

# The Affordability of Energy: How Much Protection for the Vulnerable Consumers?

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**Abstract** Affordability is a new “alien” concept penetrating the field of contract and consumer law as one of the obligations related to the provision of “universal services” or “public service” in the context of services of general economic interest. Affordability becomes an important element of the *European social model* (using Scharf’s terminology; Scharf, J Common Mark Stud 40:645–670, 2002) and its constitutional dimension will be confirmed by the Treaty of Lisbon and the Charter of Fundamental Rights of the European Union (EU). The major European Commission policy tool for ensuring the Affordability of Energy Supply is, on the one hand, functioning competition, which should bring about reasonable prices in general, and on the other hand, regulation targeted at so-called vulnerable consumers. First tested in the UK, it was later spread mainly by the requirements of the Second Energy Package in other Member States (MS). The Third Energy Package (to be implemented by March 2011) further develops this idea and clarifies the set of obligations that the protection of consumers and ensuring the Affordability of Energy Supply require in the understanding of the EU legislator. One could speculate to what extent this is a reaction to the fact that some MS and, in particular, the new MS did not implement the consumer protection requirements of the Second Energy Package, but rather opted for very different regulatory strategies. This paper will examine different regulatory strategies employed in four MS (the UK, France, the Czech Republic, and Slovakia), with special focus on the situation in the two new MS, in order to respond to the question as to whether these different regulatory strategies provide what is promised, i.e., affordable energy for all.

**Keywords** Affordability · Vulnerable consumers · Universal service · Services of general economic interest · Energy markets

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## Introduction

Two major goals of the liberalization of the energy sector are, on the one hand, the creation of market and competition and, on the other hand, the wide provision of this important service of general economic interest (SGEI)—for the important societal functions it fulfils. Achieving either of these goals seems to imply ever-increasing regulation. This development was not anticipated (by many) at the beginning of liberalization; on the contrary, privatization and deregulation in the 1980s and 1990s was driven by a belief in the withdrawal of “inefficient” state structures and belief in free competition in utilities markets, which would finally lead to complete deregulation. However, ever-increasing regulation indicates that these expectations were inaccurate (McRobb and Prosser 2000, pp. 63–64).

Both the European Union (EU) institutions<sup>1</sup> as well as numerous scholars (Grenfell 1999; McCrudden 1999; Prosser 2005) further the idea that, even if the energy market were strongly competitive, there would still be a place for regulation: in particular, for ensuring the protection of consumer interests, i.e., ensuring the access, affordability, quality, and continuity of energy supply. The empirical research that we have undertaken here shows that this contention is to a large extent true.

The EU has been the motor of the liberalization of the energy sector in all the Member States (MS; Rott 2007, p. 50) apart from the UK, Norway, Sweden, and Finland, who are considered the pioneers in the liberalization of utilities sectors (Bellantuono and Boffa 2007, pp. 52–60).<sup>2</sup> The EU liberalization strategy thus builds<sup>3</sup> on the relatively successful UK liberalization experience (more in electricity than in gas though; Grenfell 1999, p. 222), complemented by the French concept of *service public*, based on the principles of continuity, equality, and adaptability (Micklitz and Keßler 2008, p. 142). The term *universal service* was “borrowed” from telecommunication sector where it served as one of the standard justifications for the monopoly structure of the market in a number of countries, including the USA (Loube 2002, p. 226).

EU energy policy has several (complementary) objectives. It aims to ensure efficient competition in the enlarging markets (from national markets to regional markets,<sup>4</sup> with the final objective the EU Internal Energy Market). The role for consumers to play is twofold. Not only that an empowered consumer is a precondition for the emergence of strong competition,<sup>5</sup> but that broad consumer protection in the field of SGEI acquires much higher importance. It becomes the right of European citizens, a self-standing objective, which goes in line with more ambitious goals of the EU, namely, the development of a more “human face” or “social face” of Europe (Szyszczak 2001, p. 56). EU energy policy is further complemented with the concern for security and sustainability<sup>6</sup> of energy supply.

The tools for achieving broad consumer protection in the utilities sectors are *Universal Service Obligations*, *Continuity*, *Quality of Service*, *Affordability*, and *User and Consumer Protection*.<sup>7</sup> As already mentioned, these objectives will be raised to a (quasi)constitutional

<sup>1</sup> “There is broad consensus that market mechanisms alone cannot fully ensure consumers’ best interests in the energy sector.” COM (2007a), p. 3.

<sup>2</sup> See also ERGEG (2007), p. 9.

<sup>3</sup> The major components of liberalization of the market (privatization, unbundling, regulation etc.). However, the EU did not follow the UK example to reform “at once,” but it has rather divided the liberalization into several steps, depending on the political support for the liberalization by the MS.

<sup>4</sup> Recital 58 of the Directive 2009/72/EC, of 13 July 2009, concerning common rules for the internal market in electricity and repealing Directive 2003/54/EC (Electricity Directive 2009).

<sup>5</sup> Driver of competition is free choice and consumer switching.

<sup>6</sup> COM (2007b), p. 1.

<sup>7</sup> COM (2003), p. 15.

level by Protocol 23 to the Lisbon Treaty, which requires a high level of Quality, Safety, and Affordability, Equal Treatment, and the promotion of Universal Service Access and of User Rights, and by the Art. 36 of the Charter of Fundamental Rights.<sup>8</sup>

Stepping down from the constitutional level and looking into the European Commission (EC) Secondary Energy Legislation, the Second Energy Package requires the MS to ensure that everyone enjoys:

Universal service, that is, the right to be supplied with electricity of a specified quality within their territory at reasonable, easily and clearly comparable, and transparent prices.<sup>9</sup>

MS shall take appropriate measures to protect final customers and shall, in particular, ensure that there are adequate safeguards to protect vulnerable customers, including measures to help them avoid disconnection.<sup>10</sup>

The Third Energy Package, which is to be implemented by 3 March 2011, develops these obligations in more detail, building also on the experiences of the MS discussed in this paper, and to a great extent, overlapping with the policy recommendations concluding this paper. In short, it requires the MS to:

- define the concept of vulnerable consumer<sup>11</sup> (also in relation to the energy poverty—thus a vulnerable consumer may be an economically weak consumer without higher qualifications);
- prohibit the disconnections of vulnerable consumers in critical times;<sup>12</sup>
- ensure the transparency of contractual terms;<sup>13</sup>
- ensure that an independent dispute settlement mechanism is put in place<sup>14</sup> (the information should be provided with the invoice!);<sup>15</sup>
- ensure a single point of contact for any problems consumers might face.<sup>16</sup>

The Affordability of Energy Supply, that is, the right to universal service for *reasonable prices*, has two dimensions and thus has to be achieved at two complementary levels. Firstly, it is necessary to ensure reasonable prices for all users and, secondly, to ensure the provision of services to the persons who cannot afford it under normal market (or prior monopoly) conditions. The EU policy tries to provide for Affordability of Energy Supply at the first level through ensuring efficient competition and, at the second level, through the protection of so-called vulnerable consumers (Cameron 2005, p. 25) where inspiration clearly comes from the UK. Again, however, the means envisaged by the EU policy makers

<sup>8</sup> European Charter of Fundamental Rights, Art. 36: *Access to services of general economic interest*: The Union recognizes and respects access to services of general economic interest as provided for in national laws and practices, in accordance with the Treaty establishing the European Community, in order to promote the social and territorial cohesion of the Union.

<sup>9</sup> Art. 3(5) of the Directive 2003/54/EC of the European Parliament and the Council, concerning common rules for the internal market in electricity (Electricity Directive 2003). There is no similar requirement in the Gas directive (due to the substitutability of gas by the electricity), and protection is mostly afforded to the consumers who are already connected.

<sup>10</sup> Art. 3(5) of the Electricity Directive 2003, and Art. 3(3) of the Directive 2003/55/EC of the European Parliament and the Council, concerning common rules for the internal market in natural gas (Gas Directive 2003).

<sup>11</sup> Art. 3(7) of the Electricity Directive 2009.

<sup>12</sup> Ibid.

<sup>13</sup> Ibid.

<sup>14</sup> Art. 3(13) of the Electricity Directive 2009.

<sup>15</sup> Art. 3(9) of the Electricity Directive 2009.

<sup>16</sup> Art. 3(12) of the Electricity Directive 2009.

is not uncontroversial and one can attempt to provide for Affordability of Energy Supply in different ways. This paper is an attempt to test several strategies for dealing with the question of the Affordability of Energy Supply, as each of the four countries in focus in this paper has adopted a different set of regulatory strategies for securing it.

However, this paper has no ambition to give full account of different regulatory strategies and their effects on consumers (e.g., the different types of price regulation), but rather to take a close look at these four particular countries and see how the different regulatory strategies have played out *in the field*.

### Which Ways to Ensure the Affordability of Energy Supply?

Affordability is primarily an economic category having to do with the *ability of certain consumers or consumer groups to pay for a minimum level of service*. As Fankhauser and Tepic (2005) stress, the “ability to pay” is distinct from “willingness to pay” (Fankhauser and Tepic 2005, p. 4), which has a clear technical meaning in consumer theory, where it is defined as the amount of income someone is willing to forgo to obtain a certain service. At its simplest, affordability (or the affordability ratio) is defined as the *share of monthly household income (or alternatively expenditure) that is spent on utility services (such as electricity, district heating and water)*.

A household lives in so-called “fuel poverty” if it spends more than a certain part of its income on energy. In the UK, “fuel poverty” is defined by the household expenditure of more than 10% on energy,<sup>17</sup> the EBRD benchmark is 25% of expenditure on all the utilities (Fankhauser and Tepic 2005, p. 5). According to the Commission, more than one third of EU citizens find the energy expensive and, by 2008, more than 20% of people in the UK lived in fuel poverty.<sup>18</sup>

Affordability can be conceptualized as embracing two different goals:

- (a) Reasonable (affordable) prices for all users (General Level).

These can be achieved either through:

- *competition*—the model endorsed by EU energy policy,
- *price regulation*—which is still the case in most of the MS.

- (b) Ensuring the Affordability of Energy Supply for all, including the individuals who cannot afford it under normal market (or even monopoly) conditions (Targeted Level).

These can be addressed through:

- *energy sector-specific measures* (as required by the Second and Third Energy Package, in particular different measures aimed at the protection of vulnerable consumers),
- *general social welfare measures* (unemployment benefits, family support benefits, social assistance, etc.), and/or
- *price regulation* (e.g., social tariffs; but also very anti-competitive price regulatory measures (such as default tariffs) often justified in terms of the protection of vulnerable consumers).

<sup>17</sup> OFGEM (2007b), p. 31.

<sup>18</sup> Presentation of Kyriakos Gialoglou, DG Sanco, on the 2nd Social Forum of the Energy Community held in Zagreb on 14 October 2009. Presentation available at <http://www.energy-community.org/pls/portal/docs/432203.PDF>.

All of the countries examined in this paper adopted a certain combination of general and targeted measures—as we will see, different levels of protection afforded to the disadvantaged consumers (which are the focus of this paper) may be assigned to different combinations of such measures.<sup>19</sup>

### **France: The Price Regulation (Default Tariffs) in Combination with the Regulation Targeted at Vulnerable Consumers**

One of the standard types of price regulation in “liberalized” energy markets is that of default tariffs.<sup>20</sup> Default tariffs are the type where the free market model coexists with price regulation, i.e., certain energy products maintain a regulated price while the other products are priced on the basis of market forces.

The retail energy market in France was fully opened to competition by competing firms on 1 July 2007. The price of energy in the regulated part of the market—the default tariff—is set by the Minister of Economy and Energy<sup>21</sup> (a regulator acts as an advisory body) and should reflect the costs and appropriate profits of the supplier.<sup>22</sup> The only company supplying energy for regulated prices is EDF (electricity) and GAZ France (gas). The regulated tariffs are available to all consumers. Any consumer holding a contract with a regulated price may keep this contract (indefinitely). However, once a consumer concludes a free market contract, s/he can no longer conclude the regulated contract (a concept known as the non-reversibility principle).<sup>23</sup> In addition, any consumer moving into a newly created site (new building) may request a regulated electricity contract until 1 July 2010. The change of proprietor of any site with a regulated contract does not affect the right to continue with the regulated contracts. According to some sources, as of Jan 2007, regulated prices of electricity were 20% lower than the wholesale prices<sup>24</sup> and they continue to be considerably lower than the wholesale price.<sup>25</sup> Given the price trends in electricity markets as well as the 5-year contract between the government and the EDF/GAZ France on raising the price only according to the rate of inflation,<sup>26</sup> the gap between regulated and non-regulated prices can only increase. The situation is slightly different in the gas market where the regulated price is higher than the free market price because it is linked to the fuel price.<sup>27</sup>

The model adopted by France has had an adverse impact on opening the market and developing competition. To begin with, the co-existence of default tariffs and open market prices leads in principle to non-switching.<sup>28</sup> The combination of the non-reversibility

<sup>19</sup> As for the general measures and the general questions regarding comparison of the effects of the price competition, it will not be addressed in this paper.

<sup>20</sup> This is the case in France, Spain, etc. ERGEG (2007), p. 12.

<sup>21</sup> Ibid., p. 31.

<sup>22</sup> See Commission de Regulation de l'énergie (2007). The price setting, however, considerably diverges from the model outlined by that Report to the Commission (ERGEG 2007, p. 16). The last price set is from 2005 and, according to the agreement between the state and the incumbent, it should not rise more than the inflation rate until the following year.

<sup>23</sup> See, e.g., <http://www.energie-info.fr/pratique/comparer-offres#choix> or the country report.

<sup>24</sup> ERGEG (2007), p. 32.

<sup>25</sup> See Commission de Regulation de l'énergie (2008), p. 42.

<sup>26</sup> The incumbent will not rise prices for more than the inflation rate until 2010 (Commission de Regulation de l'énergie 2007, p. 89).

<sup>27</sup> ERGEG (2007), p. 17.

<sup>28</sup> Ibid.

principle (the risk of not being able to switch back if a regulated contract proves to be cheaper), the considerably lower regulated prices (in the case of electricity), the fact that the contract “sticks” to the site indefinitely (implying that such a site in future might have higher value if very cheap energy is secured), the fact that only incumbents provide regulated contracts, and finally, the generally high cost of switching in the (de)regulated markets (similarly Cseres 2006) lead to the complete conservation of the French electricity market. The same is true for the gas market. Even a much lower number of anti-competitive measures would suffice to considerably impede the development of competition.

### Protection of Vulnerable Consumers in France

As the French national report to the ERGEG highlights,<sup>29</sup> it was necessary to adopt additional measures to protect Affordability of Energy Supply for the consumers in precarious situations in order to ensure the Affordability of Energy for all groups of consumers. The first steps were undertaken in 2001 by setting up a system “to preserve or guarantee access to electricity” for people in precarious situations.<sup>30</sup> In 2005, the system was supplemented by the rules governing the procedure applicable to consumers in payment difficulties, introducing thus special procedures for disconnection.<sup>31</sup> Consumers in financial difficulties may benefit from an energy maintenance service as well as from financial assistance with paying invoices and from additional services provided by the housing solidarity fund of the EDF and the Local Distribution Companies.

In 2007, the obligation was introduced not to disconnect the consumers for non-payment from 1 November until 15 March, when the person had benefited from some of the mentioned schemes during the previous 12 months. In 2006, the energy mediator was set up, with the competence to recommend solutions to the disputes between consumers and energy suppliers and to propose changes in consumer protection system.<sup>32</sup>

France has introduced a comprehensive set of rules for the protection of vulnerable consumers, to a large extent corresponding to the requirements of the Third Energy Package. The reason is that price regulation, though setting prices considerably lower than the market price, is in itself not a tool for addressing vulnerable groups of consumers who either do not have enough funds to cover their energy costs or lack “payment discipline;” thus, generally, cheap energy does not necessarily imply that it is affordable for them. On the other hand, one could argue that the same effect might be achievable through general social welfare measures. However, France found it necessary to complement general social welfare by sector-specific regulation as the general social welfare measures were not sufficient to address the needs of vulnerable consumers. This inefficiency of general social welfare measures is also demonstrated by cases in the Czech and Slovak republics (discussed later in this paper).

<sup>29</sup> Commission de Regulation de l’énergie (2006).

<sup>30</sup> Décret no 2001-531 du 20 juin 2001 relatif à l’aide aux personnes en situation de précarité pour préserver ou garantir leur accès à l’électricité.

<sup>31</sup> Décret no 2005-971 du 10 août 2005 relatif à la procédure applicable en cas d’impayés des factures d’électricité. In case of default, the provider is obliged to inform the consumer that in case he does not fulfil his contractual obligations, the level of service may be reduced. The provider informs the consumer that he can apply to the social solidarity fund, and that in case he refuses, the provider will inform the local authorities. Thus, before any reduction of the service, one of the above-mentioned bodies has to discuss the case of the consumer. The time from defaulting the payment until the reduction of the provision of the service is rather lengthy, and in many instances, consumers can apply for help. On no occasion does the decree speak about “termination” or any other equivalent, which means that the consumers cannot be completely deprived of the provision of the service.

<sup>32</sup> Commission de Regulation de l’énergie (2007), p. 88.

To sum up, the regulatory model adopted by France has effectively prohibited competition in the (retail) energy market; this is neither in line with EU energy policy nor in the best interests of the consumers (in the case that we accept the premise that the liberalization is beneficial to the consumers). Adopting a comprehensive set of special measures for the protection of the *persons in precarious situations* (which gradually more and more resembles the UK system of protection of vulnerable consumers), points to the conclusion that the French legislator has understood that price regulation (alone) is not enough to ensure the Affordability of Energy for all groups of consumers—as, in particular, the vulnerable consumers need a special set of measures, given that the problems they face are much more diversified than just the level of the price of energy. Rather, price regulation in France mostly benefits non-vulnerable consumers as it aims at maintaining widely reasonable prices, despite having a disproportionately negative impact on the competition.

### The United Kingdom: Regulation Targeted at Vulnerable Consumers

The UK Energy Regulator, *the Energy and Gas Market Authority* (OFGEM),<sup>33</sup> was established by the Utilities Act (2000) as first in a line of statutes which were part of a systematic attempt by the Labour Government to review the body of the utility regulation, bringing in more social concerns (Prosser 2005, p. 70). The main objectives of the regulator were to promote the protection of consumers through the promotion and oversight of the competition in the energy market. OFGEM has, in principle, full competence<sup>34</sup> over competition in the energy market with some (less significant) exceptions for the Office of Fair Trading (OFT).<sup>35</sup> As we will see, the position of the independent agencies, including OFGEM, is comparatively stronger than is the case of its continental counterparts, which means that it has considerable bargaining power vis-à-vis the energy suppliers.

OFGEM ensures consumers' interests primarily by ensuring effective competition (on the basis of Competition Act 1998, Gas Act 1984, and Electricity Act 1989), with the possibility to enforce the compliance with penalties ("Enforcement Orders"). OFGEM has further competence to enforce compliance with the consumer protection legislation under the Enterprise Act (2002).

The most important tool for the enforcement of consumer protection is the right to change the *Standard License Conditions*<sup>36</sup> (Prosser 2005, p. 67), which usually leads to fierce opposition from businesses.<sup>37</sup> However, OFGEM claims that, as competition stabilizes, it tends to simplify the regulatory environment through shortening and simplifying license conditions,<sup>38</sup> leaving more and more issues to the self-regulatory schemes.<sup>39</sup> This will later be reversed by the legislator in respect of dispute settlement.

<sup>33</sup> Energy and Gas Authority is a collegial executive body, to whom is subordinated the Office of Gas and Electricity market (OFGEM). However, Authority and OFGEM are used interchangeably even by the regulator itself. See <http://www.ofgem.gov.uk/About%20us/Pages/AboutUsPage.aspx>.

<sup>34</sup> Similar to the Slovak Regulator URSO whose only statutory objective is the protection of competition in the energy market. However, consumer protection has been proclaimed an objective, e.g., in the reports to the Commission (see Urad na regulaci sietovych odvetvi 2006 or Urad na regulaci sietovych odvetvi 2007).

<sup>35</sup> OFGEM, OFT (2005).

<sup>36</sup> OFGEM has the right to enforce license conditions from 2002, under both the Gas Act 1984 and the Electricity Act 1989.

<sup>37</sup> See, e.g., OFGEM (2007a).

<sup>38</sup> Simplification of the Supply License Condition took effect from 2008. Ibid.

<sup>39</sup> E.g., Energy Retail Association Safety Net (<http://www.energy-retail.org.uk/>).



Institutionally, OFGEM was supplemented by the “Council for the Protection of Consumers” (Energywatch),<sup>40</sup> established by the Utilities Act.<sup>41</sup> Energywatch was a consumer advocate body, “consumer voice” when dealing with energy companies, compensating for the lack of sufficient bargaining power on the side of consumers when dealing with these economically significantly stronger partners. One of the major successes of Energywatch was the ability to bring a Supercomplaint<sup>42</sup> to the OFGEM on the billing procedure, which resulted in a call from OFGEM to the companies in the energy sector to establish an Energy Supply Ombudsman who would investigate billing disputes and eventually award also financial compensation. The competence of the thus established Ombudsman has been gradually widened to the general competence to decide upon any issue concerning energy supply. The number of cases decided by the Energy Supply Ombudsman has been progressively increasing, with a large number of cases decided favourably for the complainants.<sup>43</sup> This self-regulatory arrangement has been turned into a regulatory one by the Consumers, Estate Agents and Redress Scheme Act (2007), on the basis of which the Energy Supply Ombudsman became an approved redress scheme.

Except for the dispute settlement scheme, OFGEM has asked companies to restrict back-billing,<sup>44</sup> which forced many consumers into debt, and to ensure that the contract terms are not unfair or biased in favour of energy companies. In general, OFGEM asked the companies to comply with this recommendation by the means of self-regulation; otherwise, OFGEM would change the license conditions in the same way.

The Consumers, Estate Agents and Redress Scheme Act (2007), which came into effect in July 2008, brought great changes to the UK model: it introduces the obligation to belong to a redress scheme, on the one hand, and tries to bring simplification to consumer protection schemes, on the other. From October 2008, the Energywatch ceased to exist as a separate body and was incorporated into the general consumer body (National Consumer Council), whose competences were extended.<sup>45</sup> A crucial change is the establishment of a compulsory redress scheme<sup>46</sup> to which every energy supplier and network operator will have to belong. The redress scheme will have the competence to decide disputes and assign compensation to the consumers where warranted. Which bodies will be approved as redress schemes is decided by OFGEM. The Energy Supply Ombudsman has become one of them.

### Protection of Vulnerable Consumers in the UK

The regulation dealing with vulnerable consumers is found in the Standard License Condition for Supply of Energy (SLC Supply) in sections 26, 27. Which groups of

<sup>40</sup> Such consumer “watchdog” was also established in postal services; in telecommunications, a different path was taken from the beginning (self-regulatory schemes Otelio). For more details, see Elizabeth France, *Ombudsman ~ their developing role in consumer policy and utilities*, CRI occasional lecture at University College London on 6 November 2006, p. 3.

<sup>41</sup> See Sections 17–27 of the Utilities Act (2000).

<sup>42</sup> See OFGEM (2005).

<sup>43</sup> COM (2007c), p. 4. See also [http://www.energy-ombudsman.org.uk/links/3-5-case\\_study\\_bulletins.php](http://www.energy-ombudsman.org.uk/links/3-5-case_study_bulletins.php).

<sup>44</sup> Prepayment meters are installed usually by vulnerable consumers as a way to prevent disconnection. However, the old token meters needed to be updated after every change of price which the energy companies have not done regularly and which has led to back-billing and, inevitably, has left many of the consumers in debt. See Energywatch (2007).

<sup>45</sup> See Consumers, Estate Agents and Redress Scheme Act (2007), Part 1.

<sup>46</sup> See Consumers, Estate Agents and Redress Scheme Act (2007), Part 2.



consumers are considered to be vulnerable in the UK? <sup>47</sup> Customers of pensionable age, disabled, chronically sick, (partially) deaf or blind consumers (SLC 26), and consumers who are in payment difficulties (SLC 27).

The central provision, for our purposes, deals with consumers with payment difficulties, who are threatened with disconnection for debt. At the first stage, providing a consumer with an appropriate payment method is extraordinarily helpful. The UK supplier is obliged, as soon as she becomes aware or has reason to believe that a domestic customer is having or will have payment difficulty,<sup>48</sup> to offer to have payment deducted automatically from social security benefits (so called *Fuel Direct*)<sup>49</sup> received by that consumer. A further option for consumers, which suppliers have to offer, is payment by instalments or through a prepayment meter. Consumers with payment problems should also be informed about how to lower their electricity bills, and all consumers must receive information about these options.

According to consumer protection bodies and organizations, “Fuel Direct” together with prepayment meters is one of the most important possibilities for vulnerable consumers<sup>50</sup> to ensure timely payment and avoid disconnection for debt. These measures could also contribute to solving high disconnection figures in a number of (new) MS where there is reason to believe that a significant number of disconnected customers receive welfare benefits.

The SLC Supply further prohibits the disconnection of a domestic premises for debt unless the supplier has failed to take all reasonable steps to recover the payment. Suppliers cannot disconnect domestic premises in winter if the supplier knows or has reason to believe that the customer is of pensionable age and lives alone or lives only with persons who are of pensionable age or under the age of 18. SLC Supply deals also with the legal regime of prepayment meters, which were often installed by vulnerable consumers as a means of preventing disconnection,<sup>51</sup> though they are often the most expensive method of payment.<sup>52</sup> The question that might be legitimately posed is to what extent such treatment establishes inequality and to what extent the unfair terms of legislation militates against such discrimination. It is equally worth noting that, though the Council Directive 93/13/EEC on unfair terms in consumer contracts excludes the price from the assessment of unfairness, in case of services of general economic interest, wherein transparency of prices might be an issue, it might be argued that the exclusion would not apply (Willett 2008, p. 149).

<sup>47</sup> Low-income consumers (and consumers living in rural areas) are not among the vulnerable groups mentioned in the supply license conditions. However, the concept of “low-income” consumer embraces all kind of vulnerability and thus has been target directly by the regulation. See, e.g., Energywatch (2007).

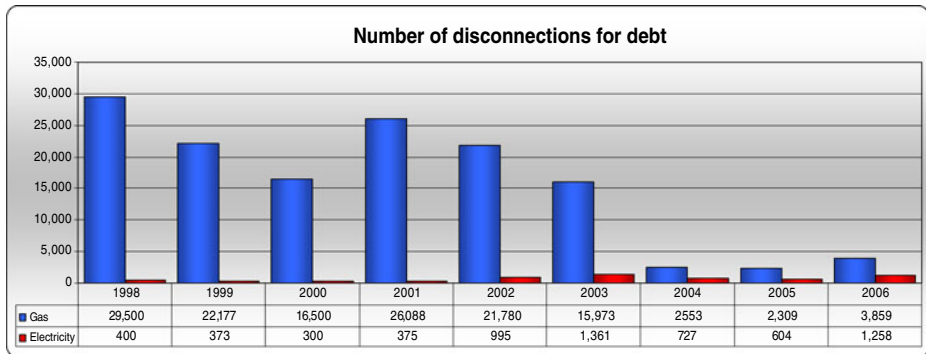
<sup>48</sup> Mirror provision contains also the Standard Gas Supply Condition.

<sup>49</sup> Fuel Direct implies direct deduction of the payment for electricity, and a proportional amount for outstanding debt, from the social benefits. It is very helpful in cases of irresponsible handling of financial resources (e.g., in cases of gambling and drug abuse, and in some new MS, it may serve as a means of protecting vulnerable consumers from the effects of usury loans they often enter into). Prepayment meters on the other hand are usually installed instead of disconnection, when the consumer has to recharge its account for electricity in advance. See <http://www.energywatch.org.uk>.

<sup>50</sup> OFGEM (2006), pp. 41–42.

<sup>51</sup> As partly mentioned before, the first generation of prepayment meters were token meters, which had to manually adjusted after every price rise and given that the energy companies have been slow to recalibrate or adjust these meters, people may have built up hundreds of pounds of debt which is likely to be added to the meter. Often consumers only became aware of this problem when they wanted to switch supplier.

<sup>52</sup> The reason given by the majority of the suppliers are the higher costs for the provision of this method of payment.



**Fig. 1** Number of disconnections for debt. Source: The OFGEM's report to the Commission, 2007 (these numbers might hide self-disconnections in cases where the consumer is not able to pre pay for the electricity when supplied with prepayment meters; Prosser 2005, p. 83)

The regulation on disconnection is supplemented by various corporate social responsibility schemes or government-sponsored social schemes (such as Home Heat Helpline,<sup>53</sup> PSR register,<sup>54</sup> Winter fuel payments,<sup>55</sup> Warm front<sup>56</sup>), which create a comprehensive safety net for the protection of the most vulnerable consumers. Of course, we should not forget the Energy Consumer Ombudsman who helps consumers in cases of inadequate billing actions by suppliers, which are often the reason why vulnerable consumers are getting into debt.

The cumulative effect of all the above-mentioned measures is that disconnection rates (foremost in gas, where they were considerably higher than in electricity) were substantially lowered.<sup>57</sup> The suppliers make efforts to distinguish between the persons “who cannot pay”<sup>58</sup> and those “who do not want to pay;” and only in the second case can disconnection be a proper enforcement mechanism. The Energy Retail Association claims that no vulnerable consumer has been disconnected since 2004 (Fig. 1).<sup>59</sup>

<sup>53</sup> See <http://www.homeheathelpline.org>. This is a free national helpline run by energy suppliers for customers having difficulties in paying their fuel bills.

<sup>54</sup> Suppliers are required to establish and maintain a Priority Service Register which lists their domestic customers who are of pensionable age, disabled, or chronically sick. Customers on the PSR are eligible for additional services free of charge and suppliers are prohibited from disconnecting premises occupied by a customer eligible for the PSR during the winter months.

<sup>55</sup> See <http://www.thepensionerservice.gov.uk/winterfuel/home.asp>. The Winter Fuel Payment is an annual payment to help with the costs of keeping warm in winter. The payment is available to people who are aged 60 or over. For individuals between 60 and 79 the payment is either £125 or £250, those who are aged 80 or over may receive £ 200, £275, or £400, depending on individual circumstances.

<sup>56</sup> See <http://www.warmfront.co.uk>. The Government's Warm Front Grant can provide a package of insulation and/or heating improvements up to a maximum value of £3,500 (or £6,000 where oil, low carbon, or renewable technologies are recommended) for some home owners and those renting from private landlords. See <http://www.warmfront.co.uk>.

<sup>57</sup> OFGEM (2007c) OFGEM's Submission to the European Commission reporting requirements under Directives 2003/54/EC and 2003/55/EC, p. 90.

<sup>58</sup> See <http://www.energy-retail.org.uk/preventingdisconnection.html>. The energy suppliers have also established schemes for the vulnerable consumers within the corporate responsibility. See, e.g., <http://www.britishtgas.co.uk/about-british-gas/what-s-important-to-us/customer-commitment.html>.

<sup>59</sup> See <http://www.energy-retail.org.uk/preventingdisconnection.html>.

Due to the specificity of the UK system, which traditionally grants broad powers to the independent governmental agencies, it was possible to bring about a number of improvements only by the threat of imposing regulation. OFGEM expressly states that once the efficient self-regulatory measures are in place, it is preferable to regulation.<sup>60</sup> Though not uncontested (Waddams and Pham 2007),<sup>61</sup> from the institutional standpoint, the combination of consumer protection obligations with the obligation to protect and develop competition in energy markets seems to contribute to an effective balance between the tools triggered by each of these, sometimes opposed, objectives.

In conclusion, the protection of vulnerable consumers—particularly the regulation of disconnection and an efficient dispute resolution mechanism—seems to be a crucial tool for ensuring affordability at the second, Targeted Level. As we will see later, the lack of regulation can have very undesirable consequences and thus a comprehensive set of tools should be put in place to contribute to provide for the Affordability of Energy Supply for all groups of consumers, in particular for those who are not able to make easy use of the advantages of the liberalization of the energy sector.

### Slovakia: The Price Regulation (Price Caps)

Price caps interfere with the free market price by setting a price for goods or services which cannot be exceeded by the supplier.<sup>62</sup> The main rationale for price regulation in liberalizing markets should be “to exercise a downward pressure on pricing to become an effective substitute for competition, incentivising the companies to become even more efficient, and to pass on efficiency gains to consumers” (Grenfell 1999, p. 224). So far, so good! However, setting the price at the optimum level is often rather difficult.<sup>63</sup> There is an abundance of empirical research showing the positive effects of the price caps on competition and the transfer of benefits to the consumers (see Biglaiser and Michael 2000; Mathios and Rogers 1989<sup>64</sup>). Yet, the situation we have encountered in Slovakia is radically different.

The Slovak Republic has opened the electricity market to retail suppliers as of 1 July 2007, but the retail gas market has not yet been opened to competition.<sup>65</sup> The Energy Regulator (URSO) has the competence to decide as to whether final price regulation is necessary at all; if yes, then either to set the prices directly or to determine the methodology for ascertaining the price.<sup>66</sup> The regulator has, by its decree, adopted price caps as the Slovakian method of price regulation,<sup>67</sup> stating that the price regulation measures would solely concern network services and the final price for household consumers and would provide a concrete methodology for setting the price.<sup>68</sup>

<sup>60</sup> OFGEM (2006), p. 36.

<sup>61</sup> Waddams and Pham (2007) argue that special competition authority sets lower standards than the general competition authority would do, as it unconsciously colludes with the firms.

<sup>62</sup> There is a number of ways how the price caps are set, e.g., classic price caps, revenue caps, profit caps etc.

<sup>63</sup> OFGEM (2002), pp. 2 and 16.

<sup>64</sup> Mathios and Rogers (1989) empirically show that the effects of price caps might be positive, negative, and neutral, in particular as it concerns the benefits passed to the consumers.

<sup>65</sup> See <http://www.urso.sk>.

<sup>66</sup> Act on regulation in network industries No. 276/2001 Coll., § 12 (7).

<sup>67</sup> Decree of the Regulator, No. 1/2007 Coll.

<sup>68</sup> Decree of the Regulator, No. 1/2007 Coll., which stipulates the level of price regulation, § 2–5 and Decree of the Regulator, No. 2/2007 Coll., which stipulates the methodology for setting a price (resembling, to a certain extent, the infamous rate of return price regulation).

The regulator has justified price regulation by the need to protect consumers (which is the reason cited in the report to the Commission).<sup>69</sup> To what extent this decision makes sense will be examined further.

Factors with direct influence on the level of prices in Slovakia:

- (a) The price of electricity in Slovakia is 13% higher than the EU average.<sup>70</sup>
- (b) The income of households is considerably lower than in the neighbouring states,<sup>71</sup> as is the price of labour.
- (c) The highest proportion of energy is produced in nuclear generation (68%) and hydro generation (12%), thus from the cheapest energy sources.<sup>72</sup>
- (d) Slovakia is a net exporter of electricity.<sup>73</sup>
- (e) Generation capacity is concentrated in the hands of one company. This company is the second biggest generator in Central Europe, with profits of over three billion Slovak Crowns (approximately EUR 100 million).<sup>74</sup>
- (f) All neighbouring EU countries (and the customers of Slovak energy producers) have energy prices considerably below the European average (more than 10%), which makes the difference in price between Slovakia and the neighbouring EU MSs approximately 25%.<sup>75</sup>
- (g) Finally, price regulation is in place, which should minimally ensure that suppliers do not abuse their dominant position because the prices are controlled ex ante (even if not setting them at an affordable level).

Taking into account factors (b) to (g), Slovakia seems to have the preconditions to make very cheap electricity available to the national consumers. In particular, electricity is produced surplus to Slovakia's needs, from the cheapest sources (hydro plants and nuclear plants) administered by a comparatively cheap labour force—thus production costs should be considerably lower than the European average. *However, Slovakia has prices that are approximately 25% higher than in the neighbouring states, to whom it exports electricity; despite all above-mentioned factors, and particularly including the price regulation.* Thus, it seems that the only effect is of direct price regulation in Slovakia—which is in essence the strongest interference with the emerging market and should, therefore, have at least correspondingly positive effects on the consumers—is, on the one hand, taking energy suppliers out of the reach of competition authorities (because of the official “rubberstamp” on the prices of energy from the regulator) and minimizing switching,<sup>76</sup> on the other hand.

<sup>69</sup> ERGEG (2007), p. 14.

<sup>70</sup> See *Internal Market Fact Sheet Slovakia*, January 2007.

<sup>71</sup> According to the Slovak Statistical Office, the average income per person (depending on the size of household) is approximately EUR 300 (<http://portal.statistics.sk/showdoc.do?docid=4618>). The average income in the Czech Republic is 30% higher. See [http://www.czso.cz/csu/2006edicniplan.nsf/t/B5002C52E0/\\$File/3012061a.pdf](http://www.czso.cz/csu/2006edicniplan.nsf/t/B5002C52E0/$File/3012061a.pdf) or [http://www.czso.cz/csu/2006edicniplan.nsf/t/B5002C52E6/\\$File/3012062a.pdf](http://www.czso.cz/csu/2006edicniplan.nsf/t/B5002C52E6/$File/3012062a.pdf).

<sup>72</sup> COM (2007b), Annex 2.

<sup>73</sup> COM (2007i).

<sup>74</sup> For comparison, the incumbent in the Czech Republic, the CEZ will make profit of almost two billion EUR (despite the crisis).

<sup>75</sup> Compare COM (2007d, e, f, g) *Internal market fact sheets: Austria, Poland, Czech Republic, Hungary, and Slovakia*.

<sup>76</sup> COM (2007d) *Internal market fact sheet: Slovakia*.

## The Position of (Vulnerable) Consumers in Slovakia

Looking into the provisions of Slovak Energy Law,<sup>77</sup> we would be unsuccessful in identifying provisions aimed at regulating the protection of vulnerable consumers. Art. 20 of the Energy Law (section on “Protection of the consumer”) does follow the Directives<sup>78</sup> in several ways: it requires suppliers to provide a contract containing various information (on price, termination of the contract, the way compensation for the failure to provide the energy is agreed<sup>79</sup> or quality is calculated, etc.) and places an obligation on suppliers to enable household consumers to choose between different methods of payment as well as the obligation to inform the consumer about modifications 30 days before they take effect.

However, what the Slovak legislation did not implement were rules on disconnection (termination is left to the contract), the protection of vulnerable consumers, and an appropriate dispute resolution mechanism. How serious the consequences of the lack of regulation are in practice, with regard to the interrelationship between high prices and low incomes, might be demonstrated by the numbers of disconnected households. *In 2006, the number of disconnected households reached 40000.*<sup>80</sup> Considering that Slovakia has four million inhabitants, and households with an average of three persons, the number of disconnected reached 3% of the population.<sup>81</sup> The data from 2007 show the same picture—*in 2007, approximately 35000 households were disconnected.*<sup>82</sup> The URSO prefers not to state these numbers in the National Report for 2008. This is alarming data, especially if compared to Great Britain (which in comparison has a population of over 60 million inhabitants) where the number was 40 times lower in the same year.<sup>83</sup>

Thus, the situation in this small country (4000000 inhabitants) is as follows. Despite the generally low income of its citizens,<sup>84</sup> the regulated prices of energy are above European average (EU 27 as well as EU 15). For this reason, a greater number of persons would qualify as living in “fuel poverty.” All these people might need special treatment and help in order to prevent disconnection.<sup>85</sup> However, there is none of this and the consequences are alarming inasmuch as a rather generous social welfare system as we see does not prevent it. It is not only that price regulation in general is not a suitable second level/ Targeted Level device for solving the hardships faced by vulnerable consumers, but also in the fact that the Slovak solution even exacerbates them.

## The Czech Republic: Reliance on Competition?

Finally, we come to the Czech model, which tries to achieve affordability through competition (no price regulation) in sole combination with general social welfare schemes

<sup>77</sup> The act on the regulation in network industries, No. 276/2001 Coll.

<sup>78</sup> Electricity Directive 2003 and Gas Directive 2003.

<sup>79</sup> There is no specific regulation of quality of electricity supply, thus the contract applies, i.e., in fact the standard contract term set by supplier.

<sup>80</sup> National Report 2006, Regulatory Office for Network Industries, Slovak Republic.

<sup>81</sup> This was not an exceptional number caused by some peculiar situation. A year before, the number reached 35000 disconnected households. See *Slovak National Report 2006, Regulatory Office for Network Industries, Slovak Republic.*

<sup>82</sup> National Report 2007, Regulatory Office for Network Industries, Slovak Republic, p. 53.

<sup>83</sup> OFGEM (2007c). *OFGEM's submission to the European Commission reporting requirements under directives 2003/54/EC and 2003/55/EC*, p. 90.

<sup>84</sup> See above, no. 71.

<sup>85</sup> Not to worsen already high social exclusion of some vulnerable consumers. Despite missing statistics there is a big possibility that many of the disconnected consumers belong to the Roma minority.

(general social and welfare benefits) and, thus, is without any sector-specific regulation aimed at the protection of (vulnerable) consumers. The Czech Republic (CR) has operated an entirely open energy market from 1 January 2006.<sup>86</sup> The Energy Law<sup>87</sup> designated the Energy Regulatory Office (ERU) as an independent regulatory agency (with approximately 100 employees) to oversee the energy market. The ERU has shared competence to oversee competition in the energy market with the Competition Authority (UOHS) where the ERU has the competence only to “support” the development of full competition in the future<sup>88</sup> (and maximally can impose a fine for the abuse of economic position under the Act on Prices), while the UOHS retains the competence for the protection of competition and enforces Art. 81 and 82 of the Treaty. Regarding the competence of the ERU in consumer matters, it is very limited and stops at the protection of consumer interests in network matters (the regulated part of the market, namely, transmission and distribution).<sup>89</sup>

Another body investigating breaches of energy regulations in the CR is the State Energy Inspection (under the control of the Ministry of Trade). This also cooperates with the ERU, also in consumer matters, and investigates breaches by suppliers “in the field.” The institutional framework is completed by the Czech Commercial Inspection (CCI), a general consumer protection body, institutionally designed to investigate breaches of consumer protection law, thus also the majority of consumer issues arising in energy markets (as there is practically no specific sector for consumer protection). However, in reality, the CCI tends to shift all the complaints to the ERU because of the “highly specific nature of the market.” Given that the ERU does not have the competence to examine or penalize the breaches of consumer law, it can only mediate between the consumer and supplier so even overt breaches can remain unpunished.<sup>90</sup>

The level of development of retail market competition is an important indicator as to what extent the eventual positive consequences of the competition regime might make up for the lack of regulation. However, the market remains highly concentrated and customer switching has been limited to date, with mainly large energy consumers switching.<sup>91</sup>

The universal service obligations were transposed loosely by the CR. The CR claims that it has implemented the universal service obligations under the Act No. 670/2004, which amends the existing Energy Act.<sup>92</sup> In reality, the CR has implemented only few provisions. These are: obligation of the supplier to make a contract when the consumer has fulfilled all the requirements set by the supplier;<sup>93</sup> the provisions on the supplier of last instance;<sup>94</sup> the obligation to inform consumers of the modification of the contract terms at least 2 months in advance in the case of electricity<sup>95</sup> and at least 1 month in the case of gas;<sup>96</sup> the obligation to offer “fair and non-discriminatory selection of payment methods;”<sup>97</sup> the

<sup>86</sup> Act No. 458/2000 Coll. on business conditions and supervision in energy sector (Energy law), §21/2/e.

<sup>87</sup> Ibid., § 17.

<sup>88</sup> Komp 3/2006-51, Czech Supreme Administrative Court, Decision of 18 December 2007.

<sup>89</sup> Energy Law, § 17.

<sup>90</sup> One could imagine more sophisticated ways of cooperation between these authorities, but it is not the case in practice.

<sup>91</sup> COM (2007h) *Energy Mix Fact Sheet: Czech Republic* and COM (2007e) *Internal Market Fact Sheet: Czech Republic*.

<sup>92</sup> See Energetický regulační úrad (2007), p. 43.

<sup>93</sup> Energy Law, § 35.

<sup>94</sup> Energy Law § 12a; until the end of 2007, no consumer has used his right to the supplier of last instance. Energetický regulační úrad (2007), p. 44.

<sup>95</sup> Energy Law, § 21(2) d.

<sup>96</sup> Energy Law, § 63 (1) a.

<sup>97</sup> Energy Law, § 21 (2) c.

obligation to include in the electricity bill information about the source of electricity and a reference to the public source of information about the environmental impact of these; the obligation to keep the parameters of supply and service quality that are set out in an implementing regulation and the right of the consumer to compensation in case the quality does not reach necessary level<sup>98</sup> as well as the proportion of the contribution by the consumer for connection to the distribution network.<sup>99</sup>

The CR did not define nor introduce any specific measures for the protection of vulnerable consumers, neither did it introduce any regulation concerning the disconnection of electricity or gas supplies (the only provisions dealing with disconnection states that the theft of electricity as well as non-payment are reasons for disconnection). Likewise, it did not introduce a number of consumer protection measures required by Annex I to the Directives in the Second Energy Package.

Given the lack of regulation, general consumer/contract law applies in these instances. This means that the additional information duties apply only in case of distance contracts and doorstep contracts; for the rest, general contract law applies with only minimal information requirements. Even more counter-productive is that there is no requirement to include in the bill, or at the very least in the contract, any reference to the regulator, calculator, or possibility of complaint to the regulator. Thus, the CR has failed to transpose the consumer protection measures of the Second Energy Package, not to mention more detailed provisions required by the Third Energy Package.

### The Position of (Vulnerable) Consumers in the Czech Republic

The CR has opted for a very adventurous way of going about the affordability question. Namely, it has not addressed the question of affordability by any particular regulatory measure; formally established competition in combination with consumer law and general social welfare schemes have to suffice.

Regrettably, we miss a reliable indicator of the level of consumer, and foremost, vulnerable consumers' difficulties in CR. Namely, until recently, the ERU did not require the information on how many households are disconnected yearly. In the report for 2008, the ERU already stated that the distributors should keep statistics of the disconnected households and provide them to the ERU. However, it fails to indicate any numbers in the report (contrary to Slovak URSO—at least in the report for 2006 and 2007—or Energywatch).<sup>100</sup> Moreover, despite all my requests to the major energy distribution companies, they refused to disclose this information.

I will, therefore, try to roughly estimate the number of disconnected households on the basis of available information. The national newspaper “Mlada fronta dnes” has published the information that the distribution company (E.ON.) has already disconnected 1200 households since the beginning of the year. E.ON. has approximately one fourth of the market<sup>101</sup> and the period elapsed since the beginning of the year is approximately 4 months. If all the suppliers have the same disconnection behaviour, the number will reach approximately 15000 households yearly. However, it is very likely that the number might

<sup>98</sup> Energy Law, §17 (7) a.

<sup>99</sup> Energy Law, §17 (7) d, l.

<sup>100</sup> In the last report to the ERGEG, the Czech Republic states practically that there is no reason for concern, as persons can be disconnected only for the reasons explicitly provided for by the Energy Law: “i.e. chiefly due to unauthorized take of energy, in particular when the customer fails to pay.” Energetický regulační úrad (2008), p. 54.

<sup>101</sup> See [http://www.eon.cz/cs/corporate/profile/eon\\_distribuce.shtml](http://www.eon.cz/cs/corporate/profile/eon_distribuce.shtml).



be even higher because, as the empirical research has shown, the most problematic service provider is the incumbent company CEZ.<sup>102</sup>

### The Results of Empirical Research and Policy Recommendations

In March 2008, I undertook empirical research at the ERU to examine consumer complaints after the liberalization of the retail market. I have examined 99 complaints put forward in 2007, 19 of them assessed as being well-founded. In 2006, ERU received 150 complaints, 14 of which were assessed as well-founded. Under the currently set legal framework where most of the issues of consumer protection are left to the general consumer law, where ERU does not have any competence, the only feasible venue (and thus referred to by the regulator) for solving these complaints is the judicial assembly. For most consumers, this is not a real option, which is even more of an issue in cases concerning vulnerable consumers.

A number of consumer complaints concerns the high level of energy prices and are lodged predominantly by older consumers. The ERU tries to respond by explaining how the prices are set in general: the price for the use of natural monopolies is set by the regulator (and this makes up approximately 40% of the price), the rest is left to the competition. The ERU cannot advise consumers to make use of some special social scheme or “corporate responsibility” scheme and it does not advise them on saving.

A second set of complaints concerns unwanted disconnection, which is clearly the most adverse consequence that the consumer might face in the energy market; the primary aim of the measures ensuring affordability being the prevention of disconnections. As already mentioned, the CR did not implement any measures to safeguard the interest of consumers in relation to disconnection, as required by Art. 3(5) of the Electricity Directive 2003. Thus, the regulation of disconnection is left to the contract drafted in advance by energy suppliers. For illustration, the standard conditions of the incumbent company group CEZ provide that the supplier has the right to disconnect a customer in case of 14 days delay of payment.

The empirical study has shown several types of problems that may result from such a short termination notice. Some customers were disconnected because of error in data transfer between old and new suppliers. Others were disconnected due to an error in the database of their supplier. In every case, customers had to pay the reconnection fee if they wanted to be reconnected and only then could they start any dialogue with the supplier to find out what in fact had happened. There is little evidence as to how many complaints of this kind are solved between the companies and consumers themselves. However, complaints that reach ERU show that the companies do not try to investigate complaints in an objective way. And if a mistake is found on the side of company, the customers still obtain at most a refund of the reconnection fee and eventually an apology.

Another group of disconnected consumers are the non-diligent consumers (customers who do not use banking systems for the payment—often elderly or low-income consumers). If consumers change their residence or if they have left their homes for a longer time for other reasons, they might find themselves disconnected shortly after the bill was sent.

Finally, a significant number of disconnected consumers simply do not have the necessary funds at the time when the payment is requested. These customers will be disconnected and thus they would not only have to pay their debt, but also the reconnection payment, which would not enhance their economic situation.

<sup>102</sup> The numbers of disconnections by the incumbent will also be higher as low income consumers tend to switch less and usually stay with the incumbents.

One of the most the most common complaints in the CR concerns the sudden increase in the sum billed for energy. Complaints show that these cases are financially (and emotionally) extremely burdening for consumers. The greatest number of consumers complain that, at one point, the bill they received had increased without any clear reason (no new electric devices in the household, no new inhabitants, etc.), in many cases more than ten or 20 times.

The whole responsibility in such situations lies on the consumer—and only bias in electrometer readings liberates the consumer from this responsibility. The only option a consumer has is to invite a technician (of a supplier) who will control whether the electrometer is free of bias. If a technician finds out that the electrometer is well-functioning, the consumer has not only to pay the bill, but also for the visit of the technician. The consumer has also the option to invite an independent expert, but this is also subject to a fee. The ERU, similar to other regulators,<sup>103</sup> does not recommend the invitation of an independent expert as the increase is rarely caused by bias of electrometer (according to Energywatch, only in 20% of cases).<sup>104</sup>

The most alarming case that I have examined concerned one such sudden increase in the bill to a customer of the incumbent company CEZ, a pensioner, living alone in a remote area, who had had the same consumption for more than 30 years.

The only offer by the CEZ to this “super-vulnerable” consumer was payment of debt in instalments; otherwise, the CEZ threatened him with disconnection. CEZ was unwilling to show any understanding of the situation and/or to lower the bill. The financial burden for this pensioner was extreme. However, the only response that ERU could give to this consumer was that CEZ had acted in accordance with the law and there was nothing that could be done. Thus, this person was either disconnected (ERU does not have further information) because he could hardly pay the instalments from a very low pension or he had paid the debt to a gigantic energy supplier and could not afford a reasonable diet to the end of his life.

What are the lessons to be drawn? From the outset, it is clear that whatever the legal framework—whether there is sector-specific regulation or general consumer law applies—a crucial starting point is the existence of an efficient, inexpensive, quick, and fair dispute resolution mechanism. Even the most elaborate regulation is insufficient if the consumers do not have a feasible way to enforce it.<sup>105</sup> In the case of the CR, an alternative to setting an independent dispute resolution mechanism (though not an equivalent alternative) would be the empowerment of the regulator to perform dispute resolution tasks.<sup>106</sup>

The high price of energy, which gradually increases in the newly created “competitive” markets,<sup>107</sup> poses a significant burden on some consumers. These would benefit from certain social schemes as is the case in the UK. Relying, in this regard, on corporate social responsibility schemes would render such measures nearly cost-less.<sup>108</sup> Eventually, a scheme or a fund co-financed by the contributions of the companies and the state might be

<sup>103</sup> See Energywatch, FAQ: [http://www.energywatch.org.uk/your\\_questions/index.asp](http://www.energywatch.org.uk/your_questions/index.asp).

<sup>104</sup> Ibid.

<sup>105</sup> Art. 3(13) of the Electricity Directive 2009 requires that the MS ensure the establishment of an independent dispute settlement mechanism.

<sup>106</sup> This would however require number of changes in case of the Czech Republic, starting from competences, budget, to the personnel structure of the regulator.

<sup>107</sup> The price of energy will decrease in the next calendar year in the Czech Republic; it is however unlikely it will be a long-term trend.

<sup>108</sup> The prices are increasing considerably every year. See Fact Sheet Internal Market in Energy: Czech Republic. The state holds approximately 60% share in the incumbent energy supplier CEZ.

an alternative. Neither in the Czech nor the Slovak Republics do general social welfare schemes seem to suffice, for many of the reasons already mentioned. Alternatively, such general social welfare schemes could be tied to payment for utilities, as is the case in the UK (*Fuel direct*).

Regarding disconnections, it is vital to enact binding rules for disconnection (issued by the legislator, regulator, or eventually, by a self-regulatory body). This is already required by the Third Energy Package.<sup>109</sup> These rules should set the procedure, which would have to be followed before disconnection: contacting a consumer in payment difficulties, finding out where the problem lies, giving advice on consumption and offering different payment methods, taking into consideration whether the consumer is able to pay (e.g., payment by deduction from social benefits, etc.) or whether the consumer cannot pay and, in this case, employing either adequate corporate responsibility schemes or governmental social welfare schemes<sup>110</sup>.

An obligation to enter into personal contact with the consumer should be required, as it is an important tool for avoiding situations where a consumer is disconnected because of change of residence or longer holidays. Such personal contact is crucial for discovering whether the consumer is not able to pay or not willing to pay, thus employing disconnection as enforcement only where fair and, in all other cases, trying to find an alternative solution. Today, some of the companies in the CR contact a consumer in writing before disconnection. This, however, is not sufficient to remove either the first type of problem or the one faced by vulnerable consumers. This is so not only because a number of letters would not be received or understood, but also because vulnerable consumers would need advice and help rather than a formal notice with the threat of contractual penalty and disconnection.

As already mentioned, it would be equally important to establish a dispute resolution mechanism; this could be the statutory establishment of an institution like the “Energy Supply Ombudsman,” which would be free, quick, and fair and competent to award compensation if warranted—of course, the information about such procedures should be easily accessible to the consumer, e.g., on the invoice or accompanying materials. This is also required by the Third Energy Package. Any compensation would not only constitute satisfaction for a consumer but also an incentive for suppliers to improve their services.

Finally, billing problems should be an ultimate priority. In respect of an unexplained increase in consumption of energy, the suppliers should share the burden at least to some extent and be obliged to enter into discussion with consumers as to why such a great increase has taken place. In similar cases in the UK, the Energy Supply Ombudsman requires the energy supplier to provide, firstly, a free in-house examination, but eventually also an independent examination of the electrometer (if the in-house examination did not show the bias), as well as to send an expert to the consumer’s household to give informed advice on energy saving.<sup>111</sup> Leaving all the responsibility to the consumer, without any “equity” arrangements, might have tragic consequences for some consumers.

## Conclusion

Why do states intervene to ensure the affordability of electricity rather than some other crucial good/service? On a more general level, the reason is the crucial role energy plays in

<sup>109</sup> Electricity Directive 2009.

<sup>110</sup> See also ERA (2007).

<sup>111</sup> See Energy Supply Ombudsman (2008), p. 9.

contemporary society for inclusion into social and economic life—for the benefit of the individual and the society in general. There are a number of other important reasons prompting intervention, such as the lack of efficient competition in the energy market, diametrically different economic power of the actors involved, the need for continual supply, and finally, the disproportionate “enforcement” power of the energy supplier (the threat of disconnection).

This paper has explored different strategies of addressing the question of affordability on two different levels (for all consumers—General Level and for the disadvantaged ones—Targeted Level)—both through *Regulation* (through *price regulation* as well as through *targeted regulation*) and through *Competition*. What are the lessons to be drawn? First of all, it seems that there is considerable difference in the level of protection achieved in old MS and new MS, disregarding what regulatory strategy the state has employed.

The UK model has proved to be well-tailored to guard the interests of vulnerable consumers, while simultaneously respecting competition and not burdening the welfare system unnecessarily. It is perhaps for these reasons that the UK model was a source of inspiration for the Second and the Third Energy Package.

In France, regulation indeed benefits consumers in general to the extent that the prices are lower than the market price would be (because the energy comes from cheap nuclear sources EDF can make a profit despite keeping the price low). However, this comes at the expense of conservation of the market and protection of the national champions and is thus disadvantageous to competition in France and the region, as well as the vision of the internal market in energy. Despite price regulation, France has still had to introduce targeted protection of vulnerable consumers because price regulation does not suffice for the effective protection of these consumers.

In contrast, the Slovak example seems to be a *prima facie* abuse of the rationale of the price regulation where the regulation disadvantages consumers rather than benefits them. The prices are considerably higher than in the other neighbouring MS, despite Slovakia being a net exporter of electricity produced from the cheapest sources. The only effect of regulation seems that the behaviour of the companies is taken out of the reach of competition authorities.

The CR has also taken a very problematic path by not regulating the majority of the aspects of supplier–consumer relationships in the energy sector. Concretely, the CR has decided to leave the great majority of the contractual issues in the relation between companies and consumers to the market and rely only on competition law, general consumer law, general social welfare schemes, and judicial enforcement mechanisms. And it has turned out to be unworkable. The disconnection rates are too high, the prices are high and getting higher,<sup>112</sup> and regulation overtly favours the energy suppliers, and given the changed market conditions, regulation has even been abused by suppliers (Bartl 2009, p. 22; for similar problems in Germany, see Rott 2005, pp. 322–323).

In the (examined) new MS, all these problems are further neglected because the whole political climate does not favour regulation aimed at protecting selected social group. Both sides of the political spectrum are unwilling to introduce “communist-like,” “class-based” measures. This communist legacy, however, only strengthens the market position of the incumbent (quasi-monopoly) companies, which is hardly a liberal outcome.

<sup>112</sup> See <http://aktualne.centrum.cz/finance/penize-a-investice/clanek.phtml?id=622923>. The incumbent company CEZ has increased their profit by 40%, to two billion EUR for 2008. See <http://aktualne.centrum.cz/ekonomika/penize/clanek.phtml?id=652767>.

The new MS examined are urgently advised to implement regulation targeted at the protection of vulnerable consumers—in particular because it is likely that they have even higher numbers of vulnerable consumers than the old MS and who often belong to the ethnic minorities. The (new) MS will also have the opportunity to make the necessary changes in relation to the implementation of the Third Energy Package until March 2011. But in the end, it is a task for the EC to enforce correct implementation of EU legislation to avoid undermining the legitimacy of the whole liberalization process.

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