receive the full answers, we would check first whether prices used by ANRE are different from those generated by PowerSym. They should not be different; if they are higher it means additional gain for producers, if they are lower that could show cross-subsidy, meaning producers have to sell at a loss in the regulated pool and find some way to finance the loss by selling at higher prices on the competitive market. By checking if technological consumption is different across suppliers, that means some suppliers would benefit more favourable conditions. Technological consumption actually means the electricity the implicit suppliers (who have also distribution companies) finance higher losses on the distribution grid.
4. Information on the regulatory activity:
 - a. List of regulatory committee meetings in 2010 and minutes of meetings
 - b. List of consultative council meetings in 2010 and minutes
5. Performance indicators for ANRE’s activity: we asked ANRE to provide information on its key objectives and concrete activities undertaken in 2009 and 2010 to meet those objectives, on the format ANRE itself used to provide this information (Annual Report 2004)
6. Impact assessment / substantiation note demonstrating the need for amendments of previous legislation (Orders that modify or complete previous Orders) – to see: why were changes needed? Is it because of actual changes in the environment? Does ANRE indeed systematically reassess the impact of its own regulations?
7. CVs of ANRE’s management, regulatory committee members and consultative committee members (to see whether they are indeed qualified for the job)
8. Petitions received and how these were actually solved, in how much time, 2009-2010 (information existing in 2004 Annual Report)
9. Control activity: what companies were controlled and the main items checked. Such information existed in the 2004 Annual Report.

ANRE has responded so far that it needs more time than the usual 10 days to complete our request (they are obliged on L544 to provide the information in 30 days at most, if it has requested the extension to 30 days within the 10 days). We are awaiting the answers and will write in the next assessment (January 2011) about the response received. We also **strongly encourage ANRE to publish this data on the website.**

4. Predictability of regulatory decision-making

As explained above, the sheer number of regulatory items (in the published work plan of the agency and the actual Orders and Decisions) is overwhelming. A worrying aspect is that a large share of Orders consists of amendments to previous legislation or, even worse, amendments to amendments (e.g., 5 out of 13 Orders in Electricity in 2010). This is an indicator that the regulations are not very predictable or that flaws require amendments for correction.

In order to ensure predictability of regulations, methodologies to establish tariffs for networks (transmission, distribution) are set in regulatory periods. ANRE has received substantial consultancy on tariff setting methodologies, from both EU and the World Bank, and the existing methodologies are good practice; in addition, the World Bank has “guaranteed” for predictability on distribution regulation in electricity in a PRG program (2004-2009) to support the privatization of electricity distribution companies.

Box 13: Regulatory periods for electricity transmission and distribution

From January 2005, price-cap tariff regulation for distribution and revenue-cap tariff regulation for transmission (plus nodal tariffs) were prepared and put in force by ANRE. Revenue cap is determined ex-ante by ANRE, for a period of 5 years (except for the first regulatory period of 3 years, 2005-2007); the revenue is adjusted with inflation but the methodology is maintained in the regulatory period. Thus, the revenue cap is determined based on quality standard, quantity of electricity, changes of losses, regulated profitability rate, tariffs. In the second period, a new factor is introduced (correction factor for minimum quality, max 2% of total revenue). Distribution tariff is also based on regulatory periods (3 years then 5), the tariff being based on network operation and maintenance costs, own energy consumption, depreciation of assets etc. For the second period tariff, there are additional incentives for reduction of losses (reduction of own energy consumption of 9.5%).

Tariffs are reviewed periodically, based on inflation and other changes in the environment. However, substantial overhaul revisions should be avoided as much as possible. There is however evidence of possible substantial revisions in the future, as a means to mitigate another media scandal with the monitoring of a privatization contract for distribution (see Box 18).

ANRE has a **regulatory program**, prepared for each year. It monitors and updates the implementation of the program. However, the program consists of a list of regulatory decisions to be discussed and approved by the regulatory committee, in chronological order. It is difficult to cross-check with orders or regulations approved

because of the time lag (from the moment they are discussed in the regulatory committee, then published for transparency and comments, then finally approved). Both for transparency and predictability purposes, it is highly recommended that **ANRE publishes its work program, containing not just regulations but also other activities, such as reporting, market analysis, inputs to major strategies adopted by other parties that affect also regulation, and impact assessments.** Below a suggested format:

- a list of key objectives for next year as headings, with each regulation under a heading, to show that regulations, analyses etc are conducive to meeting one of the key objectives (e.g., effective market monitoring, or network regulation, or investigations in market segments)
- key deadlines: discussion in consultative council if the case, approval in regulatory committee, posting date for public debate, approval with changes
- initially set deadlines and actual times to identify delays and explanations for deviations.

Such a reporting format would ensure both predictability of the yearly activity of ANRE as a whole and completeness (no regulation without debate or without clear idea of what would be achieved and which objective is met). It will also **support the introduction of performance management.**

Also, there must be a formalized feedback on implementation of previous regulations, to increase predictability of regulatory framework. Amendments to Orders should be justified by an impact assessment of the existing regulation, which has proven unsatisfactory and required the change.

PART II. REGULATORY SUBSTANCE

In this part of the assessment we focused on the quality of regulation and enforcement done by ANRE. We looked at ANRE's tariff design, commercial code, monitoring and licensing, market analysis, capacity to promote competition in wholesale and retail markets, and competition in access to networks. In assessing ANRE's regulatory quality, it should also be noted that in the early 2000s ANRE was perceived as a model regulatory agency in Europe, even being used as a model for Western regulators (France, Germany).

The main conclusions of our analysis below are:

I. ANRE focuses too much on tariffs and too little on markets development and enhancement of competition. While this was acceptable in the early days of energy regulation (late '90s), Western regulators have evolved in the past decade, from tariff regulators to agencies that effectively promote competition in wholesale and retail markets, unbiased access to networks, support of renewables and regulation of environmental aspects.

Box 14: Ofgem's role 1

*"Ofgem is the regulator for the UK's gas and electricity industries. Ofgem's role is to protect and advance the interests of consumers by **promoting competition where possible, and through regulation only where necessary**. Applying this principle has resulted in great benefits for all gas and electricity customers. To build on these benefits, Ofgem's work focuses on the following areas:*

- *making gas and electricity markets work effectively*
- *regulating monopoly businesses intelligently*
- *securing Britain's gas and electricity supplies*
- *meeting its increased social and environmental responsibilities."*

1. <http://www.energylinx.co.uk/Ofgem.htm>

What is worse, several price / tariff regulations issued by ANRE actually work against the objective of improved competition on the wholesale and retail markets. Regarding competition in and fair access to networks, this role is currently effectively done by transmission operators (Transelectrica) and we do not recommend a higher role of ANRE unless ANRE's governance issues detailed in the first part are resolved beforehand.

II. There are reasons for concerns about the capacity of ANRE to enforce some of its regulations, particularly in areas concerning consumer protection and monitoring / sanctioning the companies in breach of investment obligations according to regulatory periods. Even more, to respond to enforcement challenges, ANRE considers solutions that would affect regulatory predictability (e.g., reduction of distribution tariff to those in breach)

1. Tariff design

ANRE regulates several tariffs and end-user prices for “captive” consumers.

- distribution for electricity and gas (price cap)
- transmission (revenue cap + price cap on zones for electricity)
- gas storage (revenue cap)
- ancillary services for electricity (price cap, to mitigate hydro dominant position)
- regulated prices for (co)generation
- end-user prices for gas (“basket” price, import and domestic gas) and electricity (regulated “basket” of electricity in the wholesale market + transmission and distribution)
- social tariffs (setting directly the end-price).

In principle, the tariff methodology for all regulated activities is supposed to ensure cost recovery, while at the same time containing incentives for improvements of the economic efficiency and quality standards. Also, the tariffs for networks are in principle **predictable**, being set using regulatory periods, which started from 2005 onwards (initially 3, then 5 years); they are known ahead of time and the documents are posted on the website for comments before the approval of the final version. The introduction of the regulatory periods for transmission networks was appreciated by the World Bank. On the electricity distribution there was also an additional guarantee for stability until this year: a PRG project with the World Bank which guaranteed the stability of the regulatory framework to reduce the risk premium demanded by the investors during privatization of several electricity discoms (we noted however an exception to this regulatory stability in the case of ENEL explained below).

However, there are several issues with the tariffs regulated by ANRE, of which we selected some relevant examples to explain why these affect competition on wholesale and retail markets. We consider the **tariffs for networks and ancillary services to be relatively good** (some improvements are however suggested), whereas **tariffs for regulated consumers lead to serious market distortions**. We took examples for each: electricity transmission (for network); captive and social electricity consumer and captive gas consumers (for tariffs for regulated consumers).

1.1. Tariffs for networks and ancillary services

1.1.1. Domestic tariffs, electricity transmission

ANRE regulates the transmission tariffs for electricity transported in Romania with two instruments:

- revenue cap for the TSO (which is set in advance by ANRE for the whole regulatory period, currently 5 years). These take into account quality standards, evolution of electricity quantities, changes in losses, regulated profitability rates for assets, inflation. The legislation specifies explicitly that it should be cost recovery

- zonal tariffs on marginal cost in the nodes (costs considered are regulated assets, maintenance and operation, asset depreciation and annual investments, technological electricity consumption, electricity bought to manage congestions in the balancing market, costs on cross-border trading). All these are considered at the establishment of the revenue cap. The zonal tariffs are a means for allocation of the revenue cap on transmission customers based on these marginal costs.

This approach resembles that of other countries, and is acceptable, though we find it suboptimal (for the reasons explained in the Box 15 below).

Box 15: An alternative regulation of transmission tariffs

From an economic point of view, it would make sense for ANRE not to regulate tariffs on regions (nodes), **but instead to set only the revenue cap**. This would enable the TSO Transelectrica to better manage its network and congestions by “dividing” its revenues on zones so as to stimulate investments in generation in areas without bottlenecks and discourage new generation capacities in areas where the transmission network is congested. However, there is a regulatory risk from this policy. For example, the transmission operator could potentially manipulate the market by creating “artificial bottlenecks” in some regions and de facto prohibiting access to networks for certain producers. We support the streamlined solution of setting only revenue caps as it would optimize the allocation of resources. However, **it requires additional technical capacity in ANRE to identify potentially anticompetitive practices, and solid governance improvements in ANRE as suggested in Part I.**

1.1.2. Transit tariffs, electricity transmission

A regulation that could affect competition in the EU single market is the approval of **transit tariffs** (eg, Order 7/2010). Transmission tariffs described above (based on zonal tariff mechanism) consist of tariff at entry in network (TG) and tariff at exit from network (TL). For imports and exports of electricity Transelectrica collects only TG and TL, respectively. **There is no reason why transit tariffs should be imposed**, as TG and TL are paid already in the countries of origin and destination of electricity, and an Inter – TSO Compensation (ITC) mechanism redistributes the cost – effect of transits. This provision restricts free circulation of electricity in the Single Market by imposing additional costs for electricity traded over borders.

In addition, if the case, all attempts from the TSO to impose an additional tariff at the border for electricity imports and exports should be discouraged by ANRE. Not to mention that, if our recommended approach is followed (only revenue cap regulation and letting Transelectrica to set up the zonal transmission tariffs) and tariffs at borders are introduced, a transmission sector operator could create transmission tariff ‘pan-caking’ i.e. artificial increase of transmission service price. This is explicitly forbidden by the EU cross – border regulation. While very tempting for national governments (as it gives a competitive advantage to goods produced in the national market), **this affects competition in the Single EU market.**

1.1.3. Ancillary services price cap

The way in which ancillary system services market operate is approximately equivalent to one competitive market for an ordinary good with Transelectrica as a “broker”. In this market, Transelectrica buys and sells electricity generating reserves and voltage - reactive control requiring sellers and buyers to make offers and selecting the best offers available. Sellers that trade through Transelectrica the reserve capacities are also required to put on the balancing market at least the energy equivalent to the capacity reserve. In economic terms, this mandatory market is quite equivalent (lead to largely the same results) to a competitive, voluntary market directly between buyers and sellers (if we assume no congestion on the transmission grid). However, in this market the supply of ancillary system services is dominated by Hidroelectrica, the hydro electricity producer, which has a market share of 80-90%. To avoid excessively high prices, ANRE regulates price cap the ancillary services. In reality, ANRE approves tariffs for ancillary system services negotiated by the TSO with Hidroelectrica. Currently, this arrangement works acceptable in practice because Transelectrica is independent and well-governed while the market dominance of an only supplier remains an issue for the future regulatory developments.

1.2. Regulated prices for electricity end-users (“captive” consumers)

“Captive” end-users buy electricity from 8 implicit suppliers, at regulated prices, which consist of a “basket” price for electricity plus tariffs for transmission and distribution. The 8 retailers (supplying captive consumers in 8 different regions of Romania) buy (a) a regulated “pool” of electricity from the main producers, and (b) a balancing and pass-through - priced electricity from the competitive market. For the captive market, ANRE regulates the **quantities** and **prices** that each producer must contribute to each basket. According to ANRE's statements, the structure of the pools for the 8 suppliers is determined in such a manner that prices for end-users are relatively equal across regions. A similar mechanism is used also for the regulated gas market.

Currently, the captive consumers represent 50% of the market (in both gas and electricity), and has remained so since 4 years ago. The EC has started an infringement against Romania in June 2009 because the regulated market share does not decrease below 50%, suspecting distortionary tariffs that prohibit consumers to switch suppliers, even for consumers which are not in the “social” category.

This can be easily checked:

- We took the example of consumer in lowest consumption category, which is similar to a household or a small company. The price for electricity in June 2010 for the competitive market for a consumer in the lowest consumption category (IA) is 0.342 RON/kWh. If we add the regulated tariff for transport (0.1691 RON/kWh) and distribution (0.0569), we obtain a price of 0.568 RON/kWh. This is **much higher than the regulated price for a captive consumer** (0.43 RON/kWh, according to Order

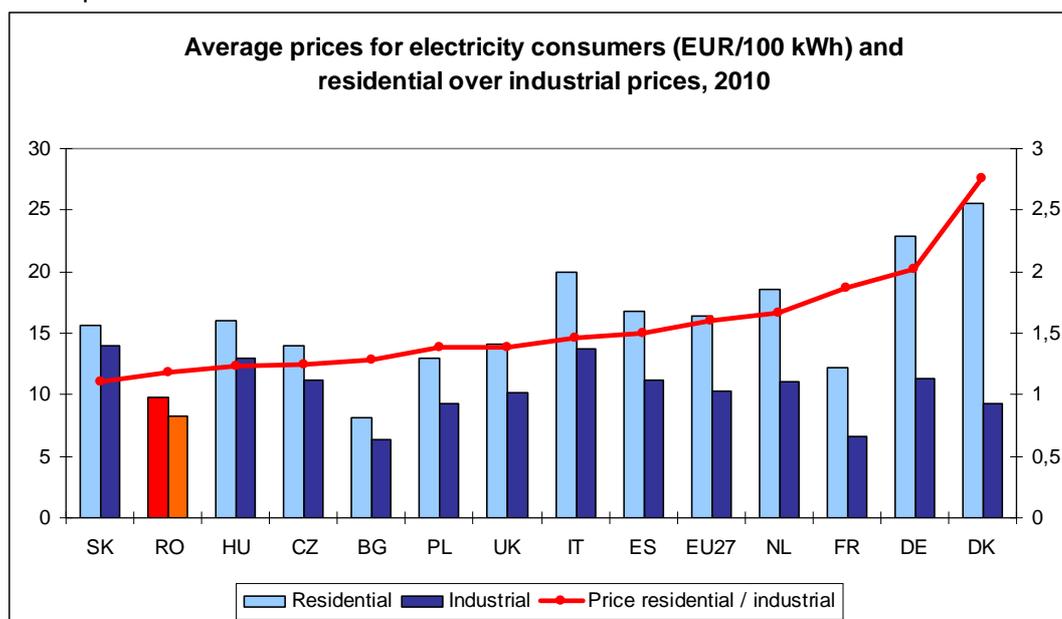
102/2009). For this reason, there is no incentive for a captive user to switch supplier and effectively pay more.

Box 16: Options for residential consumers? 1

Mr. Mihail Biolan inquired in 2008 about the possibility to switch suppliers, as a residential user. He has requested offers from more suppliers. The best one was from Electrica Bucharest, at a price 50% higher than he was paying in the captive market (0.38 RON/kWh compared to 0.26 RON/kWh, from Muntenia Nord). He also inquired from his current supplier what price he would get in the competitive market. The answer was above 0.4 RON/kWh.

1. <http://www.capital.ro/articol/ne-vom-putea-schimba-furnizorul-de-electricitate-abia-din-2010-108731.html>

- While explicitly forbidden by both the gas and electricity laws, there is also evidence of **cross subsidization from industrial to residential users**. Normally, residential users have much higher prices than the industrial ones (higher distribution costs, industrials buy in bulk etc.). On average, in EU27 the proportion of prices residential/industrial is 1.6, whereas in Romania it is only 1.18 (lower than in most EU countries). In other words, industrial users pay more so that we could have lower prices for households.



1.3. Social tariffs for electricity

To meet EU's market liberalization conditions, Romania is required to adapt its legislation to the EU, **abandoning the "social tariff" and introducing instead a streamlined concept of "vulnerable consumer" to which a form of direct income support should be given**. However, the "social tariffs" have not been abandoned until now (see Order 102/2009). In 2008, for example, 1.7 million residential consumers, of a total population of 21 million, benefited "social tariffs"¹⁰ (which means that whatever social protection is intended, it is still too thinly spread and

¹⁰ <http://stiri.kappa.ro/economie/25-04-2008/o-noua-majorare-de-tarife-energia-electrica-se-scumpeste-de-la-1-iulie-174169.html>

ineffective, in addition to distorting the markets). In addition, these social tariffs **impose losses on the suppliers without appropriate compensation**. Suppliers for the captive market are required to provide electricity to residential consumers at the social tariff, but there is no compensation for their loss; which means they have to **subsidize with proceeds from eligible consumers** (despite explicit provisions in the Electricity Law that any form of cross-subsidization is strictly forbidden).

There is evidence that such subsidization actually takes place. The table 2 below summarizes the example of a captive social consumer, from North Muntenia region, consuming less than 2 kWh/day, according to ANRE Orders 100-103 from December 2009. The price paid by the consumer is lower than the costs of supplier with distribution and tariff only, which means the supplier has to put its own money to cover the difference! Of course, this is not possible unless the supplier “cross-subsidizes” the loss from revenues on other consumers (eligible). This distorts the markets even more: prices for eligible users are higher than they could have been, to cover the supplier’s losses, discouraging captive consumers to switch suppliers.

Table 2: Cross subsidies from social to eligible consumers

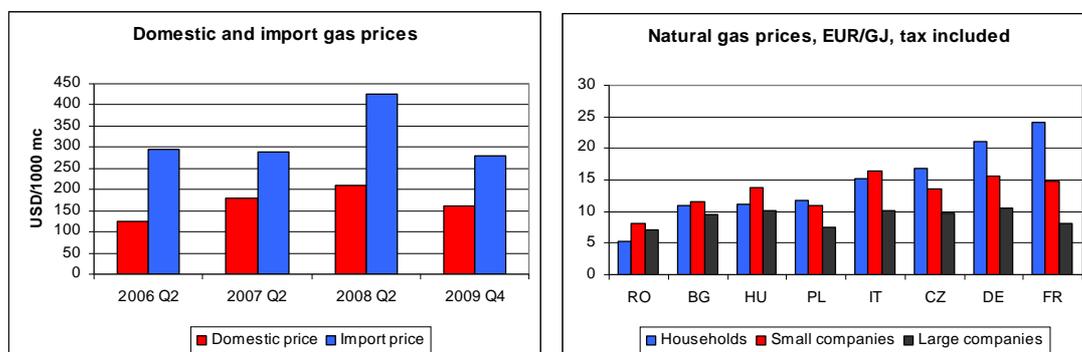
	RON/kWh	RON/kWh
Price paid by consumer		0,1804
Costs of supplier		
Distribution tariff (high, medium, low voltage)	$(13.26+34,92+120,97)/1000$	0,1691
Transmission tariff (zonal G and L tariffs, ancillary)	$(17+20,68+0,3+6,86+12,01)/1000$	0,0569
Distribution + transmission		0,226
Electricity cost (balancing figure)		-0,0456

This practice of “social tariffs” must be discontinued, as it is not in line with EU’s practices and rules. In order to avoid market distortions, social tariffs should be replaced by the system of social access to energy with a clear definition of vulnerable consumer, and direct income support only to this category, so that all consumers pay the same market-determined prices and energy efficiency is stimulated (lower waste). A more detailed discussion on consumer rights and vulnerable consumers follows in Part 2 – Regulatory substance, Consumer protection.

1.4. Captive consumers for gas:

In the gas sector, ANRE keeps domestic prices low and the captive end-consumer pays a “basket price” (plus network tariffs). Romania has agreed with the EU to align domestic to import gas prices by end-2008 but, under the pretext of the crisis, Romania has asked for an extension until 2010 (extended later until at least 2011), even though the import gas price was decreasing. Romania has the lowest gas price in Europe for both industrial and residential consumers, which could trigger the infringement procedure from the EC, because our industry is not competing fairly in the single market. What is more, Romania is **the only country where household prices are lower than industrial prices**, which suggests cross-subsidization like in the

case of electricity. In gas also, a more adequate social protection policy would be to provide direct income support to targeted poorest households and reduce energy losses in residential buildings by thermal insulation (where losses amount to 40-50% of energy consumption).



Sources: Petrom; Eurostat.

Thus, **tariffs for the captive and social consumers fail to meet several key criteria for good practice:**

- they represent **overregulation that burdens the industry**. These tariffs distort both the wholesale markets and the retail markets. In the wholesale markets, producers are required to sell at regulated “basket” prices below what they would have obtained on a competitive market, and possibly also below costs (eg, not all costs are recognized to Hidroelectrica in the basket price, for example the cost of water or true investment needs). Retail markets are distorted by the cross-subsidization explained above.
- they are **not consistent with the strategic goal of increasing energy efficiency**: keeping low prices for domestic gas actually exhaust natural resources (estimated to last 15 years, at least before the new reserves in the Black Sea are used), and low electricity prices for households encourage waste.

Because of these tariff distortions and the lack of political support for full liberalization, Romania is the laggard of Europe in its efforts for a common EU policy (see Tables 3 and 4 below):

Table 3:

Overview of market opening & price regulation in open electricity market segments as of 1 January 2010

Country	Market opening Final market opening date	Price regulation on 1 January 2010			
		Households	Small businesses	Medium-sized to large businesses	Energy-intensive industry
AUSTRIA	2001				
BELGIUM	Jan-07				
BULGARIA					
CROATIA					
CYPRUS					
CZECH REPUBLIC	2006				
DENMARK	2003				
ESTONIA	2009	2013-01	2013-01	2010-04	2010-04
FINLAND	1997				
FRANCE	Jul-07				
GERMANY	1998				
GREECE	Jul-07				
HUNGARY	Jul-07				
ICELAND					
IRELAND	2005		2010-10	2010-10	
ITALY	Jul-07				
LATVIA	Jul-07				
LITHUANIA	Jul-07	2015-01	2013-01		
LUXEMBOURG	Jul-07				
MALTA					
NETHERLANDS	2004				
NORWAY	1995				
POLAND	Jul-07				
PORTUGAL	2006		2011-01	2010-01	2010-01
ROMANIA	Jul-07				
SLOVAK REPUBLIC	Jul-07	2012-12	2011-12		
SLOVENIA	Jul-07				
SPAIN	2003		2009-07	2009-07	2008-07
SWEDEN	1996				
UNITED KINGDOM'	1990				

Price regulation : YES (yellow), NO (green), Closed market (red), N.A. (grey)

Changes between July 2008 and January 2010: End-user price regulation in open market segment removed between July 2008 and January 2010 (orange border), Segment closed in July 2008 (red border)

XXXX-XX Scheduled date of price regulation removal

Table 4:

Overview of market opening and price regulation in open gas market segments as of 1 January 2010

Country	Market opening Final market opening date	Price regulation on 1 January 2010			
		Households	Small businesses	Medium-sized to large businesses	Energy-intensive industry
AUSTRIA	2002-10				
BELGIUM	2007-01				
BULGARIA					
CROATIA					
CZECH REPUBLIC	2007-01				
DENMARK	2004				
ESTONIA	2007-07	2009-07			
FRANCE	2007-07				
GERMANY	1998				
GREECE	2009 - 2030	2031-11	2031-11	2031-11	
HUNGARY	2007-07				
IRELAND	2007-07				
ITALY	2003-01				
LATVIA	2014-04				
LITHUANIA	2007-07				
LUXEMBOURG	2007-07				
NETHERLANDS	2004-07				
POLAND	2007-07				
PORTUGAL	2010-01				
ROMANIA	2008-07				
SLOVAK REPUBLIC	2007-07				
SLOVENIA	2007-07				
SPAIN	2003-01		2009-07	2009-07	
SWEDEN	2007-07				
UNITED KINGDOM	1998				

except: Turkey (NA), Finland (exempted from opening) ; except Cyprus, Iceland, Malta, Norway (no gas)

Price regulation : YES (yellow), NO (green), Closed market (red), N.A. (grey)

Changes between July 2008 and January 2010: End-user price regulation in open market segment removed between July 2008 and January 2010 (orange border), Segment closed in July 2008 (red border)

XXXX-XX Scheduled date of price regulation removal

2. Monitoring & licensing

The following are essential elements for a good monitoring & licensing performance:

2.1. Access to all relevant information from the sector

One of the improvements in the energy laws in 2007-2008 was to explicitly empower ANRE to request and receive information from the regulated industry. In order to make full use of this right, ANRE should have a very clear idea of what information is relevant for its decisions, market monitoring activities, controls and investigations; and preferably have some published, standardized formats for the information. There are two major types of information needed for a regulator for good market monitoring and regulation enforcement:

2.1.1. For market monitoring: ANRE has published several Orders, containing the methodology on how to monitor markets, what information will be requested by ANRE and what outputs would be delivered by the market monitoring function in ANRE (e.g., Order 35/2006 on monitoring electricity wholesale markets)¹¹. The monthly market monitoring reports contain information requested monthly from market participants (producers, suppliers), from Transelectrica and OPCOM. A possible addition to market monitoring reports could be to follow Ofgem's approach (Ofgem publishes in the monitoring reports the methodology used and questionnaires sent to market participants), instead of having only the Orders on methodology in separate parts of the website.

Box 17: Alternative solution for independent market monitoring

ANRE monitors the energy markets and prepares monthly reports. However, these reports are silent on recent scandals signaled by the media (e.g., "cheap" sales of energy from state-owned companies in non-competitive deals with private partners, by bypassing Order 445/2009). An alternative solution could be to set up an autonomous, small and professional Energy Market monitoring unit (an external watchdog). The extent to which such a watchdog could be organized / financed by an association of all energy market players (electricity + gas), must be examined, to ensure independence from the interests of any individual company. If systematic reports on market monitoring are made public, this could further improve the transparency of the energy market and pressure for actions from ANRE in case of abuses.

2.1.2. For controls and investigations: Having a formalized, systematic approach for market monitoring, as well as controls and investigations, is critical for the predictability of regulation to the regulated industry. It would also be beneficial for ANRE to refer in each case to specific rules and procedures that are **discussed, general and transparent, and integrate all the relevant elements into one single coherent document**. We would recommend again following the approach of Ofgem,

¹¹ <http://www.anre.ro/documente.php?id=157>

which has issued and published on its website its “**Enforcement guidelines**”¹². This describes the processes and procedures that the regulator uses on investigations and complaints from the sector, and provides a general framework that ensures investigations are not discretionary. The Enforcement guidelines must be stable (not amended frequently) and before their approval they must be publicly debated with the regulated industry. Such a document details the implementation of the general legal provisions and explains the actual processes by which the regulator enforces its regulatory capacity.

In its annual report, ANRE discloses information on interruptions and benchmarks against EU averages. But the extent to which ANRE indeed requests and actually uses extensive additional relevant information for controls and investigations is unclear, as we will see in the next section.

2.2. Rules enforcement

There are concerns that ANRE encounters problems in the actual enforcement of some of its regulations. In the 2009 Annual report, the total amount of sanctions (600 K RON in 2009) looks quite small, and most cases investigated and sanctioned have led to relatively small penalties. We gave below an example of situation in which ANRE could not enforce its rules: monitoring the implementation of conditions for electricity distribution. Thus, a recent scandal in the media (see Box 18) highlighted the difficulties encountered by ANRE to monitor and enforce its key regulations in the electricity distribution.

While some of the requests of the Senate commission are not realistic or in line with good energy regulation practices, the investigation highlights several problems. First, ANRE could not monitor and enforce the obligations of the distribution company towards consumers. Second, the implementation of the company’s investment plan was also not verified. ANRE should have monitored the contract from the beginning and sanction non-compliance, if the case.

An additional worry is ANRE’s response to the scandal. The reduction of tariffs is **not a recommended way to apply sanctions, because the distribution tariff should be predictable in the regulatory period**, not changing from year to year. A more effective way to sanction a company in breach of its obligations would be to demand penalties in cash, and not symbolic amounts.

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<http://www.Ofgem.gov.uk/About%20us/enforcement/Documents1/Enforcement%20Guidelines%20post%20consultation.pdf>

Box 18: ENEL scandal and ANRE's response

In the spring of 2010, a Senate Commission has examined the privatization contract of ENEL Distributie Muntenia (ENEL D), an electricity distribution company, in 2005. The investigation had allegedly started as a response to a series of complaints in the media from consumers for low quality of supply and interruptions. According to the commission's report, ENEL had not met its investment plan agreed upon with ANRE, which was used by ANRE to approve ENEL's distribution tariff for the second regulatory period. Investments were 53% of the initially agreed plan in 2008 and 52% in 2009.

ANRE responded that if ENEL would have been proposing initially a 50% lower investment plan, the distribution tariffs would have been: 3% lower in 2008, 6% lower in 2009, 9% lower in 2010, 12% in 2011 and 15% lower in 2015, but with negative consequences on the quality of supply.

The Senate commission requested ¹:

- reduction of regulatory period to lower than 5 years
- annual monitoring of the investment plan
- the Consumer Protection agency to investigate maintenance agreements with ANRE because interventions in case of interruptions are much slower than before privatization
- ENEL D to improve quality and disconnect only those who do not pay or who connect illegally to the network
- Methodology to be issued by ANRE, Ministry of Economy, Consumer protection etc. to ensure consumers are connected without having to make own investments
- ENEL D to provide Electrica (state-owned, minority shareholder in ENEL Distributie) information on relations with affiliated parties and respect minority shareholder's rights
- ENEL D to publish General Shareholders' Meetings minutes in Official Gazette
- ENEL D to provide evidence it has used money from new shares issuing for investments in the energy sector, as per the privatization contract
- As ENEL transfers shares in ENEL D to another company (EIH), ENEL to provide evidence that privatization contract obligations are transferred entirely to EIH
- All state institutions involved (Ministry of Economy, ANRE, Electrica etc) to provide evidence they have monitored the implementation of ENEL D's obligations

ANRE responded in a press release² that ENEL D had been sanctioned with 355 KRON after an investigation undertaken in May 2010. ANRE also responded that it has initiated the process of reassessing the methodology for tariff distribution so that it can reduce tariffs for the next year to distribution companies that have not met their investment plan at least 80%, and not at the end of the regulatory period, as it is now.

¹ http://media.hotnews.ro/media_server1/document-2010-07-5-7533070-0-raportul-comisiei-senatoriale.pdf

² <http://www.anre.ro/informatii.php?id=900>

2.3. Licensing and authorizations

The criteria for licensing and authorizations should be transparent and non-discriminatory. ANRE publishes on its website the rules for issuing licenses and authorizations, and the general conditions for licensing. The meetings for issuing the licenses and authorizations are open to the public (those interested can ask by phone to attend the meeting). Individual licensing decisions are published, together with the licensing conditions for each license or authorization issued.

We looked at several decisions to issue licenses and authorizations, including the licensing conditions agreed upon with licensees. These contain the general conditions (copied in full) and very few specific conditions (e.g., in an Annex, the description of the authorized production capacity for an authorization to build a power plant).

The problem that arises from the conditions for licensing is that they do not provide good assurance that the **rights of consumers** would be fully respected (see below section on Consumer rights).

The withdrawal of licenses is also publicly announced and the meetings are open to the public. The published decisions to withdraw or suspend licenses do not give details on the reasons behind the decision. However, the general criteria for licensing specify the conditions under which a license could be suspended or withdrawn (time expiry, failure to meet obligations etc.). The decisions could be contested in courts.

2.4. Regulated TPA and competition in network access

Non-discriminatory, regulated third party access is one of the well-performing parts of the Romanian energy system. The regulated third-party access is the right to connect to and use, under the conditions provided by law, the transmission or distribution networks, for both gas and electricity. Currently, also as a result of the fact that the electricity transmission grid is independent and working properly, there are no cases of discrimination in access to the grid. Access of generators could be denied with just cause if the connection affects the safety of the National Power System. For the cross-border connections, the capacity is allocated by transparent auctioning, the results being available on Transelectrica's website.

ANRE's involvement is very limited in the monitoring of the auctioning of cross-border capacities or enforcement of regulated TPA; as we mentioned before, this corresponds to ANRE's activity focus rather on **tariff-setting** for networks (and less on the development of modern markets, including fair access to networks¹³).

Regarding the competition for the connection of consumers to distribution networks of gas and electricity, there is no active preoccupation from ANRE to stimulate and monitoring this aspect.

¹³ Explicit competition for transmission capacity is actual only in cross-border trade. Access to domestic network is based on energy competition. Who won on the energy market has a priority of access to network. Unfortunately, this principle is not applied at access to international interconnectors.

Box 19: Ofgem – Connections industry review¹

Ofgem issues yearly a report on competition in connections, for both gas and electricity transmission and distribution networks. The importance of doing so is highlighted in their report: “Some aspects of the distribution of electricity and gas to business and domestic customers are natural monopolies – because it is cheaper and more efficient to have one single company owning and operating the network than several competing companies with competing networks. However, the construction, owning (and operating) the network assets required to extend the network or connect to the existing network is a competitive activity. Customers could benefit from competition in connections through lower prices and better service (for example faster connection installations). Ofgem has worked over a number of years to promote competition in the gas and electricity connections markets.”

1. <http://www.Ofgem.gov.uk/Pages/MoreInformation.aspx?docid=52&refer=Networks/Connectns/ConnIndRev>

While in time ANRE could gain capacity and independence to perform well this task, currently the well functioning of the regulated TPA and the auctioning on cross-border capacity is due to the fact that **Transelectrica remains a well-governed company that is independent from political and industry interests. We do not recommend higher involvement of ANRE in these technical matters unless ANRE solves the main governance issues highlighted in the first part of the report.**

2.5. Consumer protection and managing consumer complaints

While protecting the consumer is one of the key functions of an energy regulator, a major problem is that Romania has no clear, unitary definition of **service of general economic interest (SGEI), or public service obligations**, as recommended by the Directives on Gas and Electricity and in the European Chart of rights for energy consumers.

Box 20: The European Chart of rights for energy consumers

The European Chart of rights for energy consumers¹, prepared by the EC, has the following objectives:

- to support vulnerable consumers
- improve available information for consumers, so that they choose their supplier
- formalities to switch suppliers must be reduced to a minimum
- consumers must be protected against abuses on the market.

Users have the right of access to supply of energy, of a certain quality, at an affordable price. Disconnection must be avoided as much as possible. The contracts must contain information (tariffs, payment methods, metering, energy efficiency opportunities). Consumers must have the right to choose freely their supplier, with minimum transaction costs. Users must also have rights to fight abuse, in administrative conflict resolution mechanisms. Vulnerable consumers must be identified and protected, but without distorting markets or discriminating other consumers.

<http://www.anre.ro/informatii.php?id=459>

The fact that rights for energy consumers are not enforceable can be seen in both law and actual practice. While elements of “consumer rights” exist in the current secondary legislation issued by ANRE, enforcement seems weak (see Box 21). In addition, SGEI should be regulated clearly by primary legislation (not by ANRE), in a transparent and democratic process, based on sound cost-benefit analyses.

Instead, ANRE has issued Orders for electricity and gas, on standards of performance for suppliers, which cover some of the key rights of consumers, including the rights to request and receive offers from any supplier.

Box 21: Response to request from captive gas consumer to become eligible

Based on the European Directives on Electricity and Gas, and the recommendations contained in the European Chart of rights for energy consumers, and according to the Order 37/2007 of ANRE regarding performance standards for gas suppliers, a consumer has the right to receive offers from any supplier. Suppliers are required to respond with offers in 15 days from the request from the potential customer; otherwise they are liable to penalties per day of delay.

Mr. Mihail Biolan, a consumer (residential, "captive") tested the application of this principle by asking offers from 10 gas suppliers licensed by ANRE, to become eligible consumer. The request was made in December 2009. He did not receive any offer from the suppliers after 30 days. He sent in May 2010 a complaint to ANRE to request the sanctioning of the 10 suppliers for not complying with the obligation to provide offers. Instead of applying the regulation, ANRE replied in June that "the request has no solid grounds as it is not clear which supplier should be sanctioned". The consumer filed another complaint in July addressed to the President of ANRE and no response was received since.

On **consumer complaints** ANRE publishes in its annual report only statistics with types and numbers of complaints, but **without showing how many of them were resolved**.

Among the complaints addressed to ANRE, some are related to settling disputes between consumers and suppliers. In order not to overload the department in ANRE dealing with complaints, alternative solutions could be investigated, looking at what could be applicable from international experience. Various countries have different arrangements for the resolution of such disputes: e.g., an Ombudsman consisting of private companies (UK), or an administrative – judicial mechanism (France) (see Box 22). That would allow ANRE to respond adequately and with proper substantiation to the **complaints regarding its own regulations, requests for investigation of anticompetitive practices or failure to enforce its own rules**.

Box 22: UK Energy Ombudsman¹, CRE - CoRDIS in France²

"Ofgem determined in 2005 that energy suppliers should establish a scheme to resolve outstanding billing disputes in a fair and independent way. The energy suppliers who were members of the Energy Retail Association committed to establishing an alternative dispute resolution (ADR) scheme within 12 months as part of their ongoing drive towards improving customer service and the ongoing trend towards reduced complaints within the industry. They felt that such a scheme would further strengthen existing arrangements for complaint resolution within the domestic energy sector. The Energy Ombudsman is that scheme." A consumer can complain to the Energy Ombudsman if he/she has unsolved complaints against an energy company.

In France a dispute resolution role is met by CoRDIS (Comité de règlement des différends et des sanctions), created in 2006, an entity for sanctions and disputes on access and use of public electricity and gas networks. It is composed of two councilors from the State Council (a judicial and advisory body that assists the executive with legal advice and is the Supreme Court for administrative justice) and two councilors from the Supreme Court.

¹ <http://www.energy-ombudsman.org.uk>

² <http://www.cre.fr/fr/presentation/organisation/cordis>

In addition, other elements are missing from the legislation and practice, such as a consistent definition and modern form of protection of **vulnerable consumers**. There were disparate attempts to legislate the concept of “vulnerable consumer”, such as in a general provision in the Electricity Law (vulnerable consumers are residential who, for some reasons related to health, age etc. benefit special facilities in supply of energy), or as households whose per capita revenue is below minimum wage, in ANRE’s Order 102/2009. As we explained above, the protection of “vulnerable consumers” continues to be ensured by the means of “**social tariffs**”, in contradiction to EU directives and distorting the market. All social energy aids should be transferred to a distinct system that is separated from the energy market.

Annex – Questionnaire

Questionnaire for the regulatory body (adapted from World Bank and Inogate, mid-level evaluation / in-depth evaluation). The questionnaire contains main issues related to ANRE, not the general energy framework (which is however considered in the report).

REGULATORY GOVERNANCE

(In interviews we asked also about decision-making methods, organization structure of ANRE and regulatory model followed, appellate review, ethics code if any)

INDEPENDENCE

1. Is ANRE autonomous from utilities and Ministry? In law and de facto.
2. Are there multiple regulatory agencies affecting the electricity / gas sectors?
 - a. Are there areas of electricity / gas which are not regulated? (“gap”) not the case
 - b. Are there overlap among regulatory bodies? (“overlap” of responsibilities)
 - c. Are there any responsibilities that should belong only to ANRE but are de facto split among agency / ministry / other agencies? (“split”)
 - d. Are there fuzzy areas where no one knows who should regulate? (“fog”) financial derivatives on the power exchange
3. Who finances ANRE? (own revenues such as license fees; customer levies; or general tax from budget)
4. Who heads ANRE (president or board)? Who is issuing the regulations?
5. Staffing:
 - a. directors
 - b. technical staff (engineers, economists, legal)
6. How is the head (President) appointed? (Parliament, PM ..) + is there an additional check? (eg PM nominates, Parliament approves)
7. Is the president appointed fixed-term? (in law and de facto)
8. Length of appointment
9. Can the president be reappointed?
 - a. What are the procedures to fire the head of ANRE? (legal and de facto) Have the legal provisions been observed?
 - b. Who has the authority (Parliament or PM); On what grounds? (e.g., annual report rejected in Parliament or incompetence, conflicts of interest monitored by other agency – ANI, corruption scandals – DNA prosecution or final court decision)
 - c. How often have ANRE presidents been fired before end of legal term?
10. Veto of ANRE’s decisions (in law and de facto)
 - a. Can decisions be reversed? By whom? (Parliament, Govt?, **courts**..). How often has it happened?
 - b. Are there checks from outside? (e.g., the mechanism of infringements from the EC). Does it actually work to reverse decisions or bad policy practice?

- c. Who issues policy guidelines for regulator? (PM? Parliament? Is there direct interference from Ministry of Economy? Does ANRE issue its own policy strategy? EU? EU regulatory association?)
 - d. Are these guidelines publicly available?
 - e. Can the minister, PM, or others give verbal instructions to regulator? Or informal? (eg public statements about prices without asking ANRE, having as result a change of tariffs by ANRE)
11. Can the agency obtain in due time information from regulated sector? (eg data on the market transactions, financial reports from companies, performance, items needed for tariff approvals based on clear information etc; preferably, the information requested must be in standardized format, to ensure regulated companies are judged on the same data)
12. Does ANRE request auditing of this information from companies? (eg financial reporting)

TRANSPARENCY

13. Does ANRE publish financial and performance information?
- a. Has the quality / completeness of this information increased / decreased in time?
 - b. Is performance data available in a easily accessible format for a lay person? (eg, a report explaining “in a nutshell” what ANRE has done in previous year, not just a list of orders which you have to check one by one) [Box in main report: a relevant comparison with website of another energy regulator]
 - c. Does the management and key directors disclose statements of wealth and interest? (to be monitored mainly in the second phase, because the Constitutional Court has just practically dismantled ANI, the agency that checks these aspects, and dignitaries are no longer required to publish in detail these statements)
 - d. Does ANRE present a report on how the money is spent and how assets are used?
 - e. Are technical jobs advertised and people hired competitively? Is “politicization” an issue? [we need to get old and new organization chart to make a point with the excessive no of directors]
14. Before decisions, is there consultation? How in-depth? (in law and practice)
- a. By publishing the draft orders / secondary legislation for comments
 - b. Does ANRE organize meetings with affected parties? For what decisions? (actual involvement and push for comments, not simple information and passive consultation)
 - c. Who is consulted? (consumers, investors, utilities etc)
 - d. Are consultations open to the public on request? (in law and practice)
 - e. Can decisions be appealed if stakeholders disagree?
 - f. Please describe the appeal mechanism (administrative court or body, first / second / third instance; appeal to regulator; ministry; govt or Parliament)

- g. In how many cases have there been appeals? (Informally - Do companies appeal or lobby informally/bribe? – to be asked in a manner that does not affect the person who answers, such as “how often have you heard of decisions being tailored for a company because of bribes”)
- h. Can only the directly affected parties appeal, or also others? Who?
- i. Are there decisions which are simply not published for consultation in the legal period? (“emergency” situations, exceptions to the rule)
- j. Are final decisions published? Always? On website or other very easily accessible media that can be consulted also by the general public? (in law and practice)
- k. Are decisions published with explanations? (does law require a “substantiation note”? is this followed? Are “substantiation notes” of good quality?). Are stakeholders (regulated companies, consumers) satisfied with the explanations? (e.g. How are the electricity pools for “regulated consumers” formed?)
- l. Have there been cases of information requested on Freedom of Information Act (Law 544/2001) which has not been adequately responded to? [to be tested also by us. Please recommend us some sensitive issues in terms of public disclosure which we can send information requests on L544 – e.g., how they determine the tariffs for regulated consumers and how the baskets are prepared for the 8 discoms, but also others]

REGULATORY SUBSTANCE – TARIFFS:

(I asked in interviews also details about tariff setting methodology, regulatory periods, price regulation in gas, and how these fit into best practices or follow recommendations from the existing consultancies on tariff setting methodology. An overall finding: Too little focus on market rules (if they are properly developed and observed) and market monitoring; ANRE should get rid of price setting for end users and generators, and remain with only tariffs for the grid access.)

15. Which of the following are regulated?

- a. Supply. Electricity prices for “captive consumers” – how do they define “captive consumer”, residential or also others?
- b. Transmission tariff – is methodology adequate?
- c. Distribution tariff – is methodology adequate?
- d. Generation?
- e. Storage? (for gas)
- f. Social tariffs? Who sets them, ANRE and / or Ministry? [the equivalent of the labor Ministry] Is there consultation on this among govt organizations? (eg with Ministry of Labor who deals with social issues and supports social programs)
- g. Are there known tariff distortions? This is the main issue of tariffs!
- h. Do tariffs allow cross-subsidies?

16. How are end-user prices set?

- a. What are the roles of Ministry / market / regulator in pricing? (monitoring, advising, deciding)

- b. Is participation in competitive wholesale market mandatory for state-owned companies?
- 17. What is the price control mechanism for:
 - a. Distribution (revenue cap, price cap, rate of return, other - which)
 - b. Transmission (revenue cap, price cap, rate of return, other - which)
- 18. How long is the period between price reviews? [is this the same with the regulatory period?]
- 19. Are there government subsidies for certain fuels? (e.g. coal, gas; support for renewables) Are they transparent? Are there cross-subsidies introduced by the Regulator?
- 20. Subsidies – what is the source? (budget through transparent mechanisms, budget through non-transparent mechanisms such as debt canceling on overdue taxes to the government – see Termoelectrica 2007; cross subsidies – e.g. Hidro and Deva, others?). Are there subsidies “imposed” on private sector? (e.g. a regulation that causes indirectly a private company to keep its prices low to compete with a subsidized public Co; or a regulation that forces a private Co to purchase expensive electricity or fuel to support the state-owned supplier)

INTERCONNECTION [Cross – border trade] & LICENSES

- 21. Does the law require unrestricted third party access? Are there in reality exceptions to this rule overlooked or even supported by ANRE?
- 22. Are rules ensuring level play to all parties seeking connection? (e.g. same technical requirements for all, published transparently; same prices for all who connect etc.)
- 23. How are access fees/interconnection rates set between the generation and transmission/distribution operators? (regulated, negotiated?) Regulated TPA!
- 24. Are there mechanisms to appeal to these requirements? (what mechanisms?)
- 25. Transmission grid –does ANRE define obligations other than prices (e.g., does Transelectrica have to extend network to connect generators, who pays for connection – TSO or generators etc; how about gas?) Development and investment programs are approved by ANRE in close relation to transmission rates
- 26. Distribution grid – does ANRE define technical obligations (e.g., to extend network to connect poor households in remote areas? Some of these requirements are in privatization contracts for 5 discoms. What are the requirements for the others? Are there discussions with the Competition council to make sure requirements imposed on private discoms are not affecting competition between them and state-owned?) Generally, all requirements have an impact on distribution tariffs
- 27. Are there formal procedures for granting licenses to generation, distribution, transmission, import, export, retail supply, electricity & gas? Are rules transparent and applicable to all? Are there exceptions? This is a hot spot (e.g. a company that got a license without meeting all requirements etc)?
- 28. Who approves licenses and authorizations, is it only ANRE or are there also other approvals needed from other public sector organizations (Ministry, Parliament...). (We found this is not the case; there are some permits within

the dossier that should be obtained from other authorities and network operators)

29. Are licenses granted competitively? (e.g. in gas extraction? We found this is not the business of ANRE)
30. Under what conditions can they be revoked? (in law and practice. E.g. Are there cases where a license / authorization has been revoked by arbitrary decision?)

SERVICE

31. Can utilities disconnect ALL non-paying customers? Including state-owned companies? (in law and practice, are there exceptions?)
32. Are social policies (support for poor customers e.g. low income households) clearly defined, published and clearly SEPARATED from ANRE's obligation to ensure market competition?).
33. Does ANRE's policy ensure non-discrimination among customers? (e.g., tariff issues that "discriminate" between categories of customers such as "captive" and "eligible" for the portion of "captives" that would go for market if prices were not distortionary. Are there others? Who decides who benefits from "price for domestic gas"?)
34. Are there standards for quality? (losses, interruptions – penalties etc) – are these actually ENFORCED and supervised? (have they ever been? E.g. during recent blackouts with ENEL, did ANRE check whose fault they were? Are there effective penalty mechanisms? Does ANRE follow up on improvements of quality for those who have to take measures – e.g. the reduction of losses in the distribution sector per privatization contracts)
35. Does ANRE monitor the quality of its regulations? (e.g., if they propose a regulation to increase the number of connections in remote areas, do they follow-up? Not the business of ANRE. Do they amend their legislation if it doesn't work? Monitor % of non-eligible consumers? The share of renewables after new legislation? Losses before / after new system of penalties?) On renewables: does ANRE observe the legal quota? What's its role in the establishment of connection levels?

FIT INTO THE GENERAL REGULATORY FRAMEWORK

36. Are there structured / formalized rules of cooperation with other agencies on items of interest to ANRE? (e.g. competition council on electricity market and OPCOM; consumer protection on regulation of tariffs for captive residential consumers; on quality of supply to end-users – no interruptions/fluctuations etc.)

Board of Experts

Mr. Jean Constantinescu, PhD. in engineering (power system analyses), is currently the President of the Romanian Institute for Energy Development Studies (IRE association), the Romanian representative to Eurelectric, and the editor of “Energetica” magazine. He is also a senior researcher involved in an European research (FP7) project to develop a unitary platform for safe and efficient power systems and a regional electricity market in South – East Europe. Between 2007 and 2008 he has been a Senior Electricity Market Regulatory and Monitoring Advisor with International Resources Group (IRG), Washington DC, the USAID’s contractor of Regional (South East Europe) Energy Security and Market Development project. In this capacity he has worked with regulatory agencies and TSOs in the region on the design and operation of competitive electricity markets. Between 2005 and 2007, Chief of Party on behalf of IRG, the USAID’s contractor of Romanian Energy Program Phase III (REP 3), supporting reforms in the Romanian energy sector by developing a social safety net program, and solutions for a reasonably competitive energy market. In the past, he has been president of the former integrated power company CONEL, then of the Transmission Grid Operator Transelectrica and the regulator ANRE. He has introduced the Technical Grid Code and Electricity Market Code valid today and has been the promoter of the power sector reform.

Mr. Eliade Mihăilescu, engineer, former State Secretary and Head of the Consumer Protection Office (1997-2000). Former engineer with RENEL (integrated power regie autonome), member of the Consultative Council of ANRE in 2000-2001, president of the social dialogue of UGIR 1903 employer’s association. Consultant on REP III program. Extensive expertise in consumer protection related issues, and contributions to the improvement of consumer protection legislation and approach in Romania.

Mrs. Lidia Ștefănescu, economist, former internal auditor in ANRE. Currently economic director of the Energetica employer’s association, previously internal finance auditor in Energetica. Former annual control planner in the integrated power regie autonome RENEL. Internal Auditor for Quality Management Systems and Quality Management Specialist certificates, TÜV Rheinland InterCert, 2005.

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