

**MIT-EPRG Madrid Conference**  
**Madrid, 2 and 3 July 2014**

Ladies, gentlemen,

As always, I must begin by expressing my gratitude toward the organisers of this event for their gracious invitation.

It is an honour for me to have the opportunity to open this conference in which some of the fundamental questions of the energy sector will be described.

With your permission, from the perspective of the institution over which I preside, the National Commission for Markets and Competition, I am going to outline, firstly, some of the fundamental questions faced by energy policy and regulation – which will be extensively addressed throughout this conference – in their goal to attain and preserve an energy system that is both economically and environmentally sustainable, and that guarantees both the reliability and quality of energy supply at reasonable prices through markets that work properly, transparently, and with real competition, all for the benefit of consumers and users.

It is well-known that there are some positive elements to the Spanish electrical system. It is a system in which power sources are highly diversified, with a generation mix that has incorporated non-dispatchable renewable energy and a meshed transmission and distribution grid allowing for a reasonable quality supply. Smart metering equipment is already being installed on the grid that will allow consumer-side demand management, promoting a more dynamic retail market and improved management of distribution networks.

This system is, first and foremost, structured around a liberalised wholesale electricity market which has come to encompass new sources, such as combined cycles and different renewables.

The retail market, for its part, has also trended toward growing liberalisation, first with the gradual disappearance of comprehensive rates and the introduction of the reference supply. It is true that concentration in this market is greater than in the wholesale market, but a positive trend can be seen, especially in the last few

years, with the arrival of new distributors unconnected to traditional groups, especially in the industrial sector.

Now then, the Spanish electrical system does still have several weaknesses: for instance, the low degree of physical interconnection with the rest of Europe's markets. So, despite the success represented by the recent connection of the Iberian Electricity Market with the main European wholesale markets through harmonisation and a single matching algorithm and mechanisms for assigning capacity and managing common bottlenecks, our connections across the French border do not provide for more than some 1,400 MW of commercial interconnected capacity, far below the goal of 10% set in the European summit in Barcelona over a decade ago. This remains a great challenge: to increase interconnection, both to improve the reliability of supply at a lower cost and to bolster competition and bring prices into line with those in the rest of Europe and ensure that they are not excessively volatile.

This clearly positive view of the electrical sector is the product of a structural analysis, but it cannot obscure the complicated situation that the electrical sector has arrived at in the past few years due to the contraction of electrical demand (demand in 2013 was at the same level as in 2005) and rising regulatory costs. The combination of both of these factors has put the economic and financial sustainability of the sector at risk as it has generated a deficit in regulated activities that has reached 40.4 billion euros, 28.5 billion of which are still pending payment. This deficit could not be eliminated by conventional means, such as raising tolls, despite the fact that they did raise by 122% between 2004 and 2012. The consequently high price of electricity has negatively affected our economy, both in the industrial sector and in the retail and services sector and home markets, becoming a serious concern for many citizens.

The clear risk that the discrepancy between income and costs might lead to the entire electrical system becoming economically and financially unsustainable has given rise to a reform, the main instrument of which is Law 24/2013 of 26 December, on the Electrical Sector, albeit with new, complementary regulations. The reform has focused on a return to balance, both in terms of income – the income base had already been broadened with tax measures in 2012 – and of regulatory costs, for which there has been a legislative change to reduce them both in the near and long terms, with measures aligned with the general interest.

With regard to the gas sector, like the electrical sector, it has undeniably positive elements, most significantly the diversification of gas sources, which allows Spain to limit its dependence on a single producer, situated the country, with its high

capacity for regasification, in a special position compared to its European partners who are prone to supply difficulties as a result of geopolitical tension. In this sense, the Spanish gas system could be an exceptional platform from which to search for alternative routes to guarantee the security of Europe's supply.

Nonetheless, the Spanish gas system is facing a fall in demand, which began in 2008, as well as the rising costs of infrastructure that was planned under the assumption that demand would grow strongly as it did in the first few years of this century. This situation, as in the electrical sector, is generating a nascent deficit and, consequently, a shadow of doubt about the economic and financial sustainability of the sector in the medium and long terms. That is why now is the time to act to ensure the economic and financial sustainability of the gas sector before this nascent deficit destabilises the system.

In this sense, reform of the gas sector must have the goal of ensuring the sector's economic and financial sustainability of the sector.

In any case, the energy regulation of the gas sector should progress toward the creation of a domestic market for sustainable gas with higher service quality, guaranteeing consumers reasonable prices, improving interconnection, encouraging commerce and competition and bolstering the security of the supply.

Having made this brief point regarding the fundamental problems of the energy sectors, I would like to talk about some of the more specific challenges we are dealing with in the CNMC, an institution that, as you know, has merged the authorities for supervising economic sectors with the authorities for supervising competition. I am going to highlight the most relevant challenges in which the most progress has been made.

With a markedly horizontal nature, the finishing touches are now being put on the development of a methodology for calculating tolls for transmission, distribution and access to electricity grids – and likewise for gas networks – following the criteria of sufficiency, economic efficiency, transparency, objectivity and non-discrimination, such that users pay for the costs of that their supply creates for the system, avoiding cross-subsidies between users and activities and incentivising efficient consumption.

In direct relation with this, the CNMC's technical services are developing Regulatory Information on Costs for the activities of electrical transmission and operation of the national electrical system, as well as the transport of natural gas, regasification, underground storage of natural gas and technical management of

the gas system; and likewise, minimum requirements that auditing firms must meet to verify any investments or costs requested by the CNMC in relation with the activities regulated for remunerative purposes.

Furthermore, the CNMC is implementing new functions that correspond to the national authority within the framework of (EU) Regulation No. 1227/2011 of the European Parliament and the Commission of 25 October 2011 on wholesale energy market integrity and transparency, REMIT, understood as the cash and futures markets for electricity and natural gas, taken together, with physical or financial liquidation, in each one of the Member States.

In the Spanish market, the CNMC is responsible for ensuring compliance with the prohibitions on operating with privileged information and manipulating the market, as well as the obligation to publish privileged information; for the creation of a National Register of market participants in which all parties involved in wholesale energy operations must register if obligated to report to ACER; and for regional cooperation with other energy regulators.

Another fundamental area where we act is in the supervision of the separation of accounts and compliance with the accounting requirements established in sector-wide legislation. Among them, those related to transparency between services rendered and costs borne by other entities of the group and involved parties, including the margins added by the transfer price policy; the existence of explicit and specific criteria for assigning assets, liabilities, expenses and income to the different activities; and the transparency in the information provided regarding costs necessary for proper establishment and review of the remuneration for regulated activities.

This supervisory task is extensible to that of legal and functional separation, to increase transparency in the functioning of both free and regulated activities in the natural gas and electricity sectors for the purpose of avoiding cross-subsidies and increasing competition in said sectors.

More specifically, in the gas market the CNMC is actively working on the creation of an Iberian gas hub (MIBGAS), transparent, liquid, deep and with no counterparty, in which standardised liquid products are negotiated on an electronic platform with a market operator to facilitate the transactions and contribute to market liquidity.

Additionally, in the framework of European organisations, the CNMC is working on the development of Framework Directives and Network Codes. CNMC Notices

establishing bottleneck management mechanisms have already been approved, along with a notice establishing mechanisms to assign capacity to apply to international connections. The next challenge will be to approve Notice on balance and implementation of certain issues described in various Network Codes, such as harmonisation of gas days, modification of the reference temperatures for combustion fumes and modification of the nomination and renomination cycles.

Last, but not least, the CNMC has just taken over the task of supervising supplier changes, so the activity of market agents is not distorted and consumers' free choice of distributors is guaranteed. This is part of the task of improving consumer knowledge of the way the retail electricity and natural gas market works while, at the same time, supervising the application of consumer protection measures.

Let me end by thanking once again the organisers of this Conference, which is taking place at a critical moment for Europe's energy sector and policy.