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Competition in Energy Markets – Note by Lithuania

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Ms Federica MAIORANO
[Email: Federica.MAIORANO@oecd.org]

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Lithuania

1. Introduction

1. The Note overviews ongoing liberalisation of the electricity supply market in Lithuania and relevant competition advocacy by the Lithuanian Competition Council. It shows the importance of respecting competition protection principles while opening customers' data to potential new independent electricity suppliers, questions the proportionality and usefulness of postponing market liberalisation due to tensions in international and regional energy markets as well as events in the Lithuanian independent retail electricity supply market. Finally, it highlights the remaining competition challenges when proceeding with national electricity market liberalisation, especially those linked to unprecedented rise in electricity prices.

2. Liberalisation of the Electricity Supply Market in Lithuania

2. Liberalisation of the electricity market is one of Lithuania's European Union commitments. Most countries in the European Union and the Northern European region in which Lithuania also participates in the electricity market¹ have already liberalised the electricity supply market for household consumers. Before the market liberalisation all household consumers purchased electricity from an incumbent public supplier *Ignitis*, and the price of electricity was set by the National Energy Regulatory Council. Several years ago, the regulation of retail electricity prices for non-household (business) consumers was abandoned.

3. In 2020, amendments to the Lithuanian Law on Electricity² providing that the transition from regulated to competitive electricity supply for household consumers would be implemented in three stages by 2023 were adopted. After implementing liberalisation processes, the purchase and supply price of electricity would no longer be regulated. The other part of the price – electricity transmission, distribution and public service obligation services – would continue to be regulated.

4. It was planned that regulation of the final electricity price would be abandoned in three stages:

- During the stage I – ending 31 December 2020 – for the consumers who used the most electricity, i. e. for those who consumed more than 5,000 kWh per year. There were approximately 90,000 such consumers, which accounted for 5 %.
- During the stage II – ending 31 December 2021 – for all household consumers with an annual electricity consumption of more than 1,000 kWh. There were approximately 720,000 such consumers, which accounted for 43 %.

¹ Together with Norway, Denmark, Finland, Sweden, Estonia, Latvia, United Kingdom and Germany.

² Law on Amending the Republic of Lithuania Law on Electricity No. VIII-1881 Articles 2, 7, 9, 38, 39, 40, 41, 42, 43, 44, 46, 47, 49, 51, 52, 59, 60, 61, 67 and 68.

- During the stage III – ending 31 December 2022 – for those consumers who consume less than 1,000 kWh per year as well as vulnerable electricity consumers. There were approximately 870,000 such consumers, which accounted for 52 %.

5. Regardless of the stages proposed, consumers would also be able to choose an independent supplier at their own discretion at an earlier date. In addition, it was established that guaranteed supply by electricity distribution grid operator *ESO* would be provided to consumers who did not choose an independent electricity supplier within the said deadlines or if their chosen independent supplier has failed to fulfil its obligations. In such a case, 25 % higher electricity tariff would be applied in comparison with that offered by the Nord Pool power exchange³. Such measure was intended to incentivise consumers to opt for an independent supplier in due time.

3. Respecting Effective Competition while Opening Customers' Data

6. Throughout the electricity market liberalisation process, the Lithuanian Law on Electricity⁴ obliged the public supplier *Ignitis* to inform household consumers, at specified stages, of the termination of public service and of their obligation to choose an independent supplier within a certain time period. *Ignitis* was under the obligation to inform the electricity distribution grid operator *ESO* of the customers for whom the termination of the electricity supply was envisaged. Then, *ESO* had to transfer the collected customers' data to independent electricity suppliers in order to enable them to submit commercial offers to their potential customers.

7. After customers' data for stage I had already been opened to independent suppliers, the Lithuanian Ministry of Energy initiated amendments to the Lithuanian Law on Electricity, suggesting that customers' data for stages II and III should not be opened in separate stages of liberalisation, as had been the case so far. Data of all those customers (including those having guaranteed supply) should have been available to independent suppliers at the beginning of stage II. Earlier and wider access to customers' data was expected to increase competitiveness in the electricity supply market and allow consumers to assess different offers of new market entrants.

8. In this context, the Lithuanian Competition Council recommended⁵ to add to the Law on Electricity provisions on the opening of the electricity supply market to be carried out ensuring effective competition. The Lithuanian Competition Council suggested to:

- separate the activities of the public supplier in the performance of its functions as a public supplier from its functions as an independent electricity supplier;
- require the independent supplier, which was separated from the public supplier, to act on an equal basis with the other independent suppliers, i.e. it should not invite/incentivise consumers to enter into contracts with it until the date of opening of customers' data to all suppliers;

³ According to the Article 44(2)(3) of the Lithuanian Law on Electricity an additional coefficient of 1.25 to the average electricity exchange price in the previous reference month was applicable for the Lithuanian price zone.

⁴ Article 43

⁵ The Lithuanian Competition Council's conclusion No. (2.30Mr-43)6V-331, as of 18 March 2021.

- establish that all suppliers, without any exception, may enter into contracts with customers from the date of opening of customers' data;
- provide for the mechanism of supervision of electricity market liberalisation processes enabling to solve arising issues and disputes between economic operators and assign the relevant functions to the National Energy Regulatory Council.

9. The Competition Council emphasised that during the opening of the electricity supply market, it was important to ensure effective competition between electricity suppliers. It was important to keep in mind that the incumbent public supplier *Ignitis*, which continued performing its statutory duties as a public supplier, in parallel also acted as an independent electricity supplier. Because of this dual role, it had the possibility to use the data of electricity consumers and reach out to them, for example, by sending direct information messages regarding new contracts, before its competitors were able to do that.

10. The Competition Council's view was that, during a period when customers' data had not yet been opened to all suppliers, the incumbent public supplier should not take advantage and encourage consumers, either directly or indirectly, to choose it as an independent supplier. If customers' data would become available to *Ignitis* acting as an independent electricity supplier prior to any other independent supplier, there could be a risk that consumers might enter into contracts with it even before new market entrants acquired the right to submit their offers to potential customers.

11. So, the Lithuanian Competition Council drew the attention of the policy makers to the necessity to ensure that the regulation of economic activities in the electricity supply market was objective, non-discriminatory and proportionate. It therefore emphasised that it was important to create a level playing field for all independent electricity suppliers (incumbent as well as new ones), that participated in market liberalisation, including equal terms on using information, which was essential for the start of commercial electricity supply.

12. The lawmakers made efforts to improve regulation on electricity market liberalisation considering issues raised by the Lithuanian Competition Council. On the one hand, a legally separate entity from the public supplier *Ignitis* for the independent electricity supply was not established. Furthermore, the National Energy Regulatory Council was not assigned with the supervision of electricity market liberalisation. However, fair opening of customers' data and equal terms for all independent electricity suppliers on using such information was ensured. According to the Council's internal cost-benefit analysis, such respect to effective competition principles generated approx. 600.000 Eur expected benefit to consumers during stage II, and approx. 180.000 Eur – during stage III.

4. Effect on Competition of Postponing the Electricity Supply Market Liberalisation

13. At the end of stage II of the electricity market liberalisation, only 33 % of the relevant household consumers had opted for an independent supplier. Decision makers assessed that such inactivity could cause a tense situation when many household consumers, who had not yet chosen an independent supplier, would rush to make their choices at a risk of irrational decisions. Meanwhile, independent suppliers would not be able to guarantee quality services to a large number of customers seeking to enter into contracts at the same time.

14. It was obvious that all stage II household consumers would not succeed in choosing their independent supplier on time by the end of 2021 and would therefore be eligible for a guaranteed supply. At that time, the guaranteed supply price for such consumers was

already higher than it was used to be, as it increased by more than 65 % compared to the first half of the year 2021. It remarkably elevated due to the recent increase in price on the Nord Pool power exchange (from EUR 54/MWh (in January 2021) to EUR 124/MWh (in September 2021)) and the application of an additional coefficient of 1.25 to the average electricity exchange price in the previous reference month applicable for the Lithuanian price zone.

15. In order to mitigate the significant rise in electricity prices for household consumers, the legislators decided to extend the deadline for stage II by half a year. This meant that residents who had not yet chosen an independent supplier could do so until 1 July 2022 instead of 1 January 2022. Such extension of the deadline was intended to avoid the potential ‘bottle neck’ effect and to reduce the number of consumers entering the high price guaranteed supply.

16. Halfway through stage III of the electricity market liberalisation, around 53 % of the relevant household consumers had not yet opted for an independent supplier. Yet another surge of electricity wholesale prices in 2022, mainly linked to the rise in the price of natural gas and the ongoing war in Ukraine, complicated the situation. The price of electricity on the Nord Pool power exchange increased from EUR 223/MWh (in June 2022) to EUR 480/MWh (in August 2022). A new market entrant *Perlas Energija* could not withstand such pressure and withdrew from the market abandoning around 180 000 customers who had chosen it as their independent electricity supplier.

17. The stage III covered consumers who consumed less than 1,000 kWh per year as well as vulnerable electricity consumers⁶, including elderly ones. Due to difficult situation in the energy markets, the choice of an independent electricity supplier at the end of stage III would be extremely unfavourable for vulnerable consumers. They would potentially pay a higher electricity price than household consumers from stages I and II.

18. Considering the situation in international and regional energy markets, the recent events in the Lithuanian independent retail electricity supply market and seeking to safeguard essential public and state interests, avoid significant increase in electricity prices for the stage III household consumers, the Lithuanian Government decided to urgently amend existing legal framework. Supplementing the previously adopted measure on electricity subsidies for household consumers⁷, it proposed to extend the deadline of the electricity market liberalisation stage III by three years.

19. Consequently, the public supply of electricity to stage III household consumers would be terminated not by 1 January 2023, but by 1 January 2026. In this way, according to the decision makers, stage III household consumers allegedly could choose the independent electricity supplier most suited to their needs without a hurry and when ready to do so. The delayed electricity market liberalisation would also allow for additional time to generate more renewable energy in Lithuania and better forecast electricity production prices in the future.

⁶ Vulnerable electricity consumer means a household electricity consumer who receives and/or has a right to receive monetary social assistance in accordance with the Lithuania Law on Cash Social Assistance for Low-Income Families (Single Residents) and who is entitled to benefit from the additional guarantees for vulnerable consumers.

⁷ On 30 May 2022 the Lithuanian Government approved the scheme (in place from July 2022 through December 2022), which provided for covering up to 9 euro cents per kWh for electricity. The minimum standard electricity tariff below which the cost of electricity would not be subsidized was set at 24 cents per kWh.

20. The Lithuanian Competition Council opposed the postponement of the electricity market liberalisation of both stages, II and III⁸. The Lithuanian Competition Council questioned the proportionality of such decisions and stressed their inherent risks. The delay of stages II and III of the electricity market liberalisation could increase uncertainty for existing and potential independent electricity suppliers which planned their activities in view of the fact that the liberalisation stages would take place on pre-defined dates. The postponement of those dates might cause operational difficulties for them, as independent suppliers could be chosen by a smaller number of consumers than they would have been in case the liberalisation would not have been delayed. So, the relevant legislative changes might render retail electricity supply activities less attractive, less predictable and riskier for independent suppliers.

21. In addition, the incumbent public supplier *Ignitis* (also acting as an independent supplier) might have been treated more favourably than competing independent suppliers, if its activities as a public supplier were extended until 1 January 2026. That might strengthen impression to consumers that *Ignitis* was a more reliable independent supplier than emerging new competitors. Accordingly, consumers would be more likely to choose incumbent *Ignitis* as their independent electricity supplier.

22. Such factors altogether, might reduce incentives for new independent electricity suppliers to engage in this activity, and might encourage existing new market participants to consider suspending their activities. Finally, it might lead to a reduced number of operators on the market, less effective competition between them, less incentives to innovate and offer electricity prices to consumers at the lowest possible level.

23. In the long run, the opposite effects could be reached from those expected by the Government as it is effective competition in markets that usually leads to lower prices for goods and services and stimulates innovation and progress. Nevertheless, the lawmakers did not take into account the concerns raised by the Lithuanian Competition Council's deciding to postpone stages II and III of the electricity market liberalisation.

5. Remaining Competition Challenges throughout the Electricity Supply Market Liberalisation

24. Amid stage III of the electricity market liberalisation, there were 6 independent suppliers acting on the Lithuanian retail electricity supply market. About 67 % of the relevant market share belonged to the former Lithuanian public supplier *Ignitis* now acting as an independent supplier; 14 % — to the new market entrant *Perlas energija*; 8.5 % — to *Enefit* of Estonian state capital; 9 % — to *Elektrum Lithuania* of Latvian state capital. The remaining insignificant market share was distributed among *EGTO* and *Birstonas Elektra*. So, there was a significant concentration in the market, as a single market participant accumulated almost 70 % of all electricity consumers. The factual situation showed that it was difficult for new and smaller independent electricity suppliers to compete with large Lithuanian, Latvian and Estonian state capital companies operating in the market. Sudden withdrawal of the new market participant *Perlas energija* had evidenced that.

25. Recent unprecedented rise in electricity prices also complicated Lithuanian electricity market liberalisation process. Price surge was determined by a complex of

⁸ The Lithuanian Competition Council's conclusions No. (2.30Mr-43)6V-1400, as of 7 October 2021 and No. (2.30Mr-43)6V-1155, as of 12 September 2022.

reasons: sanctions imposed on Russia over the war in Ukraine⁹, declining electricity supply across the region, hot and dry weather, unfilled water reservoirs, rising prices of gas and emission allowances, insufficient green production, algorithms applied by Nord Pool power exchange¹⁰.

26. Obviously, at the beginning of electricity market liberalisation, smaller electricity suppliers face challenges in competing with large former incumbent state-owned enterprises already well established in the market. However, from the competition point of view, in the longer term the continuation of market liberalisation should change the situation by increasing the number of competitors. While major independent electricity suppliers are state-owned, different companies will still compete on the market and consumers should benefit from competition. Of course, it would be desirable to see more private operators without state share ownership entering the market. But the sector is quite specific and has traditionally not had a large number of private actors in the European markets¹¹.

27. In fact, current circumstances might not be the most favourable to the emergence of new market participants, as the crisis in the energy sector and the exit of the new market participant *Perlas Energija* significantly discourage market entry. Nonetheless, once the situation has stabilised, it is likely that more new market players could emerge, especially, if they don't face unjustified market entry barriers. It is important now to increase competition in the liberalised electricity market in the hope that competition will play its part and eventually electricity prices will decrease. Current situation already demonstrates the benefits to consumers of implementing electricity supply market liberalization stages I and II, as they pay considerably lower electricity price to their chosen independent suppliers compared to that, which is now being charged by *Ignitis* as the public supplier.

28. There is certain role for the Lithuanian competition authority in the current situation. First, if there were appropriate grounds for that, it would consider launching an investigation into actions of the dominant independent electricity suppliers operating in Lithuania, in case of alleged violation of competition rules leading to higher electricity prices for consumers¹².

29. The Lithuanian Competition Council could also open an investigation if there were allegations that independent suppliers entered into anti-competitive agreements in order to maintain high electricity prices¹³.

30. Another tool available to the Lithuanian Competition Council is the assessment of draft legal acts and existing legislation regarding their impact on competition. After identifying unjustified negative effects on competition, the competition authority can suggest lawmakers to revise drafts or regulation in force in order to eliminate or reduce

⁹ The recent European Commission Quarterly Report On European Electricity Markets illustrates, how international sanctions against Russia and the fear of power supply interruptions have affected electricity prices that have reached historical highs across the European Union.

¹⁰ During the Nord Pool auction for electricity delivery on 17 August 2022 the max price of 4000 Euros was reached in hour 18 in Estonia, Latvia and Lithuania.

¹¹ ELTA: „Konkurencijos tarybos pirmininkas: dar anksti pasakyti, ar vartotojai pajus elektros rinkos liberalizavimo naudą“ / eng. „The Chairman of the (Lithuanian) Competition Council: it is too early to say whether consumers will benefit from the electricity market liberalisation“.

¹² Under Articles 7 and 18(1)(5) of the Lithuanian Law on Competition.

¹³ On the basis of Articles 5 and 18(1)(5) of the Lithuanian Competition Law.

negative impact¹⁴. The Competition Council also performs expert examination concerning state support measures subject to the European Union State aid rules, submits conclusions and recommendations to State aid providers¹⁵.

31. Although in some cases prices may increase as a result of cartels, abuse of a dominant position or restrictions of competition caused by too stringent regulation, in general, price growth is caused by a combination of various different market factors which cannot be directly influenced by the Lithuanian Competition Council.

¹⁴ See Article 18(1)(3)&(7)&(8) of the Lithuanian Competition Law.

¹⁵ See Article 45(1)&(2) of the Lithuanian Competition Law.