

Electricity Regulation

In 27 jurisdictions worldwide

Contributing editors

Earle H O'Donnell and Daniel Hagan



2015

GETTING THE
DEAL THROUGH 

GETTING THE
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Electricity Regulation 2015

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1 Policy and law

What is the government policy and legislative framework for the electricity sector?

The power industry is of special (national) importance in Croatia. The general guidelines of Croatia's government policy regarding the electricity sector are set out in the Strategy of Energy Development (Official Gazette No. 130/09) (the Strategy). At the time the Strategy was adopted, Croatia's main aim was to adjust and prepare the energy sector in general, which includes the electricity sector, for accession into the EU and participation in the single EU market, but at the same time to preserve Croatia's national interest. The strategy is to achieve a balance between the liberalisation of the electricity market and necessary government intervention, to enhance energy efficiency and to use more alternative energy sources and technologies that protect the environment. Croatia's further aim is to achieve security of supply (especially in import of electricity), competitiveness in the international market and sustainable energy development.

In the meantime, the global crisis affected the energy sector, which resulted in a volatile market and prices and lack of planned investments. Consequently, although the main principles remain, the Strategy is not entirely in line with the current market and some of its goals will be hard to attain. As a result, the government adopted several national action plans modifying aims set by the Strategy, implementing specific measures for realisation of EU and national energy targets.

Furthermore, on 1 July 2013 Croatia became a member of the European Union and joined the EU energy market. One of Croatia's obligations as part of its accession process was the incorporation of the EU Third Energy Package. Thus, in 2012 and 2013, new legislation was adopted governing the electricity sector: the Energy Act (Official Gazette No. 120/12), the Energy Activities Regulations Act (Official Gazette No. 120/12) and the Electricity Market Act (Official Gazette No. 22/13). These acts incorporate respective EU directives, in particular Directive 2009/72/EC, 2009/28/EC and 2005/89/EC. However, since up-to-date implementing rules and regulations have been partially passed, full application of a new legislative framework is still expected. Until new rules and regulations are adopted, the old ones are still in force, which in some cases may result in possible inconsistency between new laws and existing by-laws.

Since 2006, Croatia has been a party to the Energy Community Treaty (Official Gazette International Treaty No. 6/06). According to the Croatian Constitution, international agreements take priority over domestic laws and form an integral part of Croatian legislation.

2 Organisation of the market

What is the organisational structure for the generation, transmission, distribution and sale of power?

Croatian law regulates six electricity activities: generation, transmission, distribution, supply, retail and electricity market organisation. Traditionally, all activities were performed exclusively by the Croatian national electricity utility, HEP Grupa (HEP Group). However, through the process of liberalisation and opening of the electricity sector to market competition, certain electricity activities became market activities, while others remained as HEP's exclusive activity. Thus, generation, retail and supply of electricity (except when performed as a public service) are performed as market activities (the price and quantity of delivered power is freely negotiated). On the other hand, the transmission and distribution of

electricity, electricity market organisation and supply (when performed as a public service) are regulated activities and are performed as public service obligations.

HEP Group consists of the Hrvatska elektroprivreda dd as parent company and several subsidiaries, which each perform regulated and market activities.

HEP dd has undergone an unbundling process to meet the requirements of the Electricity Market Act. It opted for the independent transmission operator model, meaning that the transmission system operator (renamed HOPS d.o.o.) remained part of the vertically integrated undertaking HEP Group; however, it had to secure physical, technical and financial independence from HEP dd.

HEP-Operator distribucijskog sustava d.o.o. (HEP-DSO) is the Croatian distribution system operator. It is also part of the HEP Group but independent from other HEP Group undertakings and activities.

Although there are more than 30 registered electricity generation undertakings, 20 suppliers and 15 retail undertakings, HEP Group still holds dominant position on the Croatian electricity market. HEP's position on the market has been changing rapidly during the past couple of years because new competitors have been entering the market, especially the supply market, where these new competitors, such as German RWE and Slovenian GEN-I, offer up to 15 per cent lower prices. Since HEP started losing its customers, it was forced to lower its prices. The battle between suppliers is quite favourable for customers, but it is questionable whether it will be feasible for the suppliers to maintain the current rates in the long term.

Regulation of electricity utilities – power generation

3 Authorisation to construct and operate generation facilities

What authorisations are required to construct and operate generation facilities?

There are two types of authorisations necessary to construct and operate generation facilities: licences for the performance of electricity generation activities and energy authorisation for construction of new generation capacities.

The licence for electricity generation is issued by the Croatian Energy Regulatory Agency (HERA) in accordance with the Rules on Energy Licences (Official Gazette Nos. 118/07 and 107/09).

The energy authorisation for construction of generation capacities is granted by the Ministry of Economy (the Ministry) pursuant to the Electricity Market Act. Other construction, location and environmental licences are issued by authorised administrations or ministries in accordance with the respective legislation.

If and when it finds it is necessary, the government may decide on the construction of additional electricity generation facilities through a public tender procurement process in the interest of safety of supply.

4 Interconnection policies

What are the policies with respect to interconnection of generation to the transmission grid?

Under the Electricity Market Act, HOPS must provide non-discriminatory access to the transmission grid according to the regulated third-party access regime. Any new generator should file a request for interconnection to the transmission grid, which HOPS must accept if all the prerequisites set out

in the General Conditions of Electricity Supply and the Grid Code are met. HOPS may not deny access to the new generator based on possible future network limitations or additional costs related to an increase in network capacity.

Upon issuing consent for interconnection to the grid, an agreement is concluded between HOPS and the new grid user. A new generator whose access to the grid was denied may appeal against HOPS' decision to HERA. HERA's decision is final, but the unsatisfied party may file a claim with the Croatian Administrative Court.

5 Alternative energy sources

Does government policy or legislation encourage power generation based on alternative energy sources such as renewable energies or combined heat and power?

The use of alternative energy sources (water, wind, sun, geothermal sources, combined heat and power (CHP), etc) is one of Croatia's strategic plans as outlined in the Strategy. According to the Strategy, Croatia has great natural and technical potential. Following EU requirements, Croatia adopted in late 2013 a National Action Plan for Renewable Energy Sources until 2020 (hereinafter: Action Plan), as the implementing instrument for the realisation of EU targets (20-20-20) and national energy strategy. In order to meet the targets, the government has shifted its focus from encouraging wind farm construction (the incentives have been quite high in recent years) to energy production from biomass, biogas, cogeneration plants and small hydropower plants.

The Energy Act also expressly states that use of alternative energy sources and CHP is in Croatia's interest (article 13). According to the Electricity Market Act, any generator that uses renewable energy sources may be awarded 'eligible producer status'. This status gives producers of renewable energy the right to a feed-in tariff where the market operator pays for the purchase of power. Eligible producer status is regulated by the Regulation on Gaining of Eligible Producer Status (Official Gazette No. 132/13, 81/14, 93/14), while generation of renewable energies is outlined in the Regulation on Renewable Energies and Combined Heat and Power (Official Gazette No. 88/12).

6 Climate change

What impact will government policy on climate change have on the types of resources that are used to meet electricity demand and on the cost and amount of power that is consumed?

Environmental protection has a great impact on Croatia's policy in the electricity sector, as outlined in the Strategy. In this regard, Croatia encourages the use of natural gas and renewable energy sources, while in the future it plans to accept nuclear and hydrogen technology only if the aforementioned technologies prove to be safe and acceptable to the environment. Renewables are not only encouraged because they are less harmful energy sources and better for the environment, but also because national fossil energy sources are insufficient for the steady increase in electricity demand. Furthermore, Croatia has natural potential for the production of 'green energy'.

Generally speaking, because Croatia is an importer of energy, the use of renewable energy sources causes an increase in generation costs and, consequently, electricity prices.

7 Government policy

Does government policy encourage or discourage development of new nuclear power plants? How?

Croatia does not have nuclear power plants on its territory; however, HEP is a co-owner of Krško nuclear plant in Slovenia. Although Croatia recognises the need for nuclear energy and has adopted a nuclear energy programme outlined in the Strategy, construction of nuclear power plant is a hot topic in the country.

The greatest concern in construction of a new nuclear plant is its influence on the environment. To this date, the government has still not approved any nuclear energy construction projects.

Regulation of electricity utilities – transmission

8 Authorisations to construct and operate transmission networks

What authorisations are required to construct and operate transmission networks?

The national transmission networks are owned and operated by the national transmission system operator, HOPS (see question 2). Since electricity transmission is a regulated, non-market activity, HOPS, has the sole power to construct and operate transmission networks.

In accordance with the new Electricity Market Act, HOPS, with prior approval from HERA, has to pass a 10-year transmission system development and construction plan. The plan has to implement measures to guarantee enough capacity and security of supply.

HOPS was granted a licence for electricity transmission activities, issued by HERA.

9 Eligibility to obtain transmission services

Who is eligible to obtain transmission services and what requirements must be met to obtain access?

Pursuant to the Electricity Market Act, HOPS must provide non-discriminatory access to the transmission grid to all grid users, based on the regulated third-party access regime, in accordance with the General Conditions for Electricity Supply and the Grid Code. To obtain access to the transmission grid, new generators and customers are obliged to obtain consent from HOPS to connect to the grid. HOPS may deny access only in the case of limited technical or operating capabilities of the grid, undergoing maintenance works or in case of danger to the human lives or assets. Any new generator or customer whose access to the grid is denied may appeal against the HOPS's decision to HERA. HERA's decision is final, but the unsatisfied party may file a claim with the competent administrative court.

10 Government incentives

Are there any government incentives to encourage expansion of the transmission grid?

According to the Strategy, Croatia has a transmission grid that is more than 7,000km long. There are no government incentives to encourage expansion of the transmission grid.

11 Rates and terms for transmission services

Who determines the rates and terms for the provision of transmission services and what legal standard does that entity apply?

Transmission services rates are set by the Croatian government based on the Tariff System for Electricity Transmission, Rates Excluded (Official Gazette Nos. 143/06, 26/10) (the tariff system).

The tariff system was rendered by HERA and outlines basic principles and methods for calculating rates for electricity transmission. It adopts a rate-of-return method and 'post-stamp' principle meaning that the price per unit of electricity transmitted is fixed and all-inclusive.

The current rates are set by the government's decision of 27 April 2012 and are applicable from 1 May 2012.

12 Entities responsible for assuring reliability

Which entities are responsible for assuring reliability of the transmission grid and what are their powers and responsibilities?

HOPS is responsible for the reliability of the transmission grid, as the sole TSO in Croatia with the licence to carry out electricity transmission as a public service (see question 2). HOPS's main responsibility is to transmit electricity and to maintain and develop the transmission network for the purpose of the reliable supply of electricity for customers at the lowest cost and the protection of the environment.

The maintenance of the transmission network includes maintenance of overhead lines and underground cables, primary and secondary equipment, auxiliary plants, telecommunications equipment and building structures in substations and switchyards.

Regulation of electricity utilities – distribution

13 Authorisation to construct and operate distribution networks
What authorisations are required to construct and operate distribution networks?

Croatian distribution networks are owned, constructed and operated by HEP-DSO. Since distribution is also a regulated energy activity, all principles that apply to the transmission network also apply to the distribution network (see question 8).

14 Access to the distribution grid
Who is eligible to obtain access to the distribution grid and what requirements must be met to obtain access?

The regulated third-party access regime that applies to the transmission grid also applies to access to the distribution grid. Therefore, the same rules applicable to access to the transmission grid also apply to the access to distribution grid (see question 9).

15 Rates and terms for distribution services
Who determines the rates or terms for the provision of distribution services and what legal standard does that entity apply?

Rates for distribution services are set by the Croatian government under the same terms and conditions as in relation to transmission services (see question 11).

The relevant by-law regulating the tariff system for electricity distribution is also set by HERA in a Tariff System for Electricity Distribution, Rates Excluded (Official Gazette Nos. 143/06, 26/10) and is based on the same principles as for transmission services (see question 11). The current rates are set by the government's decision of 27 April 2012 and are applicable from 1 May 2012.

Regulation of electricity utilities – sales of power

16 Approval to sell power
What authorisations are required for the sale of power to customers and which authorities grant such approvals?

Sale of power to final customers (supply) may be regulated (public service) or market activity. Supply of power under regulated terms is performed as universal service (to households) or as a last resort service (to entrepreneurs).

Both types of suppliers (regulated and market) have to obtain their energy licences for supply of power to customers from HERA. In addition, a supplier under regulated terms is awarded a public service obligation by the government's decision.

17 Power sales tariffs
Is there any tariff or other regulation regarding power sales?

Croatia's power sales market has been fully open since 1 July 2008, meaning that all customers have acquired 'eligible customer status'. This means that all customers have the legal right to choose their electricity supplier and freely contract the quantity and price of the supplied electricity.

Tariffs are regulated only with respect to supply of electricity as universal service and as a last resort service (see question 16). Power sales tariffs are set by the following regulations rendered by HERA: Methodology for Calculation of Tariffs for Electricity Supply as Universal Service (Official Gazette No. 116/13, 38/14), Methodology for Calculation of Tariffs for Electricity Supply as Last Resort Service (Official Gazette No. 158/13) and Decision on Tariffs for Last Resort Electricity Supply (Official Gazette No. 73/14).

Even though the market is opened and competitors offer lower prices, a majority of customers have still not chosen their supplier and are still supplied by HEP-ODS (Last Resort Supplier). In order to encourage customers to choose their market supplier, based on the aforementioned methodologies and tariffs, entrepreneurs supplied by HEP-ODS pay 20–50 per cent higher prices as of 1 July 2014.

18 Rates for wholesale of power
Who determines the rates for sales of wholesale power and what standard does that entity apply?

Croatia does not regulate rates for sales of wholesale power; it is a market activity and all prices are freely negotiated. HEP dd is negotiating power wholesale rates with other electricity companies in the region through tenders.

19 Public service obligations
To what extent are electricity utilities that sell power subject to public service obligations?

Public service obligations exist with regard to household customers who opted for or automatically use universal service and as a last resort supply, (ie, in the event of failure of the electricity supplier).

HEP-ODS d.o.o is nominated as the universal service and last resort supplier.

Regulatory authorities

20 Policy setting
Which authorities determine regulatory policy with respect to the electricity sector?

The regulatory policy with respect to the electricity sector is determined by the Ministry and to a certain extent by HERA. HERA is both a regulatory and supervisory body.

21 Scope of authority
What is the scope of each regulator's authority?

The Ministry prepares strategy and legislation with respect to the electricity sector and implements electricity laws enacted by the Croatian parliament. The Ministry also enacts different electricity by-laws and regulations. Furthermore, it supervises and reviews economic measures affecting the status of electricity undertakings, carries out activities relating to the construction of electricity facilities, proposes measures for the efficient organisation of electricity activities, etc.

HERA is a partially regulatory and partially supervisory body (see question 20). As a regulatory body, HERA grants different licences for the performance of energy activities, participates in electricity policy design, approves investment plans and various general acts rendered by electricity undertakings, renders or approves tariff systems, etc. As supervisory body, it supervises the performance of different energy activities (generation, transmission, distribution, supply of electricity and the organisation of the electricity market), the quality of services provided by energy undertakings, unbundling process, the application of all tariff systems, the degree of transparency of market competition, etc.

22 Establishment of regulators
How is each regulator established and to what extent is it considered to be independent of the regulated business and of governmental officials?

The Ministry, as a government body, is independent of the electricity business and industry. However, in the process of preparation of electricity legislation, the Ministry follows and accepts proposals from electricity specialists.

HERA is an independent, non-profit institution established to regulate energy activities, and was founded in accordance with the Energy Activities Regulations Act. HERA is also independent from the electricity industry since members of the HERA Management Board (and members of their family) cannot be owners of any company in the energy business or perform any other activity in that sector that may lead to a conflict of interest. They are also independent of government officials since they cannot be members of Parliament, members of local representative bodies or of the political parties' main bodies.

23 Challenge and appeal of decisions

To what extent can decisions of the regulator be challenged or appealed, and to whom? What are the grounds and procedures for appeal?

HERA's decisions are either final or appealable to the Ministry, depending on the matter in question. If HERA's decision is final, it can only be challenged before competent administrative court. The Ministry's Appellate Decision can also be challenged before competent administrative court.

The Ministry's decisions are usually final. If the decision is final, it can only be challenged before a competent administrative court. Exceptionally, if it is provided by the law, the Ministry's decisions may be appealed back to the same Ministry, but also to the Appeal Senate as the second instance authority.

Acquisition and merger control - competition

24 Responsible bodies

Which bodies have the authority to approve or block mergers or other changes in control over businesses in the sector or acquisition of utility assets?

The Croatian Competition Agency (CCA) and Croatian Financial Services Supervisory Agency (HANFA) are responsible for acquisition and merger control in general, including the electricity sector (see question 25). HERA controls the eligibility of parties participating in acquisitions and applies a system of measures for protection of market competition (see question 26).

25 Review of transfers of control

What criteria and procedures apply with respect to the review of mergers, acquisitions and other transfers of control? How long does it typically take to obtain a decision approving or blocking the transaction?

Procedures, criteria and time limits for review of transfers of control are set out in the Competition Act (Official Gazette Nos. 79/2009 and 80/13) and the Act on the Takeover of Joint-stock Companies (Official Gazette Nos. 109/07, 36/2009, 108/12, 90/13, 99/13 and 148/13).

Pursuant to the Competition Act, the review procedure is performed by the CCA and European Commission. The procedure is initiated ex officio or upon the initiative of any natural or legal person, association the government or governmental and administrative bodies. Upon carrying out the procedure provided for by the Competition Act, the CCA issues a decision by which it either approves or refuses a transaction.

The CCA will block a transaction in the case of a prohibited concentration, referring to those undertakings that can significantly influence the prevention, restriction or distortion of competition. The CCA should issue a decree within three to eight months of the day the proceeding was initiated, depending on the type and complexity of the case in hand.

HANFA supervises the takeover of joint-stock companies and the application of the Act on the Takeover of Joint-stock Companies. If takeover irregularities are identified, HANFA may impose measures provided for by law such as declaring the takeover bid invalid or to instructing revision, supplementation or withdrawal of the takeover bid.

26 Prevention and prosecution of anti-competitive practices

Which authorities have the power to prevent or prosecute anti-competitive or manipulative practices in the electricity sector?

HERA supervises, inter alia, the degree of transparency and market competition between electricity undertakings. In case of possible anti-competitive or manipulative practices, HERA has the obligation to notify, cooperate with and assist the CCA. The CCA is authorised to impose measures prescribed by the Competition Act for removal of the adverse effects of such practices. For severe infringement of the provisions of the Competition Act, the CCA may fine the undertaking up to 10 per cent of the past year's total income.

27 Determination of anti-competitive conduct

What substantive standards are applied to determine whether conduct is anti-competitive or manipulative?

There are no specific criteria that apply to the energy sector that define 'anti-competitive' or 'manipulative' conduct. Regulated energy activities are regulated on the principles of transparency, objectivity and non-discrimination, while market energy activities are regulated according to the principles of market competition. Therefore, the Competition Act applies to market energy activities. The Competition Act prohibits entering into agreements that directly or indirectly fix purchase or selling prices or any other trading conditions, limit or control the market, share markets or sources of supply, etc. Furthermore, abuse of a dominant market position is also prohibited, as well as concentration of undertakings.

28 Preclusion and remedy of anti-competitive practices

What authority does the regulator (or regulators) have to preclude or remedy anti-competitive or manipulative practices?

HERA has the power to withdraw licences for the performance of energy activities, for instance, if the supplier under public obligation does not apply the prices set by the tariff system. Furthermore, HERA has the power to request the HOPS or HEP-DSO to change its conditions and rules if it is necessary to ensure their non-discriminatory application. HERA also issues other legally binding decisions in accordance with the law.

The Electricity Market Act prescribes fines for any misconduct, including anti-competitive or manipulative practices (for instance, if the HOPS or HEP-DSO unlawfully denies access to the transmission grid). The fines are imposed by the Ministry. In the case of recidivism, energy undertakings may be suspended from carrying out licensed activities for up to a year. The Electricity Market Act prescribes that a TSO or DSO may be fined up to 10 per cent of its total past year's income in the case of international discrimination of grid users.

According to competition law, the CCA issues legally binding decisions by which it prohibits anti-competitive conduct. Finally, the CCA is authorised to instigate misdemeanour court proceedings in the case of violation of the Competition Act.

HANFA is also authorised to instigate misdemeanour court proceedings in case of takeover irregularities.

International

29 Acquisitions by foreign companies

Are there any special requirements or limitations on acquisitions of interests in the electricity sector by foreign companies?

There are no special requirements or limitations in the electricity sector regarding acquisitions by foreign companies.

The only limitation concerns privatisation of HEP. Namely, the government may sell HEP's shares only in accordance with Croatian privatisation acts that regulate the privatisation procedure, control mechanisms, a portion of shares that may be sold on the capital market, etc.

30 Cross-border electricity supply

What rules apply to cross-border electricity supply, especially interconnection issues?

Pursuant to the Electricity Market Act, cross-border electricity supply is governed by international agreements binding upon the Republic of Croatia. The HOPS must carry out the transit of electricity through the transmission network according to the terms and conditions stipulated in those agreements, and the technical capacity of interconnections.

Croatia has been a party to the treaty establishing the Energy Community since 1 July 2006. The treaty abolishes customs duties and quantity restrictions and creates a legal and institutional framework for a free transport and trade in electricity and gas. It also allows a single mechanism to be created for cross-border transmission or transport of interconnected energy for the whole of Europe. This treaty enabled Croatia to become part of the European energy market.

Based on the Energy Community treaty, the HOPS has adopted the Rules on Allocation and Use of Cross-border Transfer Capacities.

Update and trends

Strategic Investments Act (Official Gazette No. 133/13) was passed in October 2013 with the aim of encouraging new investments and helping the recovery of the Croatian economy. The purpose of the act is to give preferential treatment to investment projects of national interest, in particular energy projects. The threshold for the investment is 150 million kuna for it to be eligible for strategic project status. On the grounds of the Strategic Investment Act, the government awarded coal-fired Plomin C power plant project (500MW capacity, with planned annual production of 3.6TWh) strategic investment project status. The project value is estimated at €800 million and it will be co-financed by the strategic partners and HEP. Approximately 25 per cent of Croatia's annual electricity needs are expected to be met by electricity produced from Plomin C power plant. The strategic project status should ensure the Plomin C project is delivered and will facilitate respective administrative proceedings.

Another HEP strategic project is the construction of the Kosinj/Senj hydropower plant (380MW capacity). The estimated project value

is €600 million. In August 2014, HEP announced an invitation for expression of interest for participation in the project as strategic partner on a design-build-operate-transfer basis for a period of up to 30 years. The deadline for submission of expressions of interests is 18 December 2014. This is expected to be one of the most complex but highly profitable energy projects in Croatia.

Croatia changed its energy policy with respect to renewables. Namely, in recent years incentives for construction of wind farms were quite high, however the benefits were not gained by the Croatian economy but by industries from other countries from which wind farm equipment originated. Therefore, the government shifted its focus to energy production from biomass, biogas, cogeneration plants and small hydro power plants, which should have a bigger impact on the Croatian economy and will supposedly create 10 times more jobs than wind farm construction.

Transactions between affiliates

31 Restrictions

What restrictions exist on transactions between electricity utilities and their affiliates?

Under the Electricity Market Act, all commercial and financial transactions between the parent company (HEP dd) and HOPS (including loans), have to be made in accordance with market conditions. HERA is authorised to approve or deny each transaction.

With respect to HEP-DSO, HEP dd as the parent company approves annual financial plans and sets the limits of their possible debt, but cannot

give instructions relating to their everyday operation. Cross-subsidisation of companies engaged in regulated activities and those engaged in market activities, and cross-subsidisation of activities within the same company is prohibited by the Electricity Market Act.

32 Enforcement and sanctions

Who enforces the restrictions on utilities dealing with affiliates and what are the sanctions for non-compliance?

For serious breaches of unbundling rules, misdemeanour proceedings may be initiated and a fine imposed. HERA supervises all activities mentioned in question 31 and may demand their implementation.



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