



The 2006 Report
on the Activities and Finances
of the Energy Regulatory Office

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This annual report of the Energy Regulatory Office ("Office") for 2006 provides information about the Office's work during the next stage of electricity and gas market opening and its other activities.

In the electricity industry, on 1 January 2006 the remaining protected customers – households – became eligible customers enjoying the right to select their electricity supplier. Thus, the market has been opened up completely in this area, and under Act No. 458/2000 on Conditions for Business and State Administration in the Energy Industries and Changes to Certain Laws (the Energy Act), as amended, the Office has the competencies to regulate activities in those areas of energy industries, in which competition is not feasible. Such activities include, in particular, electricity transport and those related to ensuring the financial and technical stability of electricity systems (i.e. the provision of system services in the electricity industry and the electricity market operator's activities) and also support for electricity generation from renewable and secondary resources and support for combined heat and power generation. In the areas in which the Office is authorised to control prices, these prices (or their growth) have remained substantially below the rate at which the price of energy has been increasing, usually at the level of annual inflation, throughout the Office's existence. (An example is the latest change in electricity prices on 1 January 2007: the regulated part of the price rose by 1.2 per cent on average year-on-year, while the unregulated part, i.e. the price of energy, rose by 16 per cent on average).

At the beginning of 2006 electricity distribution companies were legally unbundled, and independent companies providing distribution services and trading in electricity emerged.

Electricity generation from renewable resources developed relatively well. The buyout prices and green premiums further stimulated the development of this market segment. Work continued on specifying more precisely the basis for setting the prices of electricity generated in plants that use renewable energy resources. This activity was completed by issuing a price assessment for 2006, whereby the buyout prices of electricity from renewable resources increased by 2 per cent on average (with the exception of electricity from wind power plants).

The situation was different on the gas market. In the light of the experience in 2005 the Office reimposed controls on the commodity charge for all customer categories. The Office was compelled to decide, effective from 1 January 2006, to place temporary restrictions on the prices of gas supply, in the form of caps on the natural gas storage prices charged by RWE Transgas, a.s. and caps on the selling prices charged by traders of distribution companies that buy natural gas from the above company. The Office adopted this measure on the basis of the unfavourable experience after the first stage of the liberalisation of the gas industry. However, this measure did not constrain the emergence of competition on the Czech gas market at all (in addition to RWE Transgas, a.s., WINGAS GmbH and VEMEX, s.r.o. import natural gas into the Czech Republic), and did not prevent eligible customers from exercising their right to the selection of their gas supplier or to opt for a different pricing principle.

Throughout 2006 intensive talks were under way with gas companies and the Office for the Protection of Competition about the way in which the conditions on the gas market should be adjusted in order for the market to function well from the perspective of both the customers and gas companies' interests. This resulted in, among others, the adoption of completely new gas market rules and in the setting of the conditions for the demerger of the natural gas TSO in 2006.

During 2006 gas distribution system operators prepared their legal unbundling and demanded that the costs incurred in this process be reflected in prices. The Office examined these demands and included only justifiable and demonstrated minimum costs of unbundling in the prices of regulated activities, applying the same methodology as in the electricity industry in 2005.

The Office is a recognised arbitrator. It decides in disputes in administrative proceedings under the Energy Act, dealing with those arising between licence holders or between a licence holder and a customer, and in other areas of the electricity, gas and heat supply industries. Last year the Office dealt with 150 suggestions and complaints filed by customers and 52 questions raised under Act No. 106/1999 on Free Access to Information.

In respect of district heating, last year the Office focused again on maintaining stable business conditions, which had been introduced in 2005, for heat supply companies. These conditions motivate suppliers to rationalise their costs of thermal energy production and distribution. In addition to directing the conditions for pricing, the Office also has the remit to resolve disputes between thermal energy producers, distributors and customers. Most of the thermal energy suppliers carry on their business in an ethical manner and refrain from increasing thermal energy prices disproportionately; in spite of that there are dozens of disputes, complaints and suggestions, which the Office must address in the heat supply industry.

The Office holds an important position in the licensing of business in the energy industries and in reviewing the conditions subject to which it has issued licences.

In the interests of final customers in the low-demand segment the Office has placed information about electricity supplier switching options and methods on its website, together with a ready reckoner helping to make the required calculations and then select a supplier suitable from the perspective of electricity consumption nature and size. In the gas industry, the Office has put in place the preconditions for gas supply safety and introduced, among other things, the institute of the supplier of last resort for small customers, including the reasonable prices to be charged by such suppliers. Final customers now also have on-line access to information about the latest price development, including natural gas quality.

In 2006 the Office carried out all its tasks in the legislative area and as regards improvements to the regulatory framework, including the start of preparations for an amendment the Energy Act and co-operation with the European Commission's bodies responsible for the energy sector. The Office cooperated with central authorities of the Czech Republic's state administration, as well as with CEER and ERGEG. Under a Phare project the Office shared its experience, together with the Italian and Austrian regulators, with the Ukrainian regulatory authority.

Regional initiatives on the electricity and gas markets, aimed at removing barriers to free trade at the regional level and at creating single European electricity and gas markets, continued in 2006.

In co-operation with the Ministry of Industry and Trade, the Office prepared the second National Report of the Czech Republic on Electricity and Gas Industries for 2005.

In co-operation with the Ministry of Informatics, during the year high-quality data transmission lines between the Office's head office in Jihlava and its Prague offices were built, and helped to improve access to IT services inside the Office, enhance the security of access to the Internet, and ensure the provision of the maximum possible amount of information to outside users.

This annual report also offers a brief outline of the Office's co-operation with state administration, local governments and the public. A separate chapter is devoted to the management of the Office's budget.

I am pleased to note that last year the Energy Regulatory Office carried out all the challenging tasks with which it is assigned under the law, as well as unforeseen work. I would like to express thanks to all those who contributed to this good performance.



Josef Fiřt

Chairman, Energy Regulatory Office



The Energy Regulatory Office (hereinafter also referred to as “ERO” or “the Office”) regulates the market to substitute market mechanisms in the energy industries, in which competition is not feasible and a monopoly situation may be abused.

In the energy sector, the Office creates the preconditions for the proper functioning of competition, protects consumer interests and those of licence holders, oversees the licence holders’ adherence to the conditions for business, and creates the preconditions for reliable supplies of electricity, gas, and heat.

1.1 The position of the Energy Regulatory Office

The Energy Regulatory Office was established as of 1 January 2001 by Act No. 458/2000, on the Conditions of Business and State Administration in the Energy Industries and Changes to Certain Laws, as amended (hereinafter referred to as “the Energy Act”), as an administration authority for regulation in the energy sector.

Under Section 2, subsection 1, point 10 of Act No. 2/1969, on the Establishment of Ministries and other Central State Administration Authorities of the Czech Republic, as amended, the Energy Regulatory Office is “another central authority of state administration” with its own national budget title, no. 349.

1.2 Main developments on the energy market in 2006

Regulation in the gas industry

On the basis of initial experience with liberalisation in the gas industry the Office was compelled to impose, on 1 January 2006, temporary restrictions on gas supply prices; it applied caps on the prices of natural gas storage charged by RWE Transgas, a.s. and on the maximum sales prices charged by the traders of distribution companies who bought natural gas from the above company.

The measure adopted by the Office in no way constrained the emergence of competition on the Czech natural gas market, and did not prevent eligible customers from exercising particularly their right to gas supplier choice or to select a different pricing principle.

Changes to the legislative framework

Due to the introduction of a new gas market model a new statutory instrument (‘public notice’) laying down the rules for the needs of the completely opened market was adopted.

The Office provided for the required quality of the supplies and services related to regulated activities in the gas industry in a public notice on the quality of gas supplies and related services in the gas industry.

The amendment to the public notice on the electricity market rules brought about a fundamental change, which concerned secondary control pricing and the related changes in system imbalance pricing.

Electricity market liberalisation

On 1 January 2006 the last group of protected customers, households, became eligible customers who have the right of supplier choice, and the market was therefore completely opened. Since then the Office has only been regulating transmission and distribution activities in the electricity industry.

Unbundling

In 2006 gas distribution system operators effected legal unbundling and required that the costs incurred in this process be reflected in prices. The Office included the justifiable and demonstrable minimum costs of unbundling in the prices of regulated activities, applying the same methodology as in the electricity industry in 2005.

International relations

In co-operation with the Ministry of Industry and Trade the Office prepared the second national report, i.e. *The Czech Republic’s National Report on the Electricity and Gas Industries for 2005*.

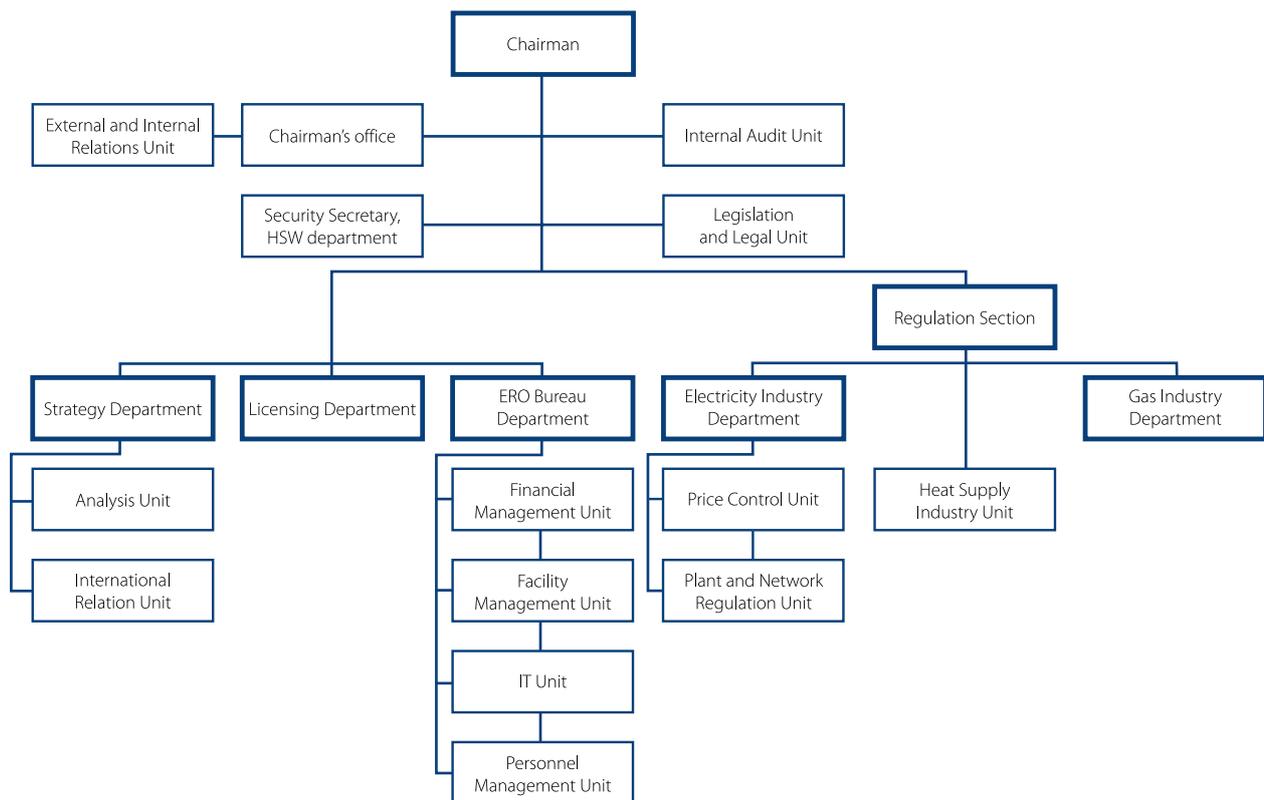
In 2006 some regional initiatives in the electricity and gas markets were launched; their objective is to remove the barriers preventing free trade at the regional level and to gradually create single European electricity and gas markets.

Implementing the Integrated Information System at ERO

In co-operation with the Ministry of Informatics, during the year high-quality data transmission lines between the Office’s head office in Jihlava and its Prague offices were built, and helped to improve ERO employees’ access to IT and to enhance the security of access to the Internet.

In 2006 the work that had been started in mid-2005 on the ERO Integrated Information System (IIS) continued. The implementation was planned in three independent stages. In line with the timetable, on 1 January 2006 the routine operation of the first stage was started, covering the modules of licences and control of entities and operations, which mainly the Office's licensing department uses for its agenda. In April the routine operation of the second stage was started. This involved the migration and putting into operation of the Energy Regulation Fund; in mid-2006 a new filing service was introduced for the whole Office. In the autumn the filing service was extended to include an archiving module. At that time the third stage of the IIS was under way, focused on the reporting module. This stage was to be put into routine operation in the second quarter of 2007 when the data reported by regulated entities for 2006 is to be processed in the new system.

1.3 Organisational structure as at 31 December 2006



Chairman	Josef Fiřt
Vice-Chairman and Director of the Regulation Section	Blahoslav Němeček
Head, Licensing Department	Luděk Pražák
Head, Electricity Industry Department	Stanislav Trávníček
Head, Gas Industry Department	Sylva Škrdlová
Head, Strategy Department	Martina Veselá
ERO Bureau Department	Viktor Kirschner

Key changes in the legislative framework for regulation in the energy industries

2



In 2006 work continued on amendments to and development of implementing legal regulations, the need for which was precipitated by the so-called large amendment to the Energy Act, i.e. Act No. 670/2004, which amends Act No. 458/2000, the Energy Act, as amended. The Office followed up on its legislative activity in 2005 and issued the following implementing regulations [statutory instruments – public notices].

2.1 No. 51/2006, on the conditions for connection to the electricity grid

This public notice of 17 February 2006 repealed those on the connection conditions, i.e. No. 297/2001, which lays down the conditions for connecting and electricity supplies to protected customers, and No. 18/2002, on the conditions for connecting and electricity transport in the electricity grid, and effective as from 1 March 2006 constitutes delegated legislation on the conditions of connecting electricity market participants to the electricity grid.

This statutory instrument is based on the following principles:

- a) Lay down general and uniform conditions for connecting electricity market participants;
- b) Simplify the connection conditions and ensure the required power input/output;
- c) Determine the share of the costs incurred in connection and in ensuring the reserved power input required by the applicant, using unit prices;
- d) The compensation for damage caused by unauthorised electricity take must be primarily based on identifying the actual situation.

2.2 No. 524/2006, laying down the rules for the organisation of the gas market and for the development, allocation and use of typical gas supply profiles

In 2005 and 2006 a need arose to amend the then applicable public notice that laid down the rules for the organisation of the gas market, due to the completion of the gas market opening process, because all final customers would be eligible customers from 1 January 2007 and the gas market would therefore be fully liberalised, and due to the assessment of the experience with the application of the Energy Act and Public Notice No. 542/2005, which amends No. 673/2004, which lays down the rules for the organisation of the gas market.

Public Notice No. 524/2006, laying down the rules for the organisation of the gas market and for the development, allocation and use of typical gas supply profiles, of 24 November 2006, therefore entered into force on 1 January 2007, with the exception of Section 27, which became effective on 1 April 2007.

This instrument is based on a new gas market model, adjusted in connection with the full liberalisation from 1 January 2007. One of the major changes in comparison with the previous regulation is the introduction of the so-called virtual trading point, which will make more flexible gas trading possible throughout the Czech Republic. No. 524/2006 provides for certain new terminology, defines different procedures for booking capacity in the transmission and distribution systems, and sets out the methods for nominating and renominating daily gas supply profiles for practical use on the gas market, for commercial balancing and settlement of imbalances, metering and processing of readings, and the development, allocation and use of typical gas supply profiles, and deals in more detail with gas supplier switching. It also lays down new provisions on supplies by two and more gas traders to one supply point and on the short-term market of gas and unused tolerances.

2.3 No. 545/2006, on the quality of gas supplies and related services in the gas industry

The Energy Act requires licence holders to keep the stipulated parameters of the quality of supplies. Should they fail to keep them, they have to provide compensation as specified in a public notice. In addition to this general obligation, in its special part the Energy Act imposes an obligation on licence holders to keep the parameters, and publish the indicators, of the quality of gas supplies and the related services as laid down in an implementing legal regulation. In its Public Notice No. 545/2006, on the quality of gas supplies and related services in the gas industry, the Office therefore provided for the required quality of the supplies and services related to regulated activities in the gas industry, including the compensations for failure to comply, setting out the time limits for raising compensation claims and the procedures for reporting the observance of the quality of supplies and services.

At the same time this public notice repealed No. 329/2001, which lays down the conditions for connecting and supplying protected customers, since the protected customer category would no longer exist on the gas market from 1 January 2007 in accordance with the Energy Act and in line with the gradual opening of the gas market. All final customers would be eligible customers.

2.4 No. 552/2006 amending No. 541/2005, on the Electricity Market Rules and principles of pricing the electricity market operator's activities and on the execution of certain other provisions of the Energy Act

One year on from the entry into force of the public notice on the electricity market rules the Office evaluated the information received from market participants about the instrument's benefits for the Czech market and its application in practice. On the basis of analysing this information the Office decided to draw up an amendment to No. 541/2005 for 2007.

In particular, this amendment

- a) specifies more precisely and extends the provisions on relationships between electricity market participants in respect of electricity supply and regulated service billing,
- b) introduces the evaluation of capacity booking at supply points electrically connected by the entity's own electrical network,
- c) specifies more precisely agreements on the provision of balancing energy and electricity procured by the TSO for controlling the transmission system and the related provisions on the balancing energy market,
- d) specifies more precisely the until then existing legal provisions on the rounding of values in calculating imbalances,
- e) changes the procedure for imbalance clearing and financial settlement, including the flows of funds obtained from imbalance settlement,
- f) broadens the scope of the information that the electricity market operator is obliged to make available or provide to electricity market participants under the law,
- g) specifies more precisely the procedure for electricity supplier switching and newly introduces provisions on the selection of electricity supplier when a final customer's supply point is being newly connected to the electricity grid.

A material change contained in the instrument concerns the evaluation of the pricing of secondary control, and the resulting changes in the pricing of the system imbalance. Because of the rising prices of energy, the system existing until then did not motivate entities to minimise imbalances; on the contrary, the risk of extreme imbalances was increasing so much that it might have exceeded the TSO's options for procuring sufficient quantities of balancing energy to ensure the electricity grid's stability.

3



3.1 The market in 2006

3.1.1 Complete market opening

The Czech electricity market was being opened up step-by-step from 2002. The market has been fully liberalised since 1 January 2006 when the last group of customers – households – became eligible customers and acquired the right of supplier choice. None of the activities in which competition is feasible, i.e. electricity generation, electricity imports, and electricity trading, are regulated on the open market any longer. Only activities having a monopoly nature continue to be subject to regulation; they include electricity transport from the generating plant over the transmission and distribution systems to the final customers and also activities related to providing for the energy system's stability in both technical and commercial terms.

3.1.2 Unbundling

The requirements for the legal unbundling of the various activities related to electricity generation, distribution and sale at integrated power utilities in the Czech Republic arose from Directive 2003/54/EC¹⁾, which had been reflected in an amendment to the Energy Act.

Under the Energy Act, distribution system operators with more than 90,000 customers must separate distribution from the other licensed activities, i.e. effect the so-called unbundling. In the Czech Republic, only the three largest groups operating in the electricity industry were obliged to separate distribution from their other licensed activities, namely the ČEZ Group, the E.ON Group, and the PRE Holding Group. These companies effected unbundling as from 1 January 2006.

3.1.2.1 Compliance Programme

In connection with the separation of the various activities there was a need to meet the obligation of providing non-discriminatory access to distribution systems for all electricity traders. To support oversight over non-discriminatory conduct, which is the objective of unbundling, a so-called Compliance Programme was put in place.

Under the Energy Act, distribution system operators are obliged to adopt, through their own internal directives, a programme that lays down measures precluding discriminatory behaviour to other electricity market participants, in particular as regards access to the DSOs' distribution systems and use of their services.

In the initial Compliance Programmes, prepared in 2005, distribution companies set out their measures and undertook to carry them out. In 2006 distribution companies first drew up Reports on Implementing the Compliance Programme, and in accordance with the law submitted them to the Office and the Ministry of Industry and Trade (MPO) and published them on their websites.

The Office analysed the submitted reports and in October and November 2006 its staff met with the Compliance Officers of all distribution companies to gain thorough knowledge of the internal directives through which the specific ways of implementing each of the measures were addressed.

The Office did not identify any serious mistakes on the part of the distribution companies when it analysed the reports or met with the Compliance Officers; however, the reports submitted failed to address specific problems, they were of only a general nature, and were not uniform. The Office therefore initiated a harmonisation of the relevant documents on the basis of a single structure. The discussions on document harmonisation were held together with the MPO, which is responsible for this issue together with the Office under the Energy Act.

In this area the Office also focuses on informing the regulated entities on a regular basis about the progress of the unbundling process and the drafting of documents in the non-profit Council of European Energy Regulators (CEER) and the European Regulators Group for Electricity and Gas (ERGEG). At the end of the year the companies were provided with information about a document offering guidelines on functional and information unbundling, drawn up in CEER, which specified further steps in unbundling related to the managerial and information separation of distribution from trade. Companies were also notified of the opportunity to respond to this document in a public consultation.

3.1.3 Tools for improving customers' information and orientation on the liberalised market

The complete opening of the electricity market precipitated the need to inform final customers about the electricity supplier switching option itself and, above all, the process of transferring to a different supplier. On its website the Office therefore published a very clear 'instruction manual' for final customers in the household category; they can use it when they decide to change their electricity supplier. At the same time the Office published a list of the electricity traders among whom customers can choose their supplier.

¹⁾ Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003, concerning common rules for the internal market in electricity and repealing Directive 96/92/EC.

In connection with the completed process of electricity market opening and the Office's effort to provide customers with as complete information as possible for their decision-making on supplier choice, the Office also placed an interactive ready reckoner of payments for electricity supplies on its website. With the help of the reckoner low-demand customers connected to the low voltage level have an opportunity to compare, on the basis of the data they enter (the distribution rate, annual consumption), the costs of electricity supplies from the various suppliers, and find the most appropriate supplier with regard to the nature and size of their consumption. The reckoner is updated on a quarterly basis, depending on information from the suppliers who have provided the Office with their price quotations on energy products intended for low-demand customers. Suppliers are not subject to any statutory obligation to publish their price lists, or to submit them to the Office, and the reckoner therefore does not contain quotations of all the suppliers operating on the electricity market.

To support better orientation in the issues concerning electricity supplies on the liberalised market the Office set up a link to Frequently Asked Questions on its website; the FAQ section summarises customers' typical questions and answers them in an intelligible way.

3.2 Price formation and setting

As from 1 January 2007 the resulting price of supply for all final customer categories is composed of controlled prices of distribution and system services, the charge to cover the extra costs incurred in support for electricity generation from renewable resources, CHP and secondary resources, and the charge for the market operator's activities, and the uncontrolled price of energy.

At the low voltage level, the same scope of tariffs as in 2006 has been maintained for 2007 for small businesses (low demand, category C) and households (low demand, category D).

Table 1 shows the development of regulated items for household customers from 2005 to 2007.

Table 1 Regulated items for customers in the household category

Regulated items	2005 [CZK/MWh]	2006 CZK/MWh	2007 [CZK/MWh]	Percentage share of price components 2007 [%]	Change in price components 2007-2006 [CZK/MWh]	Change in price components 2007/2006 [%]
Electricity market operator's (OTE) charge for clearing, related to demand of final customers, including local consumption	4.63	4.63	4.63	0.35	0.00	0.00
Charge for system services	171.80	156.28	147.15	11.14	-9.13	-5.84
Charges to cover the extra costs related to electricity purchase from renewable resources, cogeneration, and secondary resources	39.45	28.26	34.13	2.58	5.87	20.77
Network services:						
Charge for the DSO for payment mediation	0.10	0.10	0.10	0.01	0.00	0.00
Contribution to distributed (decentralised) generation for plants connected to the distribution system	7.52	7.48	9.45	0.72	1.97	26.34
Cumulative single-component price for the network service	1,026.92	1,108.05	1,124.88	85.20	16.83	1.52
Total for regulated items	1,250.42	1,304.80	1,320.34	100.00	15.54	1.19

3.2.1 Controlled components of the electricity supply price

Charge for the electricity market operator

For 2007 the charge for the electricity market operator's activities has been maintained at CZK 4.63/MWh. This charge covers the costs incurred by Operátor trhu s elektřinou, a.s. [OTE] in activities related to balancing electricity supply offers and electricity take bids, clearing the imbalances between the planned and actually supplied/taken electricity quantities between the various market participants, organising spot electricity markets, and preparing overviews of long-term consumption in the Czech Republic, and in certain other activities that the company carries out under the Energy Act. The costs incurred in providing for all these activities are, as regulated payments, paid by all final customers in the form of a contribution to the price of the electricity consumed (taken).

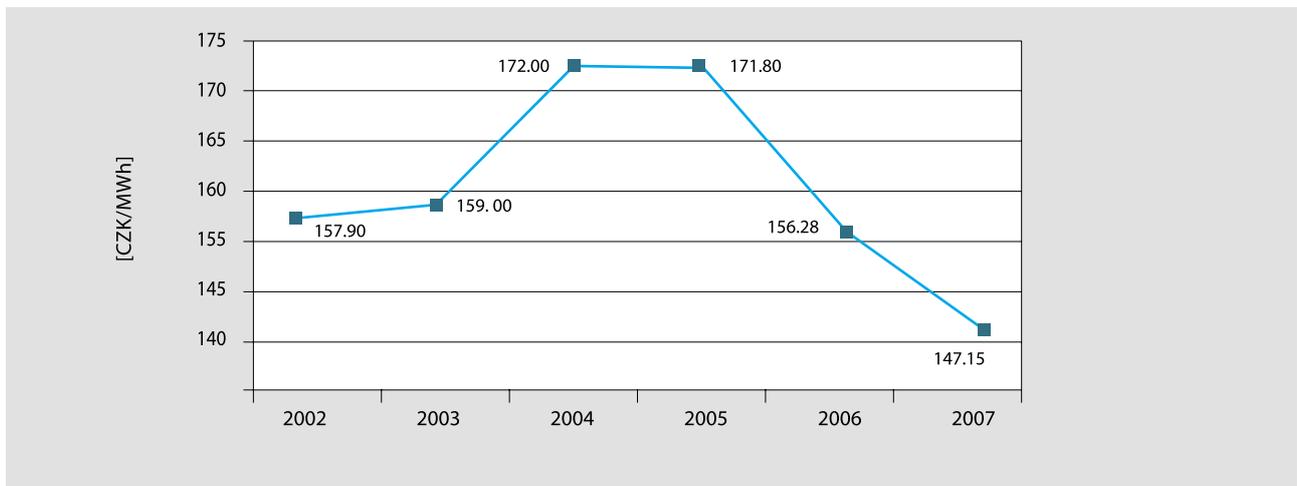
Charge for system services

System services are necessary for ensuring the balance between electricity generation and electricity demand. The transmission system operator, ČEPS, a.s., provides these services by purchasing ancillary services from their providers. Simplifying somewhat, ancillary services can be described as the readiness of those power stations that do not directly generate electricity for supplying final customers but work as reserves for the event of a sudden failure of other capacities or sudden changes in the load on the electricity grid, which are caused by sudden changes in demand or generation. The costs of these ancillary services are reflected in the prices to final customers in the form of the charge for system services.

The downward trend in the costs of ancillary services, attributable to the stabilisation of the system, and increasing demand resulted in a drop in the charges for system services by CZK 9.13/MWh to CZK 147.15/MWh.

System service prices from 2002 to 2007 are shown in Chart 1.

Chart 1 System service prices



Charge for network services

The network service charge is composed of a charge for transmission services and a charge for distribution services. The network service charge for 2007 will be influenced by several key factors as follows:

Transmission service charge

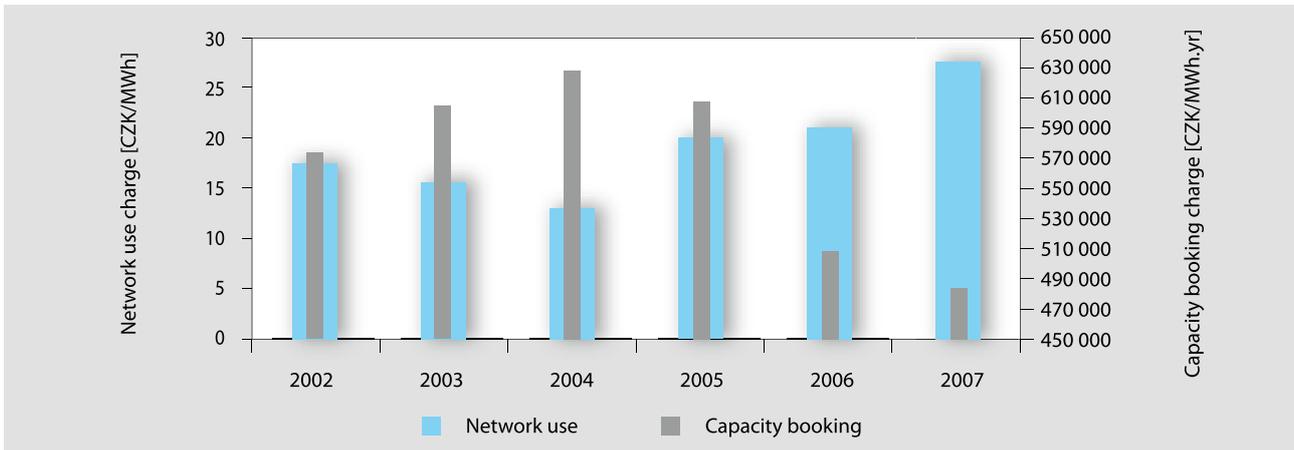
The charge for using the transmission system's services has risen from CZK 21.13/MWh in 2006 to CZK 28.08/MWh in 2007. This significant growth, caused by the rising prices of energy bought by the TSO to cover losses, has also been reflected in the charges for electricity distribution at lower voltage levels.

Acting in the opposite direction to this trend is the reduction in the unit price for booked capacity at the transmission system level, which is due to including a considerable portion of the proceeds from auctions on cross-border interconnections in the calculation of prices, in line with Regulation 1228/2003/EC of the European Parliament and of the Council²⁾. Another part

²⁾ Regulation 1228/2003/EC of the European Parliament and of the Council of 26 June 2003 on conditions for access to the network for cross-border exchanges in electricity.

of the proceeds from these auctions is used by the transmission system operator for CBT compensation payments between the national TSOs in the EU and also for the development of the transmission networks (mainly in the area of cross-border interconnections). Chart 2 shows the prices for electricity transmission.

Chart 2 Components of the price for electricity transmission



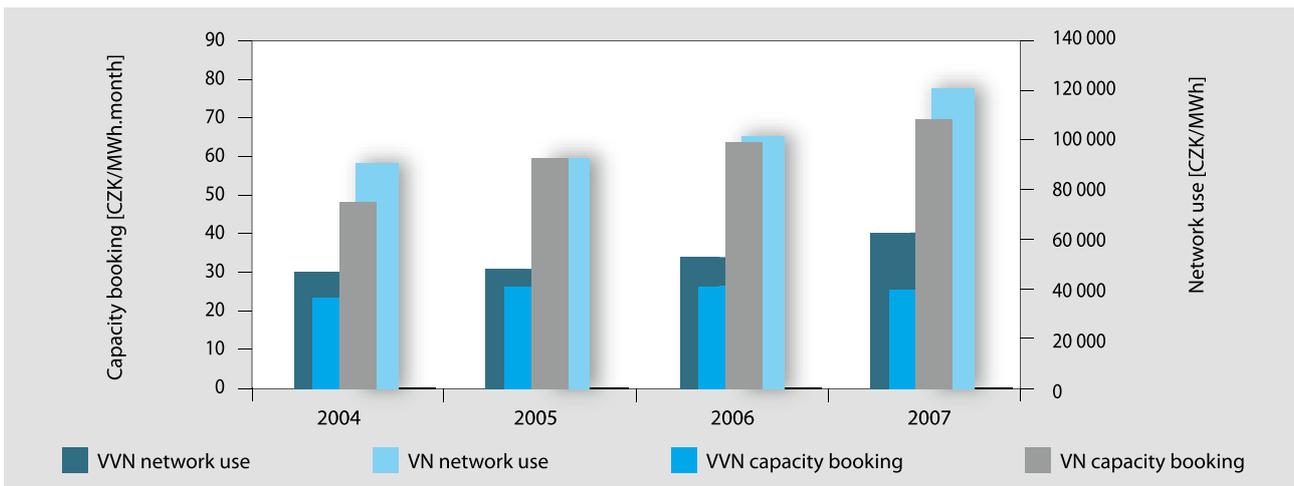
Distribution service charge

The higher prices for network use, which influence the variable part of the distribution rates, were due to the wholesale market's significantly higher prices of the energy bought by distributors for covering their losses.

The charges for booked capacity at the various voltage levels are mainly influenced by technical units (the size of the capacity reserved by customers). While at the very high voltage level a stabilisation of the situation can be observed, and the price within the Czech Republic is constant, in the case of the high voltage level final customers continue to reserve less and less capacity. This has an unfavourable influence on the unit price.

Chart 3 shows the development of both components of the distribution charge for very high voltage and high voltage levels from 2004 to 2007.

Chart 3 Components of the price for electricity distribution at very high voltage and high voltage levels



The charge for distributed generation

The charge for distributed generation takes into account the benefits of capacities connected directly to lower voltage levels, thanks to which the costs of losses in networks and in transformation at high voltage levels are reduced. The amounts of support for distributed generation at the various voltage levels have been maintained at the 2006 level.

Year-on-year, the final customers' resulting contribution to distributed generation has increased to CZK 9.45/MWh due to rising generation in distributed capacities.

The charge to meet the extra costs incurred in support for electricity from renewable resources, CHP and secondary resources

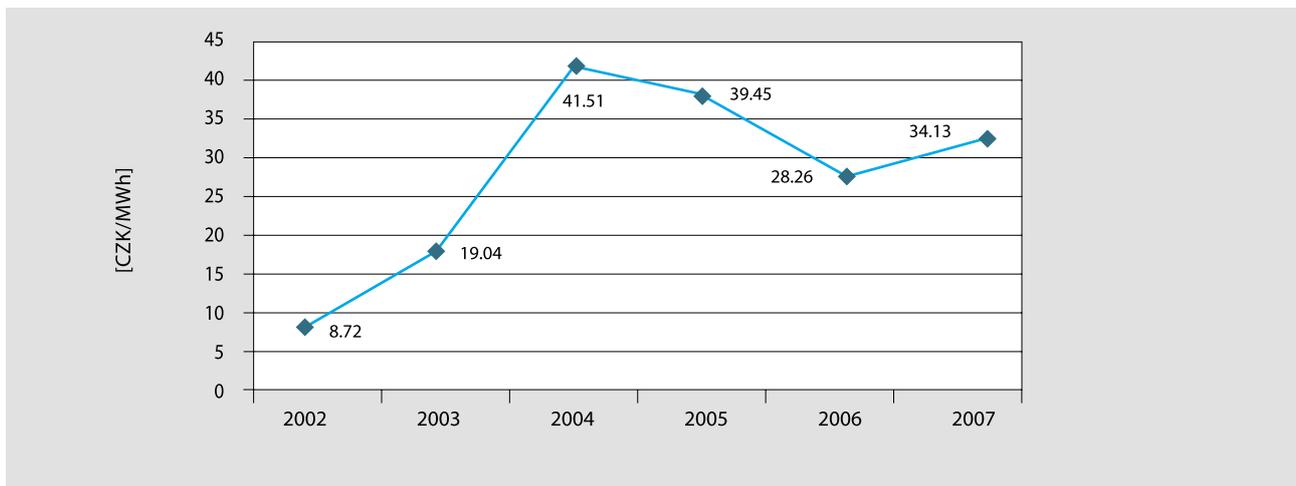
The charge to meet the extra costs incurred in support for electricity from renewable resources, CHP and secondary resources has risen from CZK 28.26/MWh in 2006 to CZK 34.13/MWh in 2007.

The increase in the contribution is mainly caused by the growing amount of electricity generation from renewable resources in connection with newly passed Act No. 180/2005 on support for electricity generation from renewable energy resources and on changes to certain laws (the law on support for renewable resources), which gives investors in environmental capacities a guarantee that the amount of support will be maintained for 15 years. This trend is most distinctly apparent in electricity generation from biomass and biogas; to a certain limited extent also a rising proportion of electricity generation in wind power plants can be registered. Not least, also the development of electricity generation in CHP and from secondary energy resources influences the level of the contribution.

In connection with the law on support for the use of renewable resources and also in connection with support for secondary resources and CHP under the Energy Act, an increase in the quantity of the supported electricity produced can be expected in the future, and therefore a gradual increase in the contribution.

Chart 4 shows the contribution from 2002 to 2007.

Chart 4 Charge to cover the extra costs incurred in support for electricity generation from renewable resources, CHP and secondary resources



Electricity prices to households

The resulting price of electricity supply to households is composed (as in all final customer categories) of regulated prices for distribution and related services, and the energy price, which is not subject to control, including the supplier's business margin.

The published average increase in the price of electricity supply for households for 2007, by 7.9 per cent, is mainly attributable to an increase of 16 per cent on average in the uncontrolled price of energy, which on average accounts for more than 52 per cent of the total costs for household customers (without accounting for the effect of VAT). The percentage shares taken by the various components of the resulting price of electricity supply to an average household customer are depicted in Chart 5 (the shares are including VAT). The increase in the electricity price for each individual customer differs depending on the selected tariff and the nature and size of consumption.

The overall increase in controlled prices for customers at the low voltage level, which the Office is able to influence, is 1.2 per cent on average for the whole Czech Republic, and basically only reflects outside factors having technical and financial impacts on the operation of networks (development of electricity production from supported environmental capacities, losses in lines, the rate of inflation, etc.).

Average prices of electricity supply and their components since 2002 are shown in Chart 6.

Chart 5 Percentage shares taken by each of the components that make up the average price of electricity supply to households for 2007

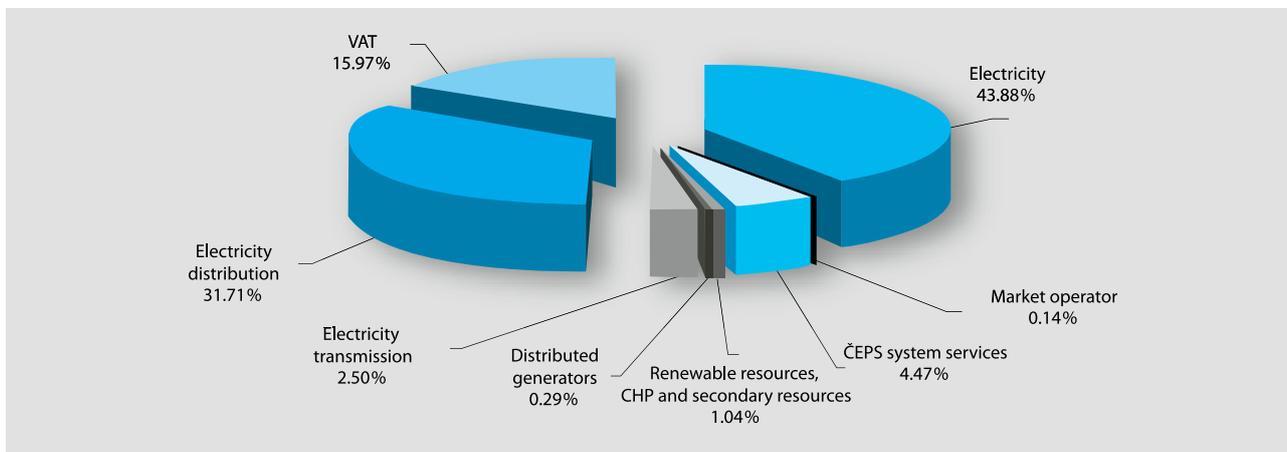
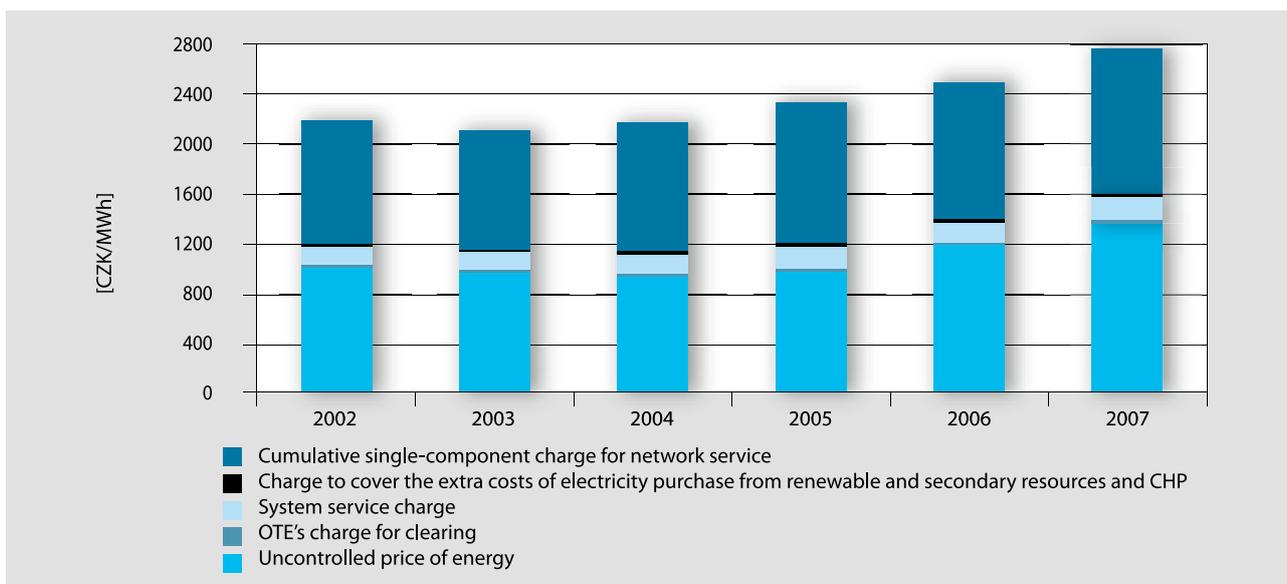


Chart 6 Average price of electricity supply to households



The year-on-year price rises for each of the regions, considering the regional suppliers' (the traders who are part of the same group as the respective distribution company) quoted prices, are listed in Table 2.

Table 2 Changes in the average prices to the households category in regions served by each of the suppliers between 2006 and 2007

Company	Households [%]
E.ON, a.s.	8.70
Pražská energetika, a.s.	7.90
ČEZ, a.s.	7.60

Prices charged by the supplier of last resort

The supplier of last resort is the last possibility of supplies for small customers and households who have the right to select their electricity supplier but have not found their supplier on the electricity market for various reasons. Under the Energy Act customers can also take supplies from a supplier of last resort in cases where their existing supplier has lost its ability to supply electricity.

Supplies of last resort take place for controlled prices. As from 1 January 2006 the Office sets, on an annual basis, prices of the electricity supplied to customers by the supplier of last resort.

For 2007 the prices of electricity supplied by the supplier of last resort have been calculated on the basis of energy quotations made by generators and traders and available on the electricity market. Characteristic load profiles (the so-called typical supply profiles), which were valued with the help of these available quotations of energy, were used for calculating the prices to be charged by the supplier of last resort in the various tariffs. The bands of the Rainbow Energy offered by the dominant generator, ČEZ, a.s., served as the basis for the valuation. It is to be kept in mind that the Office could not influence the price of energy on the generating side in calculating the prices for suppliers of last resort; the Office could only use the final energy products offered by generators and traders.

Final customers have not yet used the services of a supplier of last resort.

3.2.2 Uncontrolled prices

On the liberalised market customers can, by choosing their supplier, influence the uncontrolled part of the resulting electricity supply price, which is the commodity itself (energy), including the supplier's business margin.

Energy price

In 2007 the prices of electricity supply to all customer categories are influenced by the rise of the wholesale price of energy, which went up in the Czech Republic by more than 16 per cent on average year-on-year. This price hike is the result of the working of market mechanisms not only on the domestic market (the structure of capacities, future consumption, etc.), but it is also caused, due to the interconnection of grids, by demand and electricity prices in neighbouring countries.

The impact of the above increase in energy prices on the various customer categories differs by the nature and, primarily, size of a specific customer's consumption, i.e. in relation to the ratio between the payment for regulated items, set by the Office, and the uncontrolled price of energy. This can be felt most strongly by customers who use electricity for space heating, where the payment for the commodity taken (energy) makes up the predominant portion of the total cost of supply.

The energy price hike has also unfavourably affected the TSO's and DSO's costs of covering network losses.

3.3 Renewable resources, CHP, and secondary resources

In 2006 the Office set the support for renewable energy resources, secondary resources and CHP for 2007. It set the prices in accordance with the law on support for the use of renewable resources and the Energy Act. Buyout prices, green premiums and contributions to the energy price were published in ERO Price Decision No. 8/2006 of 21 November 2006, which lays down support for electricity generation from renewable energy resources, CHP and secondary energy resources.

Renewable resources

With a view to setting support in the form of minimum buyout prices and green premiums for 2007 correctly, in 2006 the Office held a number of meetings with associations that bring together generators of electricity from renewable resources and representatives of the competent governmental institutions. On the basis of the information so obtained the Office considered adjustments to the support for the period to come.

In respect of the buyout prices and green premiums, the principle of differentiation by the year of commissioning has been maintained. In respect of supported renewable resources the buyout prices were increased with regard to the industrial producers price index.

Green premiums for the various categories of resources, with the exception of biomass co-firing and parallel firing, have been reduced in comparison with the previous year. This reduction is due to the significant increase in the energy price on the Czech market to above the PPI level. The drop in the green premiums is fully set off by the rise in energy prices, while maintaining revenues per unit of electricity generation from renewable resources.

A change in the category of small hydroelectric power stations is the introduction of support in the form of green premiums for the high and low rate modes. At the same time the opportunity to apply double rates has been placed under more stringent rules. Only peak shaving or partly peak-shaving capacities can newly enjoy this form of support.

Wind power is the only type of renewable resource for which a new category has been created (wind power plants commissioned on or after 1 January 2007). For this category buyout prices have been set at the level of the 2006 buyout prices, i.e. the PPI has not been reflected in them. The main reason is the long-lasting decline in specific capital expenditure, which is also confirmed by European

studies, the decreasing EUR/CZK rate and, not least, stable steel prices on the world market, which influence the price of the wind power plants' towers and blades.

The 2007 buyout prices and green premiums for electricity produced from biomass take into account the rising prices of the fuels, which are used in the calculations - 2006 saw biomass price hikes on the market.

Green premiums for electricity produced by fossil fuel and biomass co-firing have been set so as to cover electricity generators' increased costs of biomass firing in comparison with the costs of coal firing. The increase in biomass prices is the reason why the green premiums have also increased for biomass co-firing and parallel firing.

In addition to biomass and coal prices, also the price of CO₂ emissions allowances influences the costs incurred by the electricity generators who use these fuels. The revenues attributable to allowances, generated by replacing coal with biomass, have been reflected in the green premiums for 2007.

CHP

Pursuant to the amendment to the Energy Act, since 2006 support for cogeneration has been granted to all categories of cogeneration units through a controlled premium on the electricity market price.

The amount of support for small cogeneration plants depends on two key factors - natural gas prices and market prices of electrical energy. In the case of natural gas a drop in prices was expected for 2007. Because of the situation on the electricity market, the prices of energy entering the calculation of the premiums for 2007 were considered 16 per cent higher than in 2006. The increase in energy prices on the market will be reflected in generators' higher revenues from the electricity they sell. Having reflected these key factors in the calculation of the premiums for 2007, the resulting premiums were lower for all CHP categories firing natural gas.

The motivating amount of premiums has been maintained in the case of large, over 5 MWe cogeneration units and also for all CHP categories firing renewable resources or drained gas.

An alternative option to select the duration of the high rate has been introduced for CHP.

Secondary resources

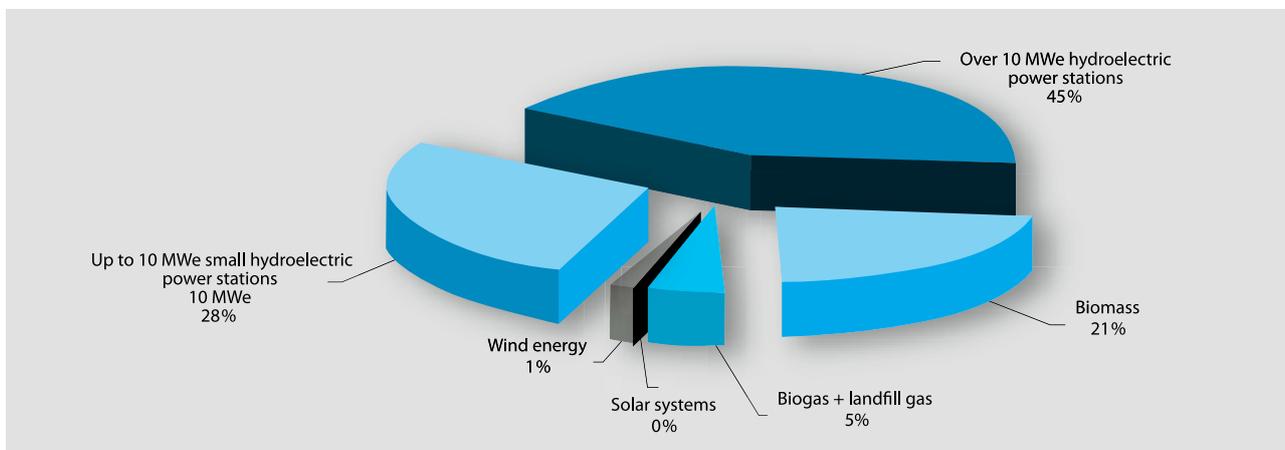
To differentiate between the levels of support for secondary resources, two secondary resource categories have been maintained: electricity generation from drained gas and electricity generation from secondary resources. The Office expects a more detailed breakdown of the secondary resource category in the years to come.

Statistics on renewable resources

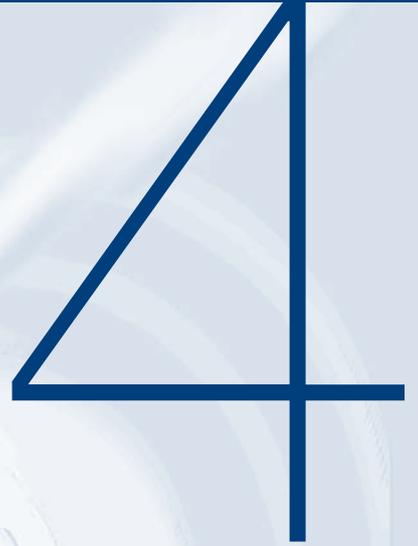
For 2006 the preliminary amount of electricity generated from renewable resources is 3.50 TWh. In that year gross electricity consumption in the Czech Republic amounted to 71.73 TWh. Electricity generation from renewable resources accounted for 4.87 per cent of gross electricity consumption.

Chart 7 indicates the shares taken by the various renewable resource categories in total electricity generation from renewable resources in 2006.

Chart 7 Categories' share of total electricity generation from renewable resources in 2006







4.1 The market in 2006

Liberalisation of the Czech gas market continued in 2006 by the second stage of market opening. On 1 January 2006 all final customers for natural gas with the exception of households became eligible customers. Households continued to be protected customers. The market was therefore opened up for more than 140,000 customers with more than 194,000 supply points. Eligible customers' offtake exceeded 70 per cent of natural gas consumption in the Czech Republic.

Three factors became the key features of the Czech gas market:

- Reimposition of the regulation of prices of gas supplies to eligible customers;
- New entrants on the gas market in trading; and
- The adoption of a new statutory instrument on gas market rules.

All of these factors are closely interrelated and influence one another. Related to the market opening are also the obligations arising for the Czech Republic from its membership of the EU, i.e. the division of gas companies through legal unbundling and meeting the requirements of Regulation No 1775/2005/EC³⁾.

The reasons that prompted the Office to reimpose price control via price caps are described in detail in the following chapter.

The key characteristic feature of 2006 was the effort to create a competitive environment in the gas market, for which the market liberalisation principle is being implemented. The basic idea of liberalisation is that a number of competing gas traders operate in the open market, and eligible customers can therefore freely select – pursuing their own priorities – their gas supplier, with whom they then enter into a gas supply agreement for a mutually advantageous and acceptable price. However, this was not achieved in the Czech gas market. From 1 January 2006 a new gas trader started to operate in the market, Wingas GmbH, which won one customer, Vetropack Moravia Kyjov, a.s., and also Vemex, s.r.o., which on 1 October 2006 started to supply a part of the total quantity of gas purchased to a regional gas distribution company, Pražská plynárenská, a.s. Of the other gas traders also MND Hodonín, a.s. should be noted; this company produces natural gas in the Czech Republic but uses it for consumption in its own companies; and also OKD, a.s., which supplies surface drained gas to Severomoravská plynárenská, a.s. These supplies are of local importance only.

The gas market's malfunctioning, demonstrated and confirmed by the developments on the market in 2006, resulted in the Office's decision to draw up a more liberal public notice on gas market rules in co-operation with gas companies and final customers. The new instrument also had to reflect the requirements of Regulation 1775/2005/EC³⁾, effective from 1 July 2006, to put in place in Europe the preferred model of entry/exit capacity booking, and to define the activities of the missing function of the market operator, determining in particular the place and exact conditions for gas trading, thereby reducing the risks for smaller traders and new trading entrants. The new gas market model, provided for in the public notice on gas market rules, brings a number of favourable changes the objective of which is to create the preconditions for competitive trading, thereby ensuring all the advantages stemming from a fully functional liberalised environment. However, its further development and simplification is tied to the expected amendment to the Energy Act.

4.1.1 Assessment of reimposed regulation

In 2005 the Office received many suggestions from eligible customers to initiate administrative proceedings on failures to reach agreement on price and contract terms and conditions. Eligible customers also documented that it was not feasible for them to choose their gas supplier. This was completely contrary to the intentions that resulted in starting market liberalisation, and prompted the decision to carry out price-related inspections at RWE Transgas, a.s. and regional distribution companies. The result was the finding of unjustifiable gain at RWE Transgas, a.s., Severomoravská plynárenská, a.s., Východočeská plynárenská, a.s., and Středočeská plynárenská, a.s., and the imposition of fines totalling CZK 14,692,420. These administrative fines are described in detail in part 11.6.

And so, on the one hand the gas market was liberalised formally under the Energy Act, and owing to this liberalisation the individual categories of final customers were deprived of protection through price controls, while on the other hand no genuine competition had yet emerged on the Czech gas market.

On the basis of its findings the Office decided to reimpose restrictions on gas supply prices from 1 January 2006, in the form of the maximum permissible selling price of the gas supplied by the trader of RWE Transgas, a.s., the maximum price to be charged by RWE Transgas, a.s. for gas storage and the maximum permissible price of gas supplies charged to eligible customers by the gas traders who bought gas from RWE Transgas, a.s. Price controls as applied in the previous regulatory period, when prices had been set on a quarterly basis and subsequently corrected to reflect the actual costs of natural gas procurement, was selected as the most appropriate regulatory method.

The decision to impose price controls again was accepted favourably by eligible customers; according to the Office's calculations, this decision helped to reduce eligible customers' costs of natural gas purchase in 2006 by approximately 4.4 per cent, i.e., they saved approximately CZK 2 billion. The lower price was attributable to the imposition of regulated margins on the gas traders, and also the effect of natural gas storage, since in winter usually cheaper gas injected in summer is withdrawn from UGS facilities. Companies in the RWE Group, but also Wingas GmbH and Vemex, s.r.o. accepted the reimposed price controls unfavourably.

³⁾ Regulation (EC) No 1775/2005 of the European Parliament and of the Council of 28 September 2005 on conditions for access to the natural gas transmission networks.

The Office's decision to lift the regulation on 31 March 2007 was preceded by a number of meetings with RWE Transgas, a.s. on the conditions and methods of pricing after 1 April 2007; these consultations were intended to ensure the development of a competitive environment on the market and adequate prices to final customers. The RWE Group also prepared new draft contracts that would be offered to customers and expected to remedy the shortcomings found in these contracts in the past period.

4.1.2 Unbundling

The principal changes on the gas market, which were carried out in 2006 in line with the European Communities *acquis*, include those resulting from unbundling. The Czech Republic adopted legal unbundling, i.e., within companies licensed activities were separated so that henceforth they would be carried on by legally independent entities enjoying legal and factual decision-making independence, which is one of the key prerequisites for ensuring their non-discriminatory behaviour.

Unbundling is one of the elements of market liberalisation, the objective of which is to create structures enabling business competition and eliminating monopoly from the energy sector. Its objective is to achieve a permanent separation and independence of those levels in vertically integrated undertakings at which value added is created.

The first company in which legal unbundling took place was RWE Transgas, a.s. From 1 January 2006 a new entity started to operate on the Czech market, RWE Transgas Net, s.r.o., the transmission system operator. The licensed activities of gas trading and gas storage were retained in RWE Transgas, a.s.

Intensive preparations for the legal unbundling of the eight regional distribution companies that have more than 90,000 customers (Jihočeská plynárenská, a.s., Jihomoravská plynárenská, a.s., Pražská plynárenská, a.s., Severočeská plynárenská, a.s., Severomoravská plynárenská, a.s., Středočeská plynárenská, a.s., Východočeská plynárenská, a.s., and Západočeská plynárenská, a.s.) took place throughout 2006, with a view to effecting the unbundling as from 1 January 2007. The deadline was met in line with the Energy Act.

Since in the unbundling process the regulated entities are compelled to incur certain unplanned costs, the Office has, pursuant to the Energy Act, the remit to decide on the inclusion of the justifiable and demonstrable minimum costs of unbundling into the prices of regulated activities. The methodology for calculating and quantifying the minimum costs was developed *ex ante* and followed the same rules as in the electricity industry in 2005.

During the course of preparing detailed analyses, which helped to eliminate unjustifiable costs and set the minimum level of justifiable costs, the following cost categories were identified:

- One-off operating costs of unbundling – these costs will be incurred in the period directly including the legal unbundling exercise as such;
- Capital costs of unbundling – one-off expenses related to the acquisition of the assets necessary for carrying out the unbundling are understood to be capital costs;
- Ongoing operating costs of unbundling – these costs will be incurred on a regular basis, for the first time in the year of the unbundling itself and then in the following years because of the new nature of the unbundled companies' functioning.

With regard to the resulting level of the unbundling costs the Office decided to spread the recognition thereof over several years, which means that only a certain part of unbundling costs has been recognised in the gas distribution prices for 2007.

4.1.2.1 Compliance Programme

Similarly as in the electricity industry (see part 3.1.2) also gas distribution companies prepared, pursuant to the Energy Act, their initial Compliance Programmes that set out the measures to preclude discriminatory approach to other gas market participants, particularly as regards access to the distribution system and use of the gas distribution companies' services.

Having analysed these documents the Office did not find any breach of non-discriminatory behaviour and proceeded to the harmonisation of these programmes on the basis of a standardised structure.

Like the power utilities also regulated gas companies were given information about the progress of the unbundling and the drafting of documents in CEER and ERGEG, and the document giving guidelines on functional and information unbundling was presented to them.

4.2 Pricing

In the gas industry, the Office sets the gas prices once a year with effect from 1 January. Changes related to those in the price of the energy, caused by developments on the market of oil products, which serve as an alternative to natural gas and from the prices of which the natural gas price is derived on exchanges, may also be made effective from 1 April, 1 July, and 1 October of the respective year.

In 2006 the price of natural gas supplies was increased from 1 January and from 1 April. These price increases responded to the rise of oil and oil product prices, which had started in mid-2005. When setting the selling price of RWE Transgas, a.s. with effect from 1 July the Office decided to leave the commodity charge unchanged on the basis of indications from commodity markets. During July and August oil prices on exchanges peaked, whereupon they started to decline. The drop in oil and oil product prices had a favourable influence also on natural gas prices, which started to decrease thanks to the lower input costs and the Czech currency's favourable US

dollar and euro rates. These factors resulted in a reduction in the above selling price as from 1 October 2006 and 1 January 2007. In April 2006 there were, moreover, changes in the input parameters at one of the foreign suppliers for the benefit of customers in the Czech Republic. Natural gas prices charged by RWE Transgas, a.s. to regional distribution companies can be seen in Chart 8.

Chart 8 Natural gas prices charged by RWE Transgas, a.s. to regional distribution companies

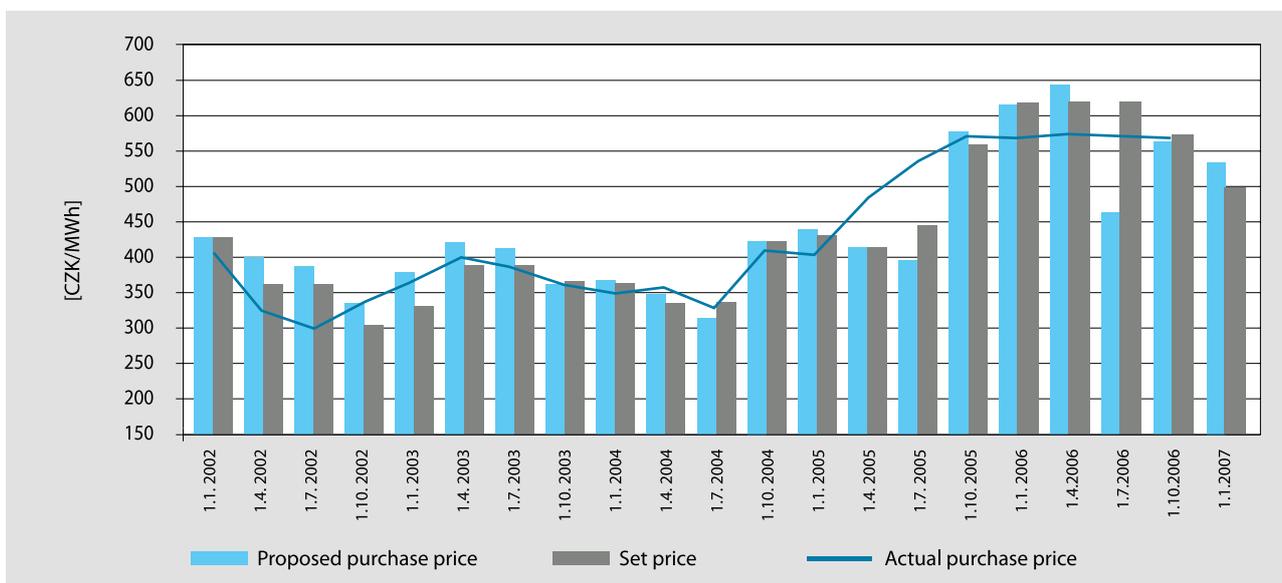
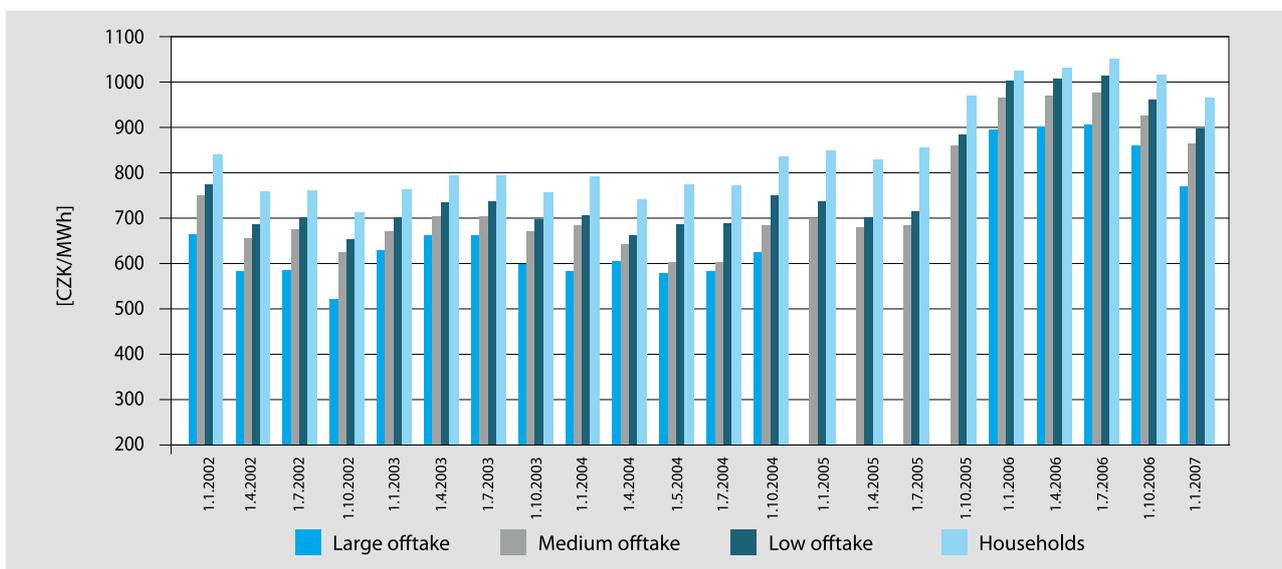


Chart 9 depicts the development of average natural gas supply prices for each category of eligible customers.

Chart 9 Average natural gas supply prices to the various customer categories



Under the Energy Act the Office sets the prices of the regulated activities of gas transmission and gas distribution. The prices for the storage activity, if needed by the customer, and for the supply activity are negotiated prices for eligible customers – they agree on these prices when entering into contracts. The prices for gas transmission and distribution are fixed and cannot be changed contractually.

4.2.1 Prices to eligible customers

On 1 January 2006 all end users of natural gas with the exception of households became eligible customers. For eligible customers, 2006 did not mean a fully liberalised market. Having assessed the outcomes from its price-related inspections the Office decided to

impose temporary price caps also on gas supplies to eligible customers. For the whole of 2006 the price to eligible customers who did not use the gas supplier switch option was set on the same principle as the price to protected customers. Other customers could use the price agreed in the contract between the two parties, which could be calculated on any time base.

4.2.2 Prices to protected customers

The principle on which gas supply prices were set for protected customers, in 2006 only households, did not change in comparison with 2005. This principle was also adopted for setting gas supply prices to eligible customers once the gas supply prices were restricted by imposing price caps.

4.2.3 Natural gas supply prices

The price charged for natural gas supplies by the natural gas trader, i.e. RWE Transgas, a.s., to the respective licence holders who supply gas to final customers connected to regional distribution systems and who have a dominant position in their respective region, continues to be a double-component price. It is composed of the variable commodity charge, which covers the price for the energy in natural gas and the business margin, and a fixed capacity charge covering the costs related to natural gas transmission and storage.

The commodity charge is the most important component of the final price, accounting for about 60 to 70 per cent of the gas supply price. The actual percentage depends on the current commodity charge.

The basis for setting the commodity charge is mainly the forecasts of the development of oil product prices on the world markets and predictions of the Czech currency's US dollar and euro rates. The price is further adjusted to reflect the difference between the actual cost of gas purchase by RWE Transgas, a.s. and the price set by the Office in the preceding closed quarter.

The principle on which gas supply prices to final customers are set has also remained unchanged. It is a double-component price, which derives from the gas supply price set for trader RWE Transgas, a.s. and is extended to include the distribution charge and the trader's costs incurred in selling the gas it delivers to the final customers. Chart 10 shows the composition, in per cent, of the average gas supply price to household customers in the first quarter of 2006, while Chart 11 shows the composition for the first quarter of 2007.

Chart 10 Structure of the average gas supply price to household customers, 1Q 2006

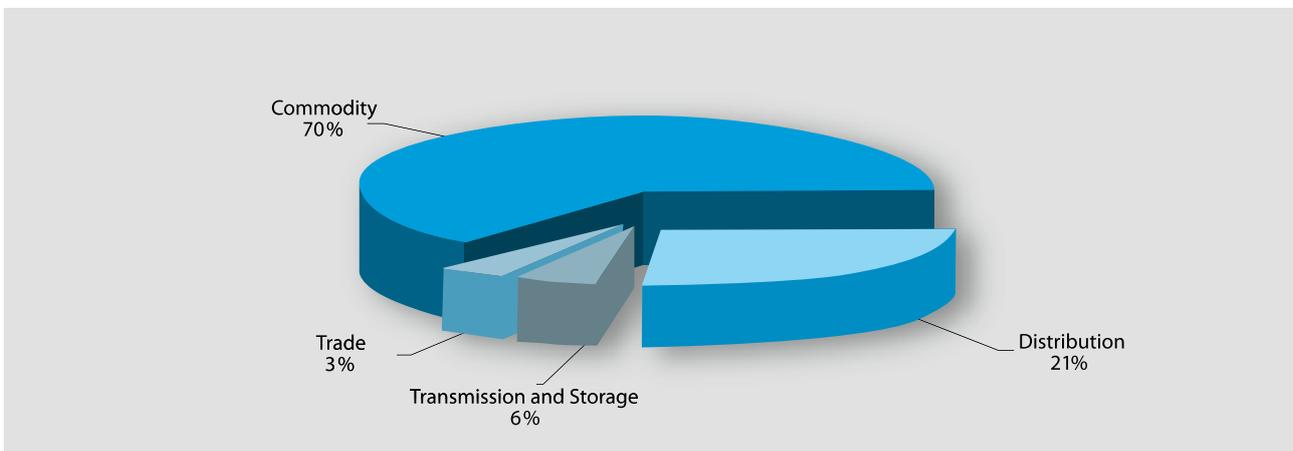
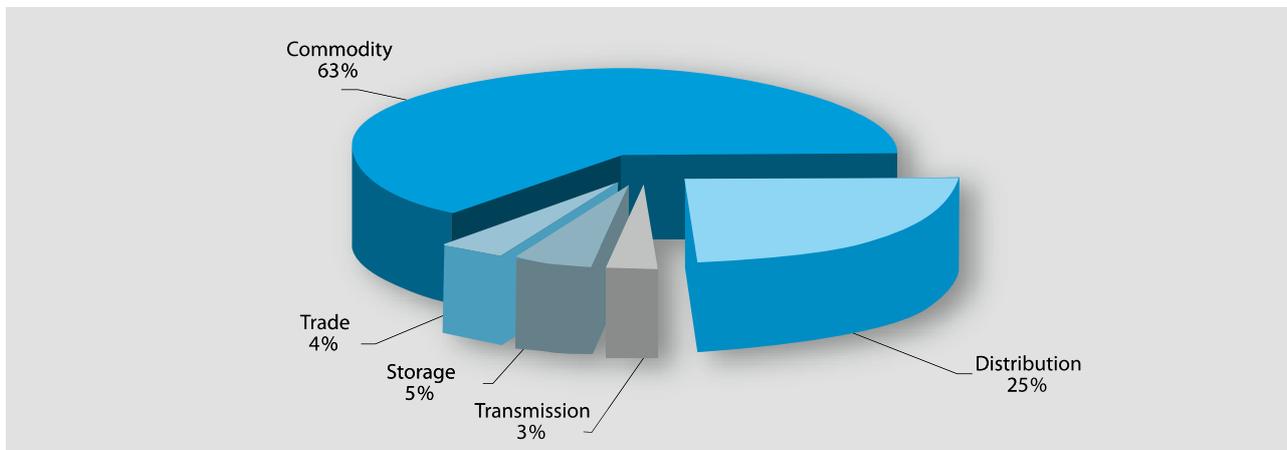


Chart 11 Structure of the average gas supply price to household customers, 1Q 2007



The variable component of the price relates to the natural gas quantity taken and is understood to be the part of the price, which responds to the current developments on the natural gas market. The fixed capacity-related component of the price covers the costs related to natural gas transmission, storage and distribution.

On 1 January 2007 all final customers became eligible customers and they can now select their own natural gas supplier that best meets their requirements. A precondition for a well-developed liberalised market is uncontrolled prices formed by a naturally competitive environment. In the gas industry, these prices include the gas storage charge and the commodity charge. The Energy Regulatory Office regulates activities that by their very nature prevent competition. These include the gas transmission and distribution services.

The structure of the gas supply price in 2006 already partly reflected the future situation from 2007 and the final price was divided into a distribution part and other services, which included the commodity charge and the charges for the use of the transmission system and underground gas storage facilities. The final customers therefore could see the individual components of the price and the level at which they were priced.

Another logical step in price setting for 2007 was consistent separation of controlled and uncontrolled components of the price, i.e. the charge for using the transmission system and the charge for using underground gas storage facilities.

Average prices, in percentage terms, of natural gas supplies to each category of customers in 2006 and 2007, with a detailed view of the household category, can be seen in Table 3.

Table 3 Average prices, in percentage terms, of natural gas supplies for each category of customers in 2006 and 1Q 2007

	Category	Natural gas prices in each quarter												
		Price [CZK/MWh]						Quarterly price changes [%]						
		IQ 06	IIQ 06	IIIQ 06	IVQ 06	IQ 07	IQ 06	IIQ 06	IIIQ 06	IVQ 06	IQ 06	IQ 07		
Czech Republic	Large offtake	884.28	906.00	906.00	856.71	758.17	0.00	2.46	0.00	0.00	0.00	0.00	-5.44	-11.99
	Medium offtake	976.68	991.45	991.45	942.16	849.72	10.40	1.51	0.00	0.00	0.00	0.00	-4.97	-9.78
	Low offtake	1,025.67	1,040.44	1,040.44	991.15	910.84	14.97	1.44	0.00	0.00	0.00	0.00	-4.74	-8.08
	Households	1,056.57	1,071.34	1,071.34	1,012.82	974.81	4.78	1.40	0.00	0.00	0.00	0.00	-5.46	-4.17
	Total	964.03	982.05	982.05	929.95	854.11	5.73	1.87	0.00	0.00	0.00	0.00	-5.31	-8.62
Jihočeská plynárenská, a. s.	1,131.66	1,146.43	1,146.43	1,087.91	1,067.89	8.93	1.31	0.00	0.00	0.00	0.00	-5.10	-1.88	
Jihomoravská plynárenská, a. s.	1,034.65	1,049.42	1,049.42	990.90	947.69	4.61	1.43	0.00	0.00	0.00	0.00	-5.58	-4.53	
Pražská plynárenská, a. s.	1,051.55	1,066.32	1,066.32	1,007.80	969.58	4.96	1.40	0.00	0.00	0.00	0.00	-5.49	-4.90	
Severočeská plynárenská, a. s.	1,115.50	1,130.27	1,130.27	1,071.75	1,038.42	7.27	1.32	0.00	0.00	0.00	0.00	-5.18	-3.24	
Severomoravská plynárenská, a. s.	1,075.15	1,089.92	1,089.92	1,031.40	999.97	5.77	1.37	0.00	0.00	0.00	0.00	-5.37	-3.33	
Středočeská plynárenská, a. s.	1,057.93	1,072.70	1,072.70	1,014.18	956.11	2.97	1.40	0.00	0.00	0.00	0.00	-5.46	-5.77	
Východočeská plynárenská, a. s.	1,004.64	1,019.41	1,019.41	960.89	937.93	2.65	1.47	0.00	0.00	0.00	0.00	-5.74	-3.13	
Západočeská plynárenská, a. s.	1,080.20	1,094.97	1,094.97	1,036.45	980.55	3.01	1.37	0.00	0.00	0.00	0.00	-5.34	-5.57	

4.2.4 The transmission charge

Natural gas transmission involves multiple types of cost, mainly the cost of transporting natural gas through the Czech transmission system, the costs incurred in identifying and keeping the required natural gas quality standards and the costs incurred in balancing the Czech gas system.

The transmission charge set for 2006 is, as in previous years, a fixed single-component price, which is uniform for the whole market and independent of distance because of the small area covered by the Czech Republic (the postage stamp principle). Its amount depends on the gas quantity that has to be transported over one day (maximum daily capacity out of all the values over the year). The transmission charge is set for one-year agreements and longer.

In addition to the standard one-year term, transmission agreements can be executed on a daily basis and for a term of one to twelve months, taking into account that the use of the transmission system varies in different months of the year, and therefore the amount of the effort to provide transmission capacity for a shorter period depends on the specific calendar month and the length of the period. This must be reflected in the final charge for transmission.

The transmission charge also included a part of the TSO's justifiable minimum unbundling costs, which the Office had set under the Energy Act on the basis of the 2005 methodology.

In comparison with 2006 there was a major change in transmission pricing in 2007. This change was precipitated by the changes in the approach to the organised natural gas market in the Czech Republic, as provided for in an amendment to the public notice laying down the rules for the organisation of the gas market and for the development, allocation and use of typical gas supply profiles. The new rules define the entry/exit points on the Czech gas system, which had to be evaluated and for which fixed charges for booked capacity had to be set. This resulted in six different fixed charges for daily booked firm capacity throughout the term of annual contracts, unlike the previous years when a single transmission charge was set.

The new approach to gas market organisation also made it possible to increase the tolerance in overstepping daily booked capacities at an exit domestic point from two per cent to 3.8 per cent. As in 2006, the charge for overstepping daily booked firm or interruptible capacity is billed only once, for the highest value of the actually achieved capacity.

In respect of the setting of the fixed charge for gas transmission reduction or interruption, which is paid by the transmission system operator to the users, in 2006 the approach was specified more accurately as regards the execution of both annual interruptible transmission contracts and monthly and daily interruptible transmission contracts.

4.2.5 Natural gas storage price

In 2006 the Office controlled, through price caps, also the prices for natural gas storage for both eligible customers and the natural gas suppliers who bought gas for the purpose of supplying it to eligible customers, in addition to gas transmission and distribution.

The calculation of the storage charge continued on the same principle as introduced at the beginning of the second regulatory period. From 1 January 2006 an amendment to the public notice that lays down the rules for gas market organisation entered into force. This amendment expanded the TSO's role to include transmission system balancing. In this connection it was necessary to reserve sufficient withdrawal capacity in the underground gas storage facilities in the Czech Republic to support this new role. The costs of reserving the withdrawal capacity for the purpose of transmission system balancing are included in the transmission charge. They are therefore not a part of the price of storage for final customers.

On the natural gas storage market the following companies operated in the Czech Republic in 2006: RWE Transgas, a.s., which owns six of the eight underground gas storage facilities located in the Czech Republic, and Moravské naftové doly, a.s., in which more than 50 per cent are held by SPP Bohemia, a.s., which operates the Dolní Bojanovice UGS facility used for the Slovak Republic's needs.

This clearly indicates that in 2006 RWE Transgas, a.s. held a monopoly for the provision of underground gas storage services. The gas stored in underground gas storage facilities and intended for supplying the Czech market was owned by RWE Transgas, a.s.

The principle of pricing natural gas storage in underground gas storage facilities has been maintained for 2007. The costs incurred in connection with market liberalisation had to be reflected in the prices for natural gas storage, similarly as with the transmission system.

But there is a change in the pricing of the use of underground gas storage facilities within prices to final customers. The categories of customers who use the storage service to a larger extent, or on the contrary do not use storage facilities because of the nature of their gas consumption, have been specified in more detail.

4.2.6 The distribution charge

In the final price of natural gas supply the distribution charge is the second most important component after the commodity charge. Distribution, as gas transport through the distribution system to every supply point, is a typical business that will be regulated on a fully liberalised market too because the ownership of a distribution system establishes a natural monopoly in the area served by the system.

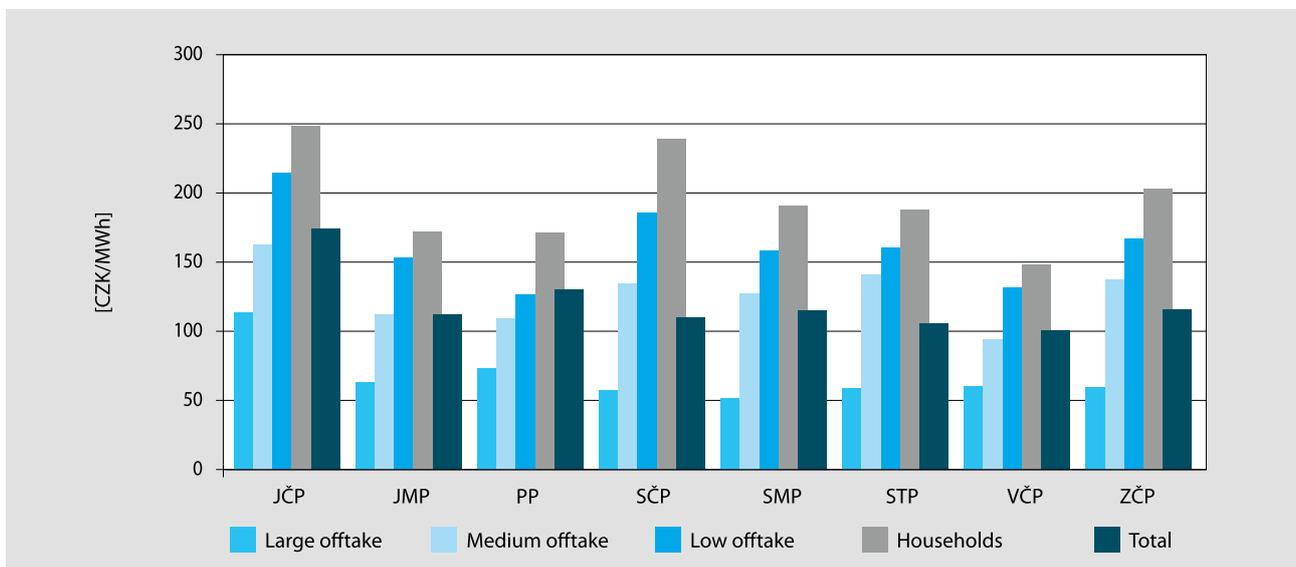
The distribution charge includes the costs incurred in operating the system, metering, and identifying and processing the data required for balancing the Czech Republic's gas system. Depending on their geographical conditions, degree of industrialisation

of the area they serve, and density of gas penetration in the household category, distribution systems differ considerably. This also necessitates differentiated controlled prices for each of the distribution companies.

The distribution charges are double-component prices; one component is variable and relates to the gas quantity taken at a particular supply point. The other component is fixed; in the case of supply points taking annually no more than 63 MWh it has the form of the standing monthly charge for the capacity available, and in the case of higher offtake supply points this fixed component has the form of a fixed annual charge for the maximum daily capacity available. Through this charge, customers at specific supply points pay the cost of the capacity required to support the maximum daily offtake at the lowest temperatures in the case of space heating, and the maximum output of the process equipment installed in the case of gas offtake for process purposes.

Average prices of distribution companies in 2006, for groups of customers having different annual natural gas demand, are shown in Chart 12. Average prices include both components of the distribution charge and are set on the basis of the annual values of the technical units for these customer groups.

Chart 12 Average natural gas distribution prices in 2006



The distribution charges for 2006 were calculated on the basis of the data obtained from the metering conducted for the purpose of developing typical supply profiles. Such readings had never been taken before to such a large extent. This data provides a new, more accurate notion of the use of distribution systems by the various types of customers, and was the basis for allocating distribution costs, mainly fixed costs. This is why various changes, in percentage terms, were made to the average distribution charges for the various groups of customers. In comparison with 2005 distribution charges averaged over all customer groups were increased by 2.24 per cent, and the increase was more than 10 per cent for certain groups. This approach helped to achieve a correct adjustment of prices.

The data obtained has proved that customers taking more than 63 MWh annually, included in the low-offtake and household category, have a demand profile similar to that of medium-offtake customers, and in this group the standing monthly charge has been replaced by the fixed annual charge for reserved capacity.

An important change in 2006 was the use of a new model for computing distribution charges for the various customer categories and offtake bands. This model ensured uniformity of the calculations of controlled prices and applied more accurately the principle of cost intensity to the charges for the various groups of customers.

The use of the model required the unification of the segmentation of supply points in the large-offtake category, in which the dividing lines between the individual offtake bands had been different for each of the distribution companies, or a different number of offtake bands had even been used.

The more accurate reflection of cost intensity in the prices for each individual supply point is the result of taking into account the pressure level to which a particular supply point is connected. This principle was also applied to the low-offtake and household category by dividing the 9.45 to 63 MWh/year band into ten 5 MWh bands.

In comparison with 2006, the average distribution charge set for 2007 for the whole Czech market went up by CZK 8.82/MWh, i.e. 7.47 per cent.

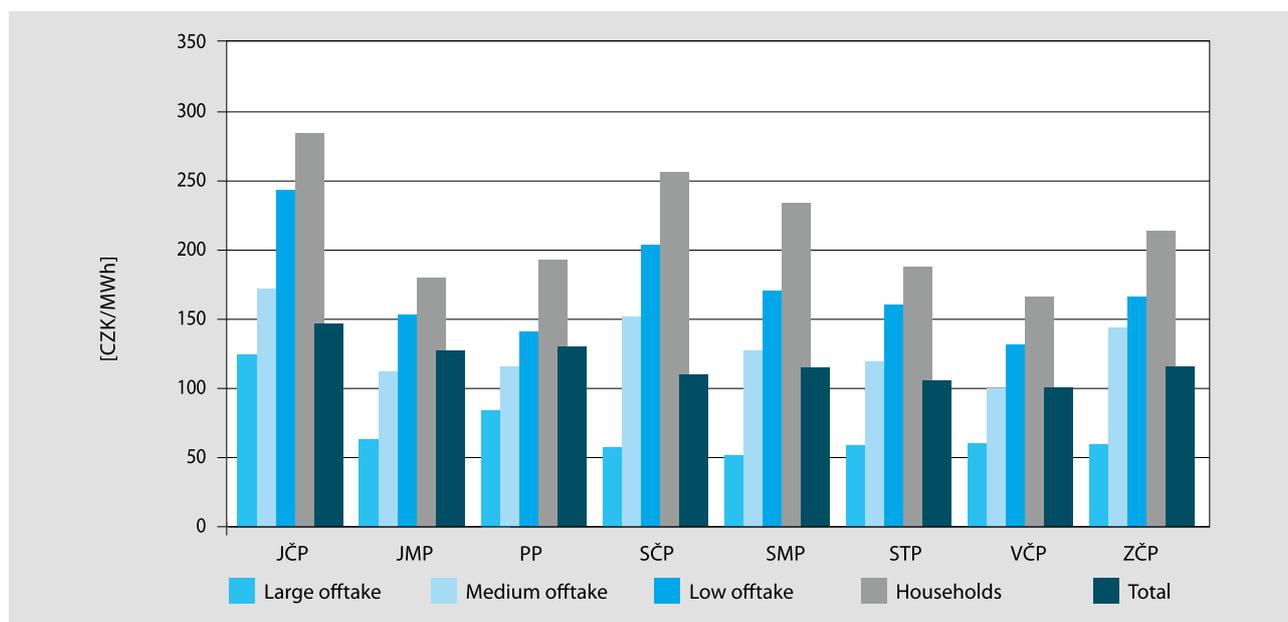
At the distribution companies within the delineated areas of which Českomoravská plynárenská, a.s. was operating, the distribution prices reflected the purchase of its gas assets from RWE Gas International B.V., which became the sole shareholder of Českomoravská plynárenská, a.s. in 2006. At the same time all customers of this company, located in each of the delineated areas, were included into the number of the offtake points of regional distribution companies.

This transfer resulted in a decrease in the gas quantity distributed by Pražská plynárenská, a.s., while the gas quantity distributed by Středočeská plynárenská, a.s. increased accordingly; the latter company now distributes gas to the Černošice delineated area, which in 2006 was served by Českomoravská plynárenská, a.s.

In 2007 the costs incurred in gas market opening are first reflected in the distribution charge. Gas companies provided detailed analyses of these costs and the Office commissioned an opinion on and estimates of demonstrable minimum justifiable costs incurred in gas market opening from independent consultancies in relation to these analyses. On the basis of these opinions and estimates the amount of costs applied in distribution pricing was calculated.

Chart 13 shows average distribution charges for 2007, broken down by customer categories and distribution companies.

Chart 13 Average prices of natural gas distribution for 2007



In 2006 eligible customers and gas traders could enter into gas distribution agreements under the Energy Act. These agreements could be one-year agreements for a period of at least twelve months, taking into account the annual period. For such agreements the prices and terms and conditions are set out in the relevant part of the Office's price decision. Besides one-year agreements eligible customers and gas traders could enter into monthly agreements on gas distribution for a term of at least one month and a maximum term of eleven months. The prices under these short-term agreements are set using the procedure set out in the applicable price decision on the basis of the prices under one-year agreements, using monthly coefficients. These coefficients take into account the demands on the use of the distribution system during a year. Daily booked capacity is the decisive variable for gas distribution.

Similarly as in the case of the transmission charge, for 2007 the approach to the setting of the fixed charge for distribution reduction or interruption, paid by distribution system operators to the users, has been specified more accurately; this concerns the execution of both annual interruptible capacity contracts and monthly interruptible capacity contracts.

4.2.7 Local distribution systems

The amendment of 1 January 2005 to the Energy Act no longer permitted local distribution system operators (LDS), who held only the gas distribution licence, to also supply gas to their customers connected to their system. In a statutory instrument that elaborated on the amended Energy Act in more detail, the approach to the regulation of the prices of distribution provided by LDS operators in the gas industry changed significantly.

In addition to the opportunity to use the prices of the higher-level regional distribution system as the standard practice, the legislation in place allows LDS operators to ask the Office to set individual distribution charges.

In 2006 the Office therefore updated its information about LDS operators. The purpose was to find the then current technical and financial data and see how the newly introduced way of regulation met the gas market's real needs and whether or not regulation should be continued using the same method. The research into the current situation with LDS confirmed the objective, which was to ensure that the market would function in this area. This means that the LDS operators who did not carry on business in the gas industry and held gas distribution licences requested the revocation of their licences under the influence of regulation. For those operators who want to carry on business in the gas industry firm pricing rules have been put in place.

Since 1 January 2005 a total of twelve LDS operators have asked for individual distribution charges to be set for them. In two cases no individual distribution charge was set after calculating the individual charges and on the basis of consultations with the LDS operators.

In 2006 individual charges were newly set for six LDS operators. With the exception of Českomoravská plynárenská, a.s. and QUANTUM, a.s., they are companies operating gas distribution in industrial complexes.

In the light of these findings it appears to be appropriate to categorise LDS into two groups for the purpose of setting individual charges – industrial complexes, and other. In setting individual charges for the LDS that carry on the licensed activity in industrial compounds the Office has to approach problematic cases on an individual basis and assess the specific conditions under which the LDS operates its licensed activity. The standard approach can be adopted in respect of the other LDS.

The natural gas supply prices to protected customers whose equipment is connected to an LDS were regulated in 2006 by price caps. This involved only Českomoravská plynárenská, a.s. and QUANTUM, a.s., which supplied gas also to household customers. The price of natural gas supply to eligible customers supplied by LDS operators who were also gas trading licence holders was not regulated in 2006, because unlike eligible customers supplied by a regional distribution company's trader these eligible customers could switch their supplier and start buying gas from a regional company's trader for whom the supply prices were set by the Office.

For 2007 the number of distribution charges set individually for local distribution system operators has not changed. However, there are changes in the structure of local distribution system operators specified in the respective ERO Price Decision.

Českomoravská plynárenská, a.s. discontinued its gas distribution business in connection with the inclusion of its distribution systems in each of the delineated areas into those of regional distribution companies mentioned in the preceding section. Therefore no individual prices were set for this company.

The Office newly set an individual distribution charge for the STAVEBNÍK housing development cooperative, a gas distribution licence holder.

The heat supply industry



5.1 The heat supply market

The heat supply industry is a highly diversified industry in terms of the way of thermal energy generation, the size of the thermal generating installations and also the size of the various heat supply companies. Unlike the electricity and gas industries, there is no integrated system of transit and transmission networks here. Thermal energy is usually supplied only to a certain region or locality.

The Czech Republic is one of the countries that have traditionally had a large proportion of district heating systems. In areas where thermal energy is supplied largely from district heating systems, the operators of such installations have the position of a local monopoly. In the heat supply industry, competition rather means competition between the energies used for individual heating.

The right to choose the method of heating exists in the Czech Republic, but sometimes only at the time of taking the very first decision on the method of heating. Changing the selected way of heating later is usually accompanied by the need to overcome considerable financial, administrative and time barriers.

Regulation in the heat supply industry should mitigate the impacts of these market imperfections, protect final consumers in the environment of natural monopolies, and take action largely in cases where competition is not strong enough to influence thermal energy prices.

In the light of the above, it is quite a challenging exercise to devise thermal energy pricing rules that will be fair to all and prevent disproportionate price hikes, and at the same time will not place too heavy limitations on the regulated entities.

5.2 Thermal energy price control

5.2.1 Cost-plus price control

Under Section 6 of Act No. 526/1990 on prices, as amended, thermal energy prices shall be subject to cost-plus regulation. Thermal energy price control consists in stipulating a mandatory procedure for formulating and calculating the price. Only economically justifiable costs and reasonable profit from thermal energy production and distribution may be reflected in thermal energy prices.

In 2006 the same conditions were maintained for thermal energy pricing, applicable to all thermal energy suppliers, as had applied in the previous year under ERO Price Decision No. 9/2004 of 20 October 2004, on thermal energy prices.

In 2006 the Office set only one procedure for thermal energy pricing, regarding a higher year-on-year growth of fixed costs and profit, which differed from the procedure set out in Price Decision No. 9/2004, specifically in ERO Price Decision No. 5/2006 of 29 June 2006 laying down a different procedure for thermal energy pricing.

For 2007 ERO Price Decision No. 7/2006 of 27 October 2006, which changed ERO Price Decision No. 9/2004 of 20 October 2004, specified more accurately – with effect from 1 January 2007 – certain economically justifiable costs in thermal energy prices and added formulas for calculating the thermal energy quantity in cases where no licence is awarded for thermal energy generation or distribution and no thermal energy metering is installed.

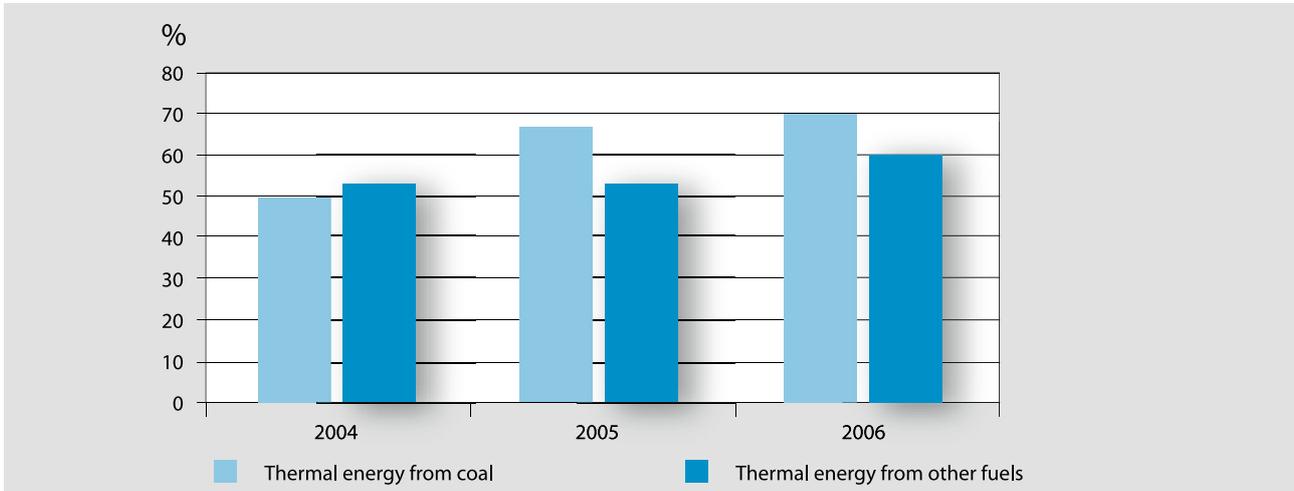
5.2.2 Thermal energy price levels

The average thermal energy price applied in relation to heat generating plants and heating systems in one municipality, or heating systems in different municipalities connected by pipes, is compared against the thermal energy price levels set by the Office for each level of transferring thermal energy produced from coal or from other fuels (usually natural gas and fuel oils).

In view of the increase in natural gas and electricity prices from 1 January 2006 and the expected rise in the coal price (including coal transport), the thermal energy price levels set by the Office were recalculated, and increased accordingly, with effect from 1 January 2006, in ERO Price Decision No. 13/2005 of 30 November 2005, which changed ERO Price Decision No. 9/2004 of 20 October 2004. From 1 January 2006 the thermal energy price level to which the prices of thermal energy for final consumers are compared was increased by about three per cent for supplies of thermal energy produced from coal and by about 10.5 per cent for supplies of thermal energy produced from other fuels.

The change in the prices of thermal energy produced from coal and natural gas, which was expected to come in 2007, resulted in a reconsideration of the thermal energy price levels applicable as from 1 January 2007 and the promulgation of ERO Price Decision No. 12/2006 of 27 November 2006, which changed ERO Price Decision No. 9/2004 of 20 October 2004, with effect from 1 January 2007. In the case of thermal energy production from coal the price is expected to rise by about four per cent on average and in the case of thermal energy production from natural gas the price is expected to go down by about three per cent on average.

The relaxation of control of the thermal energy prices that are lower than the respective price levels motivates suppliers to optimise their costs and make the operation of their installations more efficient so that the thermal energy price is calculated below the respective price level. The rising proportion of thermal energy produced from coal or other fuels, the price of which is calculated below the stipulated price level, can be seen in Chart 14 for the last three years.

Chart 14 Thermal energy quantity below the stipulated price level

5.2.3 Year-on-year growth of economically justifiable fixed costs

The rise in total fixed costs and profit is limited on an annual basis only in respect of thermal energy prices above the respective thermal energy price level set by the Office.

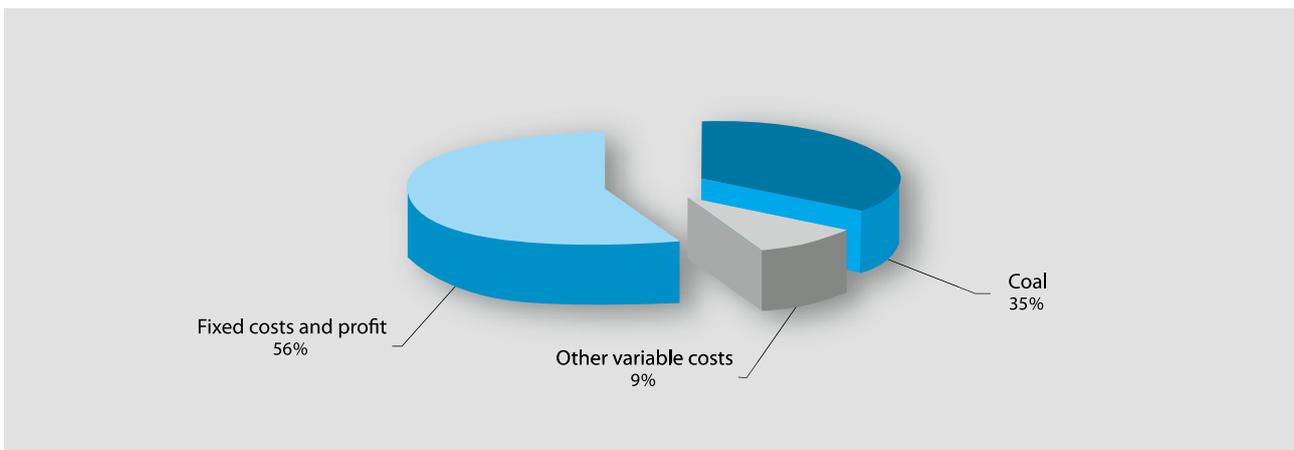
The amount of fixed costs and profit in thermal energy prices depends on the technology of thermal energy production and the fuel used.

The other factors that influence the overall composition of fixed costs in thermal energy prices may include

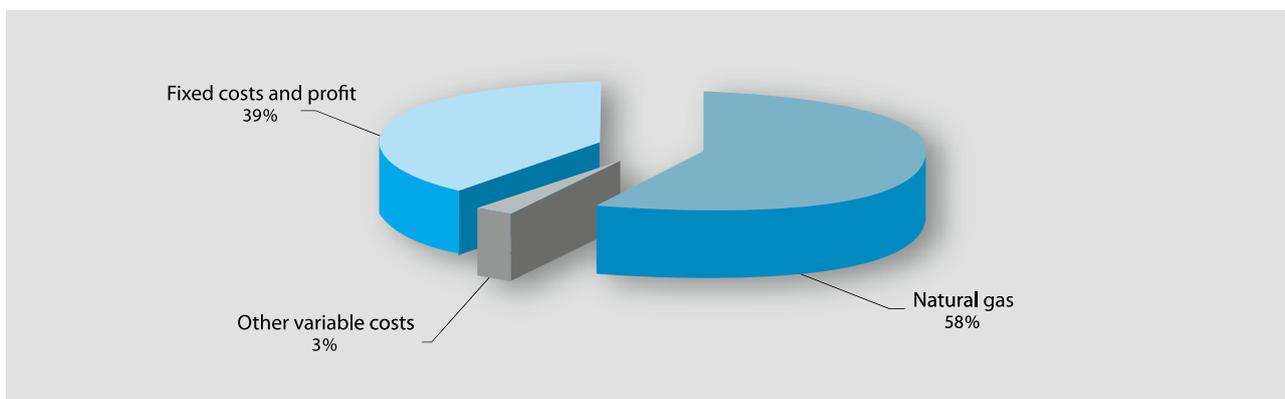
- the age of the installations,
- their service life, and/or
- the way of their financing upon their acquisition.

Higher thermal energy prices are controlled intentionally to encourage the rationalisation of economically justifiable costs and the development, modernisation and optimisation of suppliers' thermal installations.

The average share of costs in the price of thermal energy produced from coal and from other fuels is shown in Charts 15 and 16.

Chart 15 Share of costs in the price of thermal energy from coal

In comparison with Chart 15, which illustrates the share of costs in the price of thermal energy from coal, fixed costs of thermal energy production from natural gas are lower, as are the variable costs (costs of fuel), due to the technology used.

Chart 16 Share of costs in the price of thermal energy from natural gas

5.3 Development of thermal energy prices

For every year under regulation, thermal energy generation and thermal energy distribution licence holders furnish the Office with reports on data on thermal energy prices. Since the reports contain financial and technical data on both licensed and non-licensed activities, thermal energy generation and distribution, the Office obtains an overview of the situation and developments in the heat supply industry in the Czech Republic.

Every year the Office publishes on its website databases of the preliminary and resulting thermal energy prices that thermal energy suppliers charge at each transfer level within one price locality every year under regulation.

This information serves mainly for the purpose of thermal energy price control, for reviewing the stipulated thermal energy price levels and for assessing thermal energy suppliers' technical and financial stability.

All average thermal energy prices cited in this section are inclusive of VAT.

5.3.1 Average thermal energy prices

The data on average thermal energy prices and thermal energy quantities supplied is based on the regulatory reports and is shown here in relation to the fuel used in thermal energy generation. Between 2003 and 2005 average prices and actual volumes of thermal energy supplies were ascertained from the reports on the resulting thermal energy prices, while for 2006 data expected as at 1 January is cited.

The development of thermal energy prices from 2003 to 2006 indicates their slow increase, primarily due to changes in fuel costs and the permissible increase in fixed costs and profit in line with the binding conditions for thermal energy pricing. Another factor that affects the price is the decreasing quantity of thermal energy supplied. In the period under review the average price of thermal energy from coal rose by approximately CZK 32/GJ, and by CZK 87/GJ for other fuels (mainly due to the marked increase in natural gas prices), and the highest increase can be seen in 2005 and 2006.

Average thermal energy prices for 2007 are based on the expected thermal energy quantity and the year-on-year change in fuel and electricity prices, in particular coal price increases and natural gas price decreases.

The development of these prices is illustrated in Table 4 and Charts 17 and 18.

Table 4 Average prices and quantities of thermal energy delivered at all transfer levels

Year	Coal		Other fuels		Total	
	Price [CZK/GJ]	Quantity [GJ]	Price [CZK/GJ]	Quantity [GJ]	Price [CZK/GJ]	Quantity [GJ]
2003	241.91	114,654,045	309.11	54,523,670	263.56	169,177,715
2004	248.08	117,117,241	311.00	54,837,815	268.14	171,955,056
2005	259.34	109,992,011	349.05	52,950,012	288.49	162,942,023
2006	273.42	102,809,906	396.50	57,062,450	317.35	159,872,356
2007	278.57	104,234,494	395.10	48,632,908	315.64	152,867,402

Chart 17 Average prices and quantities of thermal energy delivered between 2003 and 2007

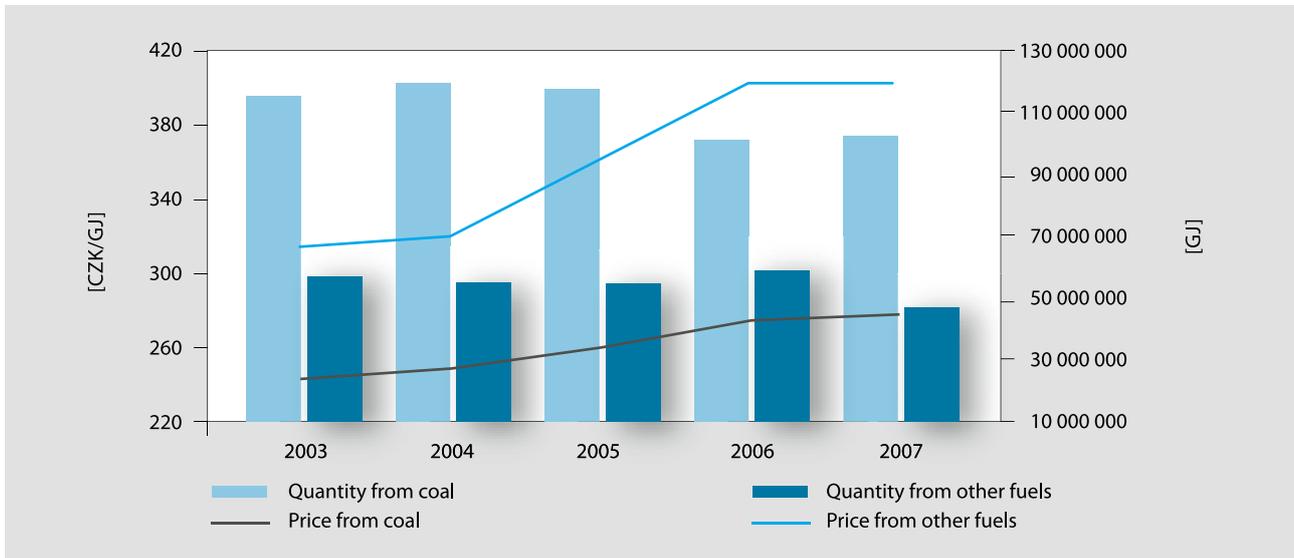
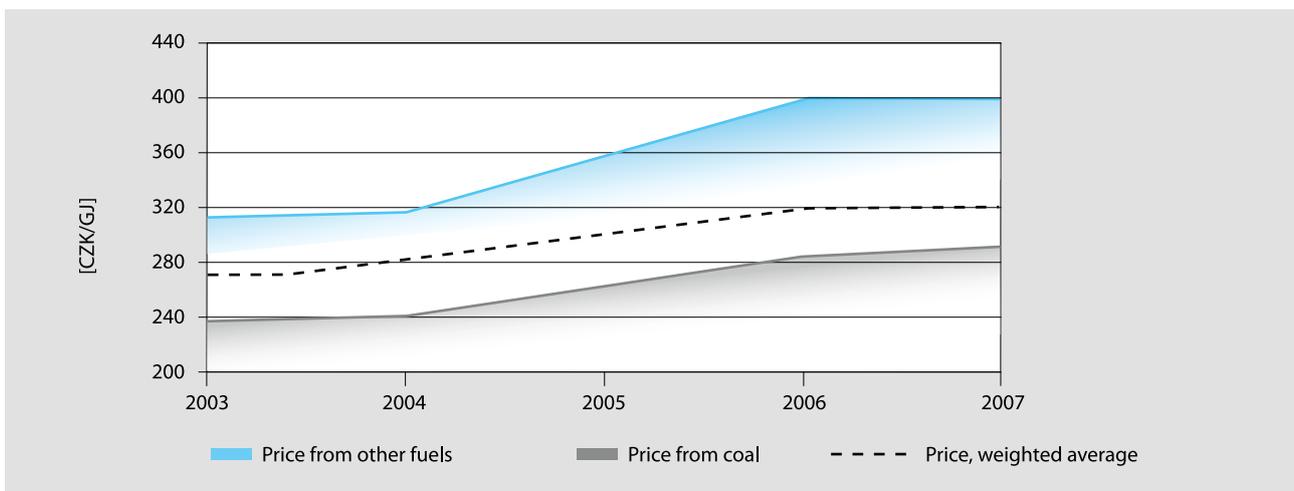


Chart 18 Average prices of thermal energy delivered between 2003 and 2007



5.3.2 Average thermal energy prices at transfer levels

The development of average thermal energy prices and thermal energy supplies can be observed for each of the thermal energy suppliers and at the transfer levels, i.e. where thermal energy is transferred from one part of the district heating system to another part or where thermal energy is transferred from the thermal energy source directly to the equipment that takes this thermal energy. The average prices are compared against the various price levels, which have been set by the Office since 2004.

Between 2003 and 2006 there was a gradual rise in thermal energy prices for supplies of thermal energy from coal at all transfer levels, while relatively constant quantities of thermal energy were supplied in this period.

Prices and quantities of thermal energy from coal are listed in Table 5.

Table 5 Average prices of thermal energy produced from coal

Transfer level		2003	2004	2005	2006
Supplies from production, capacity over 10 MWt	Quantity [GJ]	11,746,463	9,502,755	8,753,220	11,733,770
	Price [CZK/GJ]	165.46	162.59	170.50	175.35
	Price level [CZK/GJ]		160.00	195.30	197.40
Supplies from the primary distribution	Quantity [GJ]	62,703,800	65,541,842	60,596,573	51,799,670
	Price [CZK/GJ]	215.06	217.70	226.79	248.59
	Price level [CZK/GJ]		240.00	275.10	278.25
Supplies from production, capacity less than 10 MWt	Quantity [GJ]	443,007	197,899	27,982	36,495
	Price [CZK/GJ]	296.74	285.86	394.92	393.28
	Price level [CZK/GJ]		265.00	305.55	319.20
Supplies from the central exchanger station	Quantity [GJ]	7,998,913	7,268,314	6,823,994	7,396,816
	Price [CZK/GJ]	278.21	285.86	300.02	313.10
	Price level [CZK/GJ]		265.00	305.55	319.20
Supplies from the block boiler house's distribution	Quantity [GJ]	485,343	457,916	622,804	447,613
	Price [CZK/GJ]	332.25	350.68	371.50	385.12
	Price level [CZK/GJ]		290.00	330.75	340.20
Supplies from outside secondary distribution	Quantity [GJ]	28,096,699	30,000,058	29,022,169	25,899,073
	Price [CZK/GJ]	310.97	317.33	327.58	340.56
	Price level [CZK/GJ]		290.00	330.75	340.20
Supplies from a house transfer station	Quantity [GJ]	3,179,820	4,148,457	3,783,408	3,765,201
	Price [CZK/GJ]	330.56	343.75	362.15	367.80
	Price level [CZK/GJ]		290.00	330.75	340.20

Table 6 shows the prices and quantities of thermal energy produced from other fuels between 2003 and 2006.

In 2005 natural gas and fuel oil prices went up considerably, which led to an increase in thermal energy prices not only in 2005 but also in 2006. The quantity of the thermal energy supplied depends mainly on average ambient temperatures every year and also on savings or optimisation measures carried out by customers or thermal energy suppliers.

Table 6 Average prices of thermal energy produced from other fuels

Transfer level		2003	2004	2005	2006
Supplies from production, capacity over 10 MWt	Quantity [GJ]	7,125,716	7,994,324	5,690,514	7,266,332
	Price [CZK/GJ]	193.17	183.50	173.26	215.86
	Price level [CZK/GJ]		230.00	264.60	330.75
Supplies from the primary distribution	Quantity [GJ]	15,618,287	17,694,983	15,072,050	14,164,901
	Price [CZK/GJ]	279.62	276.29	319.54	367.07
	Price level [CZK/GJ]		310.00	344.40	413.70
Supplies from production, capacity less than 10 MWt	Quantity [GJ]	2,871,188	1,180,075	1,237,141	2,504,929
	Price [CZK/GJ]	319.95	318.28	332.96	401.55
	Price level [CZK/GJ]		335.00	371.07	454.65
Supplies from the central exchanger station	Quantity [GJ]	2,594,411	2,507,497	2,636,490	2,949,270
	Price [CZK/GJ]	358.81	362.69	375.65	452.82
	Price level [CZK/GJ]		335.00	371.07	454.65
Supplies from the block boiler house's distribution	Quantity [GJ]	10,439,291	9,705,461	9,571,449	9,669,340
	Price [CZK/GJ]	337.93	358.78	395.74	455.94
	Price level [CZK/GJ]		360.00	394.80	475.65
Supplies from outside secondary distribution	Quantity [GJ]	9,632,632	10,023,897	9,294,621	11,534,318
	Price [CZK/GJ]	354.73	372.66	399.21	437.52
	Price level [CZK/GJ]		360.00	394.80	475.65
Supplies from a house transfer station	Quantity [GJ]	6,242,145	5,731,578	6,501,605	6,077,281
	Price [CZK/GJ]	371.00	383.10	416.62	465.53
	Price level [CZK/GJ]		360.00	394.80	475.65

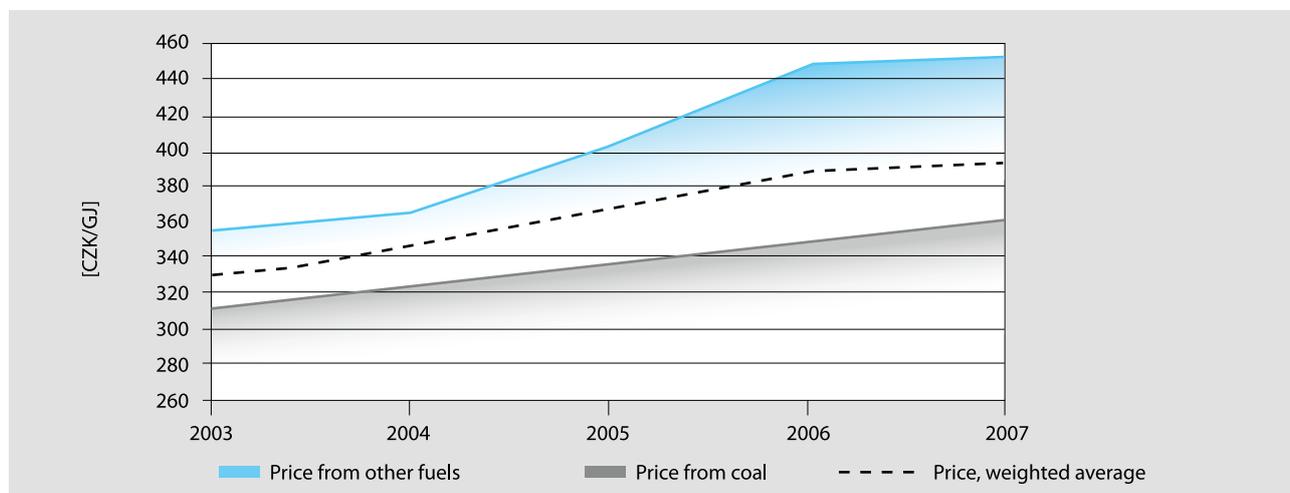
5.3.3 Average thermal energy prices to final customers

The development of average prices of thermal energy supplied to final customer from 2003 to 2005 and as at 1 January 2006 and 2007 has been traced from the data that covers supplies from block boiler houses' distributions, from outside secondary distributions and from house delivery stations. The overview has been prepared in relation to the type of fuel used for thermal energy generation and the average price for each year is a weighted average.

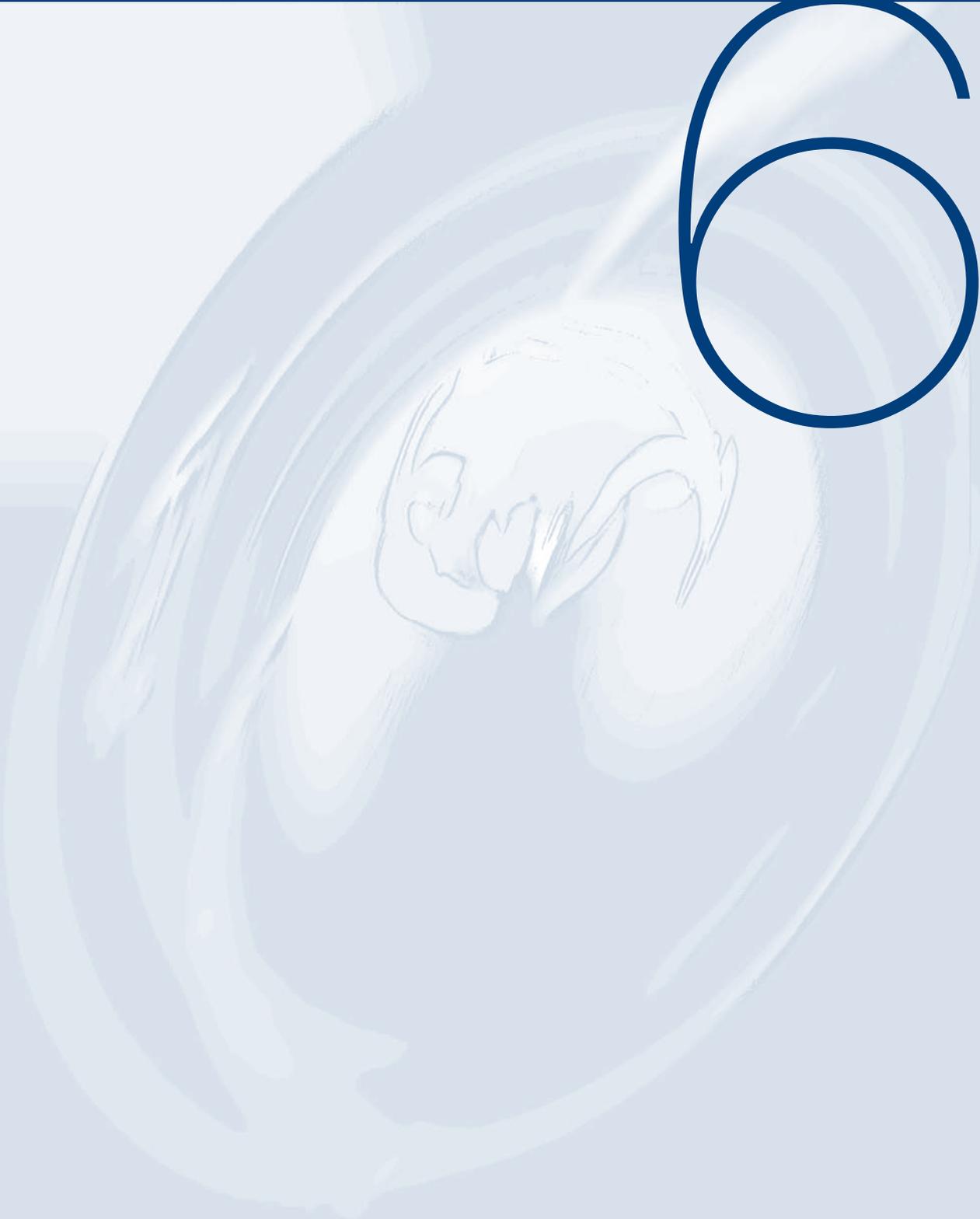
Table 7 and Chart 19 show the development of thermal energy prices to final customers.

Table 7 Average thermal energy prices to final customers

Fuel	2003 [CZK/GJ]	2004 [CZK/GJ]	2005 [CZK/GJ]	2006 [CZK/GJ]	2007 [CZK/GJ]
Coal	313.26	320.94	332.30	344.55	357.59
Other fuels	351.92	369.72	402.36	450.46	454.47
Weighted average	330.78	341.62	362.53	394.95	399.89

Chart 19 Average thermal energy prices to final customers





6.1 Licensing policy

In 2006 licensing focused mainly on awarding licences for electricity generation from renewable resources in lower capacity installations, in response to requests of the operators of newly built generating capacities, and also on businesses' requests for changes to licences, often necessitated by asset transfers.

6.2 Awarding, changing and revoking licences

Licence revocation largely concerned distribution activities in the electricity and gas industries, which were redirected towards a non-business way of operating distribution facilities in compounds of erstwhile industrial complexes. In the heat supply industry, licensing reflected the transition to thermal energy generation in the entities' own local installations.

In 2006 the number of electricity and gas traders rose only slightly.

The numbers of valid licences, broken down by object of business, are listed in Table 8.

Table 8 Numbers of valid licences from 2001 to 2006 by object of business

Licence	2001	2002	2003	2004	2005	2006
Electricity generation	572	1,258	1,302	1,353	1,407	1,467
Electricity distribution	147	395	380	348	321	282
Electricity trade	55	87	106	146	274	285
Gas production	3	8	12	12	14	13
Gas distribution	73	134	136	135	124	103
Gas trade	12	15	17	31	69	83
Gas storage	3	4	4	4	4	4
Thermal energy generation	204	678	688	693	689	674
Thermal energy distribution	215	725	753	747	737	721
Total	1,284	3,304	3,398	3,469	3,639	3,632

The number of administrative proceedings on licence award, change or revocation can be seen in Table 9.

Table 9 Number of licensing proceedings from 2002 to 2006

Licence proceedings	2002	2003	2004	2005	2006
New licences	1,619	376	312	372	413
Licence changes	334	485	493	495	542
Revoked licences	161	137	194	228	229

In 2006 the trend of rising numbers of holders of licences for electricity generation from small hydroelectric power stations continued, the number of applicants for licences for electricity generation in wind power plants increased quite considerably, and interest was shown in the use of photovoltaic for electricity generation and biogas for use in cogeneration. These are plants with low installed capacities; see Charts 20 and 21 and Table 10.

Table 10 Number of plants for electricity generation from renewable resources

Operating plants		2001	2002	2003	2004	2005	2006
Hydro	Number	878	1,154	1,214	1,262	1,271	1,320
	Capacity [MW]	79.03	105.17	110.49	114.80	115.21	122.44
Wind	Number	7	14	17	26	42	57
	Capacity [MW]	3.39	6.97	8.19	11.49	34.41	44.5
Solar	Number	1	1	3	10	13	27
	Capacity [MW]	0.01	0.01	0.02	0.12	0.15	0.35
Biogas	Number	5	6	6	8	14	27
	Capacity [MW]	2.12	2.27	2.27	2.34	2.74	7.9
Landfill gas	Number	5	5	15	15	18	20
	Capacity [MW]	1.27	1.27	3.3	3.3	4.87	5.45
Biomass	Number					2	5
	Capacity [MW]					18.09	18.58

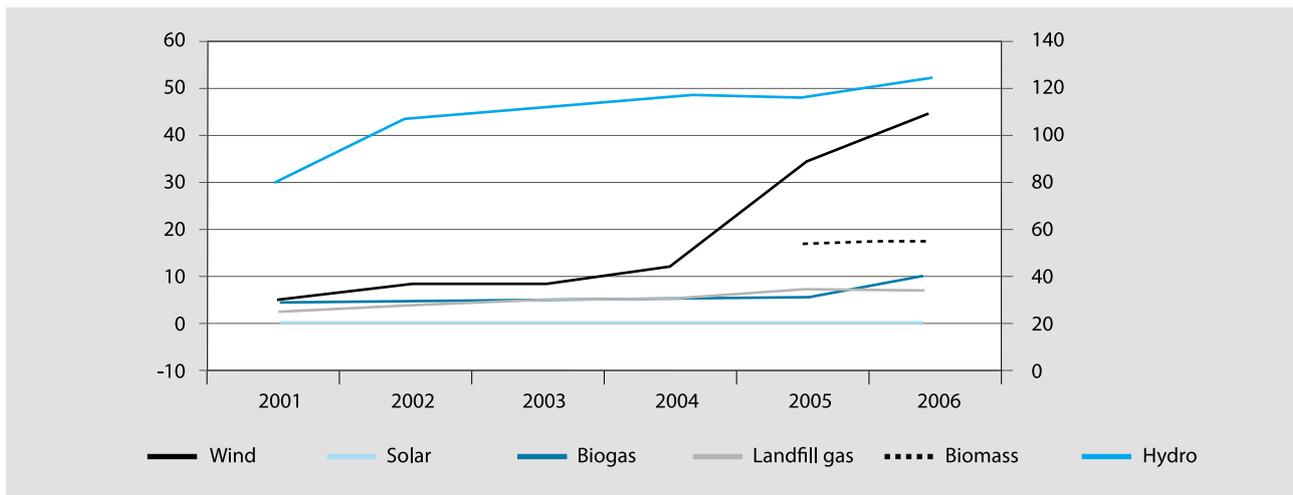
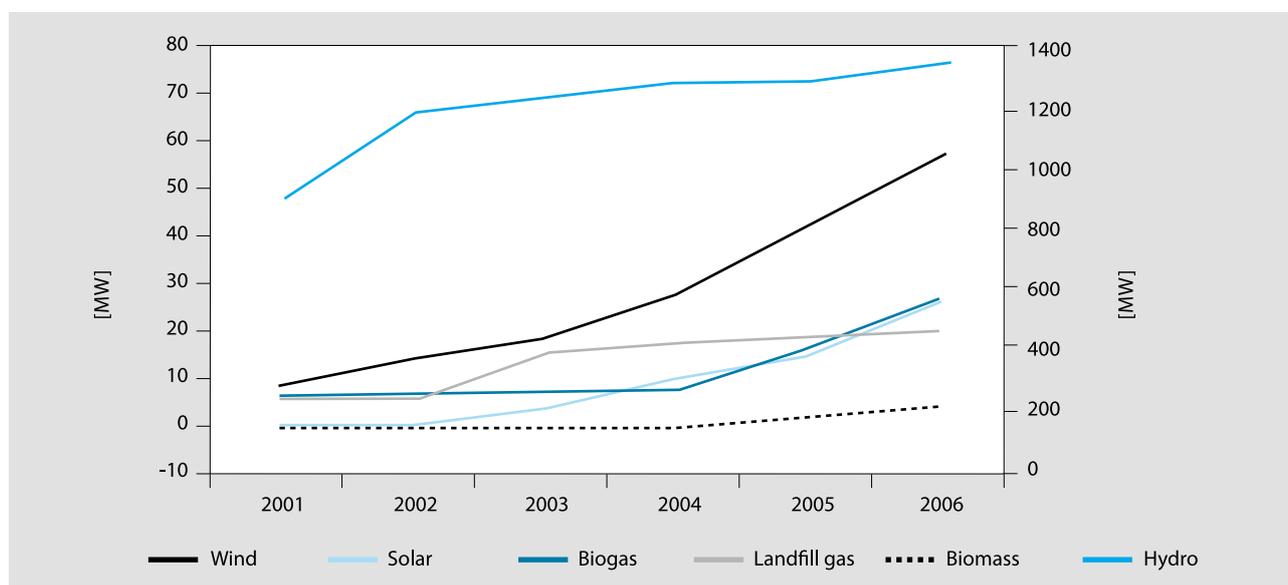
Chart 20 Number of operations based on renewable resources

Chart 21 Installed capacity based on renewable resources

Information on the content of the licences awarded, and on changes to and revocation of licences, is published in the *Energy Regulation Gazette*; a list of valid licences is published on the Office's website; it is a list of licence holders structured by the licence groups. There is also a web application that helps to search for data on a particular licence holder. Subject to the electricity and gas traders' consent their contact details are published to facilitate search for potential electricity and gas suppliers.

6.2.1 Proceedings on administrative fees

In connection with proceedings on licence award, change or revocation, 22 proceedings on administrative fees were conducted, and two licensing proceeding were discontinued for failure to pay the administrative fees.

6.3 Recognition of professional qualifications

In 2006 the Office decided in 14 administrative proceedings on the recognition of professional qualifications, with favourable results. No compensation measures within the meaning of Act No. 18/2004, on the recognition of professional qualifications, were required. More complicated cases were consulted with the national coordinator, Ministry of Education, Youth and Sports of the Czech Republic.

6.4 The Energy Regulation Fund

Under Section 14 of the Energy Act, the Energy Regulatory Office shall keep funds intended as compensation for demonstrable losses suffered by the licence holders who carry out the obligation of supplies over and beyond their licence.

In 2006 the Energy Regulation Fund paid CZK 36,700 from its account to TEDOM s.r.o., a heat supply company that the Office required to provide supplies over and beyond its licence. Since the balance in the account did not decrease to under the stipulated limit there was no need to collect new contributions to the Fund.

Under Public Notice No. 377/2001 as amended, in 2006 regulatory reports were used to find the amount of the sales of 1,691 licence holders in the heat supply industry. Total annual sales achieved in licensed activities for the period of 2005 amounted to CZK 38,267,939,680. Table 11 lists the sales of heat supply companies between 2002 and 2005, showing the strong effect of cold weather at the end of 2005.

Table 11 Sales of heat supply licence holders

Sales [CZK '000]	2002	2003	2004	2005
	37,618,116	36,664,441	34,421,816	38,267,940



Administrative proceedings



7.1 Administrative proceedings

In 2006 five administrative proceedings were concluded in the **electricity industry**. The disputes concerned the following: failure to reach agreement on access to the transmission system and allocation of cross-border capacity; termination of agreements on bundled services of electricity supply from very high voltage and high voltage networks; assignment of the D 45 tariff; and two disputes over the connection of wind power plants between the same parties (the last mentioned case was partly addressed in some other administrative proceedings in previous years). One of the above proceedings was concluded by a decision in the first instance, endorsement of conciliation. In the other four cases the proceedings were concluded by the ERO Chairman's decision on remonstrance.

Similarly as in previous years it can be noted that the situation surrounding disputes has stabilised – only a small number of disputes emerge. This is considerably helped by a stable environment, predictable for the electricity market players, that has emerged thanks to the Office's activities in the promulgation of public notices and price decisions, and also its educational activities, etc. These activities are conducted towards the introduction of clear-cut and unchallenged rules.

A new element was an administrative proceeding in which one of the parties was a foreign person and the Office cooperated with a foreign regulatory authority, specifically the Austrian regulator E-Control.

In 2006 twenty-one administrative proceedings were concluded in the **gas industry**. Most of them concerned failure to execute an agreement on bundled gas supply services in 2005 between traders of regional distribution companies and eligible customers due to disagreement with the proposed price on the part of the customer as an eligible customer (13 proceedings). The Office also decided on the commercial part of gas supplies, primarily on questions of amendments to already executed agreements or failure to sign an addendum to an agreement on bundled gas supply services. In comparison with the commercial part, the issue of distribution was much less controversial (the dispute over an agreement on connection to the distribution system, agreements on gas distribution, the issue of aggregating supply points), but in spite of this the number of disputes increased in comparison with the previous year. Seventeen proceedings were concluded by a first instance decision; in two cases the Office endorsed conciliation. In four cases the proceedings were concluded by the ERO Chairman's decision on remonstrance.

In 2006 the Office decided in one case to revoke an entity's gas distribution licence in connection with imposing the obligation on it to make its energy facilities available, and decided to impose the obligation to provide distribution over and beyond a licence on another entity. Another two similar proceedings were discontinued after the parties' agreement prior to deciding in the case. No case involved any interruption of distribution, and therefore gas supply.

The significant increase in the number of disputes in the gas industry was caused mainly by the initial stages of the gas market liberalisation, which, however, was not accompanied by any genuine functioning of the market or the entry of new traders, i.e. the emergence of a truly competitive environment. The gas industry can therefore now be viewed as the most problematic in terms of disputes.

In 2006 five administrative proceedings were concluded in the **heat supply industry**. One dispute concerned thermal energy price. The other disputes concerned the execution of an agreement (or an addendum to an agreement) on thermal energy supplies (there were various reasons for the disputes: controversy over the setting of the values of the load profiles for 2006, failure to reach agreement on the amount of advance payments and the effective date of the agreement, disagreement with the double-component price of thermal energy and the method of setting the fixed component of the price, change in the way of billing hot water from an exchanger station). Of these proceedings, in 2006 two were concluded by a first instance decision: in one case conciliation was reached and endorsed, in the other the matter was set aside. In three cases the proceedings were concluded by the ERO Chairman's decision on remonstrance.

In comparison with the previous year, when ten proceedings were concluded, the number of disputes decreased considerably. In the heat supply industry the number of administrative proceedings varies considerably year to year. A clear trend is that thanks to the Office's activities, particularly as regards its price decisions (invariability of the basic principles of price decisions) there are less disputes concerning the structure of thermal energy prices and their level – in 2005 there were two proceedings in the area of pricing, in 2006 there was one such dispute. The other disputes concerned failure to reach agreement on the wording of the contract (or addenda thereto) for thermal energy supply.

7.2 Dispute settlement

Electricity industry

Moravská Energetika, s.r.o. and **E.ON Distribuce, a.s.:** Two disputes over the connection of wind power plants to the distribution system (disputes continued from previous years). Demand that an obligation be imposed on E.ON Distribuce to connect Moravská Energetika's plants and that the latter be provided with connectable power of 5.2 MW. Since at the time of filing the motion for the initiation of this proceeding this was not a dispute that the Office had the remit to adjudicate, the proceeding was discontinued.

Mrs Eva Svobodová and **ČEZ Distribuce, a.s.:** Dispute over the assignment of the D 45 tariff. The customer had an agreement on the D 25 tariff and carried out changes in the switchboard, had the changes inspected, and carried out other required modifications to have direct electrical heating installed in the building and the D 45 tariff assigned. According to the distributor it was not technically

feasible to grant the D 45 tariff. Later, the parties executed an agreement on bundled electricity supply services from low voltage networks in the D 45 tariff, and the Office endorsed the conciliation and concluded the proceeding.

Zásobování teplem Vsetín a.s. and ČEZ Prodej, s.r.o.: Zásobování teplem Vsetín's motion for initiating administrative proceedings on failure to reach agreement on the termination of agreements on bundled electricity supply services from very high voltage and high voltage networks. In the event of the termination of agreements on bundled electricity supply services by the parties' mutual consent such consent is not enforceable under the Energy Act and the contracting parties have full contractual freedom whether, and under what conditions, they will terminate their agreements that were entered into "upon their mutual, solemn, understandable and definite discussion and the content thereof reflects the actual state of affairs and is an expression of their true and free will". This was not a dispute the disposal of which fell within the competencies of the Office or any other administrative authority, and the matter was set aside.

ČEZ, a.s. and ČEPS, a.s. (+ ELEKTRIM and PSE): Dispute over failure to agree on access to the transmission system and the allocation of cross-border capacity. Due to the existence of a long-term contract for electrical energy transmission from Poland to Austria over the Czech transmission system, there were reductions in the cross-border capacity offered in auctions for cross-border capacity on lines from the Czech Republic to Austria (the ČEPS/APG interconnection). In his decision on remonstrance the ERO Chairman changed the first instance decision as follows: ČEPS is obligated to offer on the Czech-Austrian ČEPS/APG interconnection, the entire capacity for electricity transmission effective from 1 January 2007, but for the reliability margin under Regulation 1228/2003/EC 2) and the TSO Code.

Gas industry

BMT a.s. and Jihomoravská plynárenská, a.s.: Two disputes over the execution of an agreement on bundled gas supply services. BMT challenged the disclosure of the price charged to the customer and the making of changes to the commercial terms by **Jihomoravská plynárenská** by way of their publishing on **Jihomoravská plynárenská's** website, in one national daily paper and at **Jihomoravská plynárenská's** contact points. In the first administrative proceeding the Office discontinued the proceeding because the parties properly executed an agreement and BMT's requirements did not concern the material points of the agreement. In the second proceeding BMT's demand was rejected because the Office is unable to impose an obligation on a trader to provide the relevant information via electronic mail.

Západočeská plynárenská, a.s. and ŠKODA, KOVÁRNY, Plzeň, s.r.o.: Dispute over failure to sign an addendum to an agreement on bundled gas supply services, concerning the commodity component of the natural gas price, for a period from 1 August 2005 to 31 December 2005. The parties signed an agreement on bundled gas supply services, with provisions on the calculation of the commodity charge for the first half of 2005. The price for the second half-year and the method of its calculation was to be agreed by the parties on the basis of experience in the first half-year. However, no agreement was reached. It was decided that the price for the second half-year would be calculated on the same principle as in the first half-year.

Energetika Vítkovice, a.s. and VÍTKOVICE STEEL, a.s.: Energetika Vítkovice's motion for the initiation of administrative proceedings on failure to execute an agreement on natural gas supply for the first half of 2006. The Office or any other administrative authority did not have the competence to dispose of the dispute, and the case was set aside because the Office received the motion for the initiation of the proceedings as late as September 2006 and the Office may not make retroactive decisions on agreements no longer effective at the time of filing the motion for the initiation of the proceedings.

Energetika Vítkovice, a.s. and VÍTKOVICE, a.s.: Dispute over failure to execute an agreement on bundled natural gas supply services due to differing interpretations of the aggregation of supply points. On the basis of a hearing at the Office, the parties reached consensus on the execution of the agreement and withdrew their motion for the initiation of the proceedings. The Office then discontinued the proceedings.

Mr Radek Fiala and Západočeská plynárenská, a.s.: Dispute over failure to execute an agreement on connection to the distribution system. The applicant noted that he did not receive any draft agreement despite having been issued with an affirmative position on the connection.

STAVEBNÍK - stavební bytové družstvo and Středočeská plynárenská, a.s.: Dispute over the execution of a gas distribution agreement. The Stavebník cooperative was the operator of a local distribution system but was not a gas trading licence holder. From 1 January 2005 only gas traders were authorised to supply gas also to protected customers, and the Stavebník cooperative therefore executed with Středočeská plynárenská an agreement on the conditions of the operation of interconnected gas systems, an agreement on natural gas distribution and an agreement on natural gas distribution to protected customers. The parties reached conciliation, and the proceeding was then discontinued.

RWE Transgas, a.s. and Jihočeská plynárenská, a.s.: Dispute over failure to agree on a proposal for a change of a material provisions of an agreement on natural gas purchase and sale (adjustment to the mechanism for pricing gas to eligible customers). In his decision on remonstrance the ERO Chairman rejected RWE Transgas's proposal for executing an addendum to the agreement on natural gas purchase and sale with Jihočeská plynárenská, in the wording contained in RWE Transgas's proposal, because this dispute did not concern the price, or the method of pricing gas.

CHEMOPETROL, a.s. and Severočeská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that the prices for gas supplies from Severočeská plynárenská to CHEMOPETROL in 2005 were justifiable.

KAUČUK, a.s. and Středočeská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that the prices for gas supplies from Severočeská plynárenská to Kaučuk in 2005 were justifiable.

ČESKÁ RAFINÉRSKÁ, a.s. and Severočeská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that the prices for gas supplies from Severočeská plynárenská to ČESKÁ RAFINÉRSKÁ in 2005 were justifiable.

Teplárny Brno, a.s. and Jihomoravská plynárenská, a.s.: Dispute over failure to execute an addendum to an agreement on gas purchase and sale due to the customer's, as the eligible customer's, disagreement with the proposed price. The parties reached agreement and withdrew their motion for the initiation of the administrative proceedings. The Office then discontinued the proceeding.

SPOLANA a.s. and Středočeská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. On the basis of a hearing at the Office agreement was reached, and the Office then endorsed the conciliation.

KRKONOŠSKÉ PAPIRNY a.s. and Východočeská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that the prices of gas supplies from VČP to KRKONOŠSKÉ PAPIRNY in 2005 were justifiable.

ENERGETIKA TŘINEC, a.s. and Severomoravská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that Severomoravská plynárenská justifiably requested ENERGETIKA TŘINEC to execute a bundled gas supply agreement, with price provisions setting out a total amount of payment for 331,401 MWh of gas supplied in 2005 at no more than CZK 192,115,110.

Energetika Vítkovice, a.s. and Severomoravská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that the prices for gas supplies from Severomoravská plynárenská to Energetika Vítkovice in 2005 were justifiable.

LASSELSBERGER, a.s. and Západočeská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that the prices for gas supplies from Západočeská plynárenská to LASSELSBERGER in 2005 were justifiable.

LASSELSBERGER, a.s. and Středočeská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that the prices for gas supplies from Středočeská plynárenská to LASSELSBERGER in 2005 were justifiable.

BorsodChem MCHZ, s.r.o. and Severomoravská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that Severomoravská plynárenská justifiably requested BorsodChem MCHZ to execute a bundled gas supply agreement, with price provisions setting out a total amount of payment for 648,618 MWh of gas supplied in 2005 at no more than CZK 356,008,630.

Precheza a.s. and Severomoravská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that Severomoravská plynárenská justifiably requested Precheza to execute a bundled gas supply agreement, with price provisions setting out a total amount of payment for 220,801,002 kWh of gas supplied in 2005 at no more than CZK 119,995,670.

Zásobování teplem Vsetín a.s. and Severomoravská plynárenská, a.s.: Dispute over failure to execute an agreement on bundled gas supply services due to the customer's, as the eligible customer's, disagreement with the proposed price. It was decided that Severomoravská plynárenská justifiably requested Zásobování teplem Vsetín to execute a bundled gas supply agreement, with price provisions setting out a total amount of payment for 168,564 MWh of gas supplied in 2005 at no more than CZK 93,414,640.

Heat supply industry

Pražská teplárenská a.s. and Stavební bytové družstvo STAVBAŘ, družstvo: Dispute over the setting of the values of the load profiles for 2006. According to Pražská teplárenská, the Stavební bytové družstvo STAVBAŘ cooperative demanded the recalculation of the load profile values for 2006, proposed by Pražská teplárenská on the basis of actual consumption in 2004, to temperatures of 2000, which, however, Pražská teplárenská said was at variance with its commercial terms for thermal energy supply (OPDT/2004) and a decision of the Office for the Protection of Competition (ÚOHS). The Office rejected Pražská teplárenská's proposal because despite the Office's request, Pražská teplárenská did not prove the justifiability of its demand in any way; nor did ÚOHS Decision No. 138/04 support the proposal demanded by Pražská teplárenská.

VYTEP UNIČOV s.r.o. and Stavební bytové družstvo Olomouc: Dispute over the signing of price clauses and payment schedules for 2006 for supply points in Lutín and in Olomouc, Přichystalova Street, due to disagreement with the thermal energy price for 2006. It was determined that the preliminarily calculated thermal energy price of VYTEP UNIČOV s.r.o. in 2006 for the price locality Olomouc, Přichystalova Street, amounted to CZK 452.41/GJ w/o VAT and for the price locality Lutín to CZK 452.84/GJ w/o VAT.

Pražská teplárenská a.s. and Společenství vlastníků jednotek Budějovická 557: Pražská teplárenská asked the Office to decide on a change in the method of billing hot water from an exchanger station at Antala Staška 82/1345, Praha 4. Since there existed an agreement on the method of allocating costs to supply points under Section 78, subsection 3(e) of the Energy Act, the Office or any other administrative authority did not have the competence to dispose of this dispute and the matter was set aside.

ERDING, a.s. and TEBO, a.s.: Dispute over the execution of an addendum to an agreement on thermal energy supply, concerning the amount of advance payments, effect of the agreement, and the price. On the basis of a hearing at the Office the parties reached agreement on heat supplies for 1Q 2006 (ERDING declared that after 1Q it would terminate the offtake and would procure thermal energy in some other way); subsequently the Office endorsed the conciliation.

The municipality of Roštín and Mr Jan Bábík and Mrs Vladimíra Ludvová: Dispute over the execution of agreements on thermal energy supply. Since the until then existing agreements were not satisfactory, new draft agreements on heat supply were presented and the single-component thermal energy price was changed to a double-component thermal energy price, composed of a variable component billed on the basis of the metered quantity of thermal energy and a fixed component independent of the thermal energy quantity taken, while for calculating the fixed component the supplier selected thermal output and in the draft heat supply agreement the thermal output was set out on the basis of the installed capacity of the house delivery stations. It was decided that the agreement complied with legal regulations and that the price was formulated in accordance with ERO Price Decision No. 9/2004 as amended, and that the customers had to sign the agreement if they wanted to continue to take the heat supply.

Price inspections

Under Section 2c of Act No. 265/1991 on the competencies of the Czech Republic's authorities in the area of prices, as amended, and under Sections 1 and 14 of Act No. 526/1990 on prices, as amended (the Price Act), the Office is authorised to check compliance with the Price Act. Because of the situation on the newly liberalised gas market and the numerous complaints received from eligible customers, the Office conducted checks of whether or not the traders of regional distribution systems and the transmission system breached the obligation set out in Section 2, subsection 3 of the Price Act in their gas supplies to eligible customers under Section 15, subsection 3 of the Price Act in 2005 (January to December).

The Office found that Severomoravská plynárenská, a.s., Východočeská plynárenská, a.s., Středočeská plynárenská, a.s., and RWE Transgas, a.s. violated Section 2, subsection 3 of the Price Act and decided to impose fines on them for these violations. The administrative fines are described in detail in part 11.6.

7.3 Administrative proceedings in which the ERO Chairman delivered decisions on remonstrances

Under Act No. 500/2004, Administration Code [rules of administrative procedure], remonstrances fall within the competencies of the ERO Chairman, who decides upon proposals submitted to him by the remonstrance commission appointed by him. This commission is composed of ten, mostly external experts, lawyers, engineering experts, and economists. In 2006 the Office received 17 remonstrances against its first instance decisions.

Electricity industry

Moravská Energetika, s.r.o. and E.ON Distribuce, a.s.: Upon the remonstrance commission's proposal the ERO Chairman delivered a rejecting decision on the remonstrance; the Office's first instance decision therefore became final. The reason for this decision was the fact that Moravská Energetika initiated the resolution of the dispute with E.ON Distribuce too early, prior to the expiry of the time limit for E.ON Distribuce's comments; this time limit starts running only after the filing of a request for comments, free of any factual and formal defects, under the respective public notice (No. 18/2002 on the conditions of connection and electricity transport in the electricity grid, now No. 51/2006 on conditions of connection to the electricity grid).

Moravská Energetika, s.r.o. and E.ON Distribuce, a.s.: In this proceeding, on a similar matter as in the above case, a rejecting decision on the remonstrance was delivered, also for procedural reasons.

Zásobování teplem Vsetín a.s. and ČEZ Prodej, s.r.o.: The Office delivered a resolution whereby it discontinued the proceeding on the dispute over failure to agree on the termination of agreements on bundled electricity supply services. Zásobování teplem Vsetín filed a remonstrance against this decision. In a decision on the remonstrance it was rejected on the grounds that the Office's remit may not be extended by an extensive interpretation of the respective provisions of the Energy Act to include also the termination of such relationships, because this would result in a constitutionally impermissible expansion of interference by a governmental authority vested with executive powers with contractual relationships, and the Office's decision was upheld.

ČEZ, a.s. and ČEPS, a.s. (+ ELEKTRIM and PSE): Österreichische Elektrizitätswirtschafts-Aktiengesellschaft filed a remonstrance against the Office's decision on the award of the status of a party to the proceedings on access to the transmission system and allocation of cross-border capacity. In the first instance decision, the Office did not find any content-related conflict in the sources of the *acquis* and the national law such as would have prevented it from deciding on the matter. The decision on the remonstrance partially changed the Office's reviewed decision to accept objections of procedural nature to the rulings in the original decision, without casting any doubt at all on the "mainstay grounds for the decision", on which the Office's first instance decision had relied. For the above reasons the remonstrance was rejected, and the Office's decision upheld.

Gas industry

BMT a.s. and Jihomoravská plynárenská, a.s.: BMT filed a remonstrance against the decision in the dispute over whether an eligible customer has the right to have in its agreement with a gas trader, provisions on the trader's obligation to inform the customer about changes in the price and commercial terms in writing to the customer's address or via electronic mail. In the remonstrance proceedings the objections raised were dealt with. Since the petitioner itself defines the subject matter of the proceedings in its submittal and in its motion for the administrative authority's decision, and since in this particular case the petitioner's submittals defined the subject matter of the proceeding, the decision on remonstrance rejected it and upheld the Office's first instance decision.

Mr Radek Fiala and Západočeská plynárenská, a.s.: In the remonstrance proceedings the ERO Chairman changed the impugned decision and ordered Západočeská plynárenská to provide Mr Radek Fiala with a new draft agreement on connection, in particular because there was no examination of whether or not Západočeská plynárenská proceeded in a "positively" discriminatory way in relation to any other persons wanting to have gas supplies in the particular locality, although it is not possible to legally force a gas distribution company to extend distributions for the purpose of bringing gas supplies to a certain parcel of land and the residential house being built on it.

Západočeská plynárenská, a.s. and ŠKODA, KOVÁRNY, Plzeň, s.r.o.: On the remonstrance filed by Západočeská plynárenská against the Office's decision delivered in the dispute between the former company and ŠKODA, KOVÁRNY, Plzeň over failure to execute an addendum to an agreement on bundled gas supply services, concerning the commodity charge, the ERO Chairman decided in his decision on the remonstrance, whereby he rejected the remonstrance in view of the Office's remit to adjudicate the so-called price disputes between parties to agreements on bundled gas supply services and in view of the potential form in which this type of dispute may be decided (the decision may be either constitutive or declaratory), and upheld the Office's first instance decision.

RWE Transgas, a.s. and Jihočeská plynárenská, a.s.: RWE Transgas filed a remonstrance against the Office's decision in the dispute over the execution of an addendum to an agreement on natural gas purchase and sale, in which it primarily claimed that the matter had been incorrectly assessed as to the law, i.e. the concept of the dispute as a dispute over the interpretation of the agreement, for the adjudication of which the Office has no remit, rather than as a dispute over the execution of an addendum to the agreement, for the adjudication of which the Office does have the remit. In his decision on the remonstrance the ERO Chairman changed the first instance decision on procedural grounds, by rejecting RWE Transgas's motion for the imposition of an obligation on Jihočeská plynárenská to execute the addendum to the agreement on natural gas sale and purchase.

Heat supply industry

Pražská teplárenská a.s. and Stavební bytové družstvo STAVBAŘ, družstvo: Pražská teplárenská filed a remonstrance against the Office's decision on the dispute over the load profile values for 2006. The remonstrance was rejected on the grounds that the petitioner failed to furnish any evidence to support its claims.

VYTEP UNIČOV s.r.o. and Stavební bytové družstvo Olomouc: Remonstrance proceedings – in which all the objections raised were examined – took place on the remonstrance filed by Stavební bytové družstvo Olomouc against the Office's decision delivered in the dispute with VYTEP UNIČOV over the signing of price clauses and payment schedules for 2006, concerning disagreement with the amount of the preliminarily calculated thermal energy price for 2006. In the decision the remonstrance was rejected, in particular on the grounds that the supplier's profit could increase year on year, since it was below the price level set out in point 1.2 of ERO Price Decision No. 9/2004 and since the Office does not examine the purposes for which the supplier uses its profit, as the purpose for which profit is used is solely up to the supplier.

The municipality of Roštín and Mr Jan Bábík: Remonstrance proceedings took place on Mr Jan Bábík's remonstrance against the Office's decision delivered in administrative proceedings instigated under Section 17, subsection 8(a) of the Energy Act by the municipality of Roštín, on the dispute over the execution of an agreement on heat supply between Roštín, as a holder of licences for thermal energy generation and distribution, and Mr Jan Bábík, a customer for thermal energy; in the proceedings a rejecting decision on the remonstrance was delivered, and the Office's decision upheld. There was a certain change as against the first instance decision in the substantiation thereof, concerning the obligation to pay the costs incurred in the working of the exchanger.

The municipality of Roštín and Mrs Vladimíra Ludvová: Remonstrance proceedings on a similar subject matter as in the above dispute between Roštín and Jan Bábík were initiated in the case of the municipality of Roštín and Mrs Vladimíra Ludvová. Also in this case, and on the same grounds, the remonstrance was rejected and the Office's first instance decision upheld.

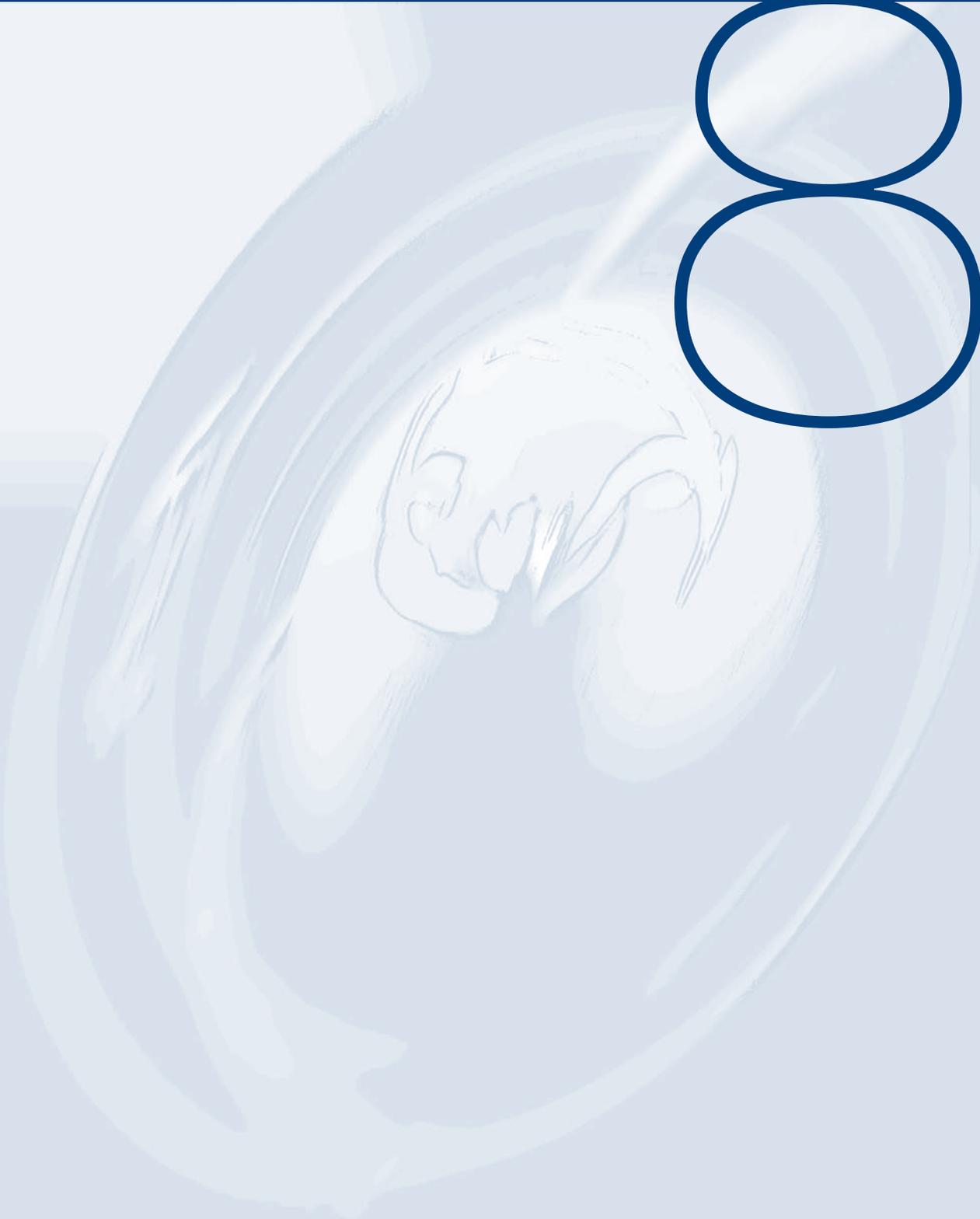
Licence revocation

Milan Bušek: In proceedings initiated under official duty, the Office decided to revoke a licence for electricity generation on the grounds specified in Section 10, subsection 2(a) of the Energy Act, because the licence holder no longer met the Energy Act's conditions for holding this licence on the basis of a final judgment. The Supreme Court later reversed this final judgment. On the basis of this reversal the Office allowed the proceeding to be reopened. After commencing the reopened proceeding under Section 100 *et sequentes* of Act No. 500/2004, Administration Code, on the revocation of the licence for failure to meet the condition of the licence holder's probity, the proceeding was stayed upon Mr Bušek's motion pending the conclusion of the court proceedings.

Price inspections

Severomoravská plynárenská, a.s.: In appellate proceedings, the remonstrance filed by Severomoravská plynárenská against the Office's decision to impose a fine of CZK 8,569,390 under Section 15, subsection 3 of the Price Act was rejected in a decision on this remonstrance, particularly in view of the general provision contained in Section 2, subsection 3 of the Price Act, under which the seller is not allowed to abuse its economic position to win an unreasonable economic gain through sale for an agreed price covering unjustifiable costs or unreasonable profit. This provision is directed especially at market relationships in which prices are not subject to control by any of the methods of permissible price control (so-called free prices).

Remonstrance proceedings on a similar subject matter were also initiated with **Východočeská plynárenská, a.s.**, **Středočeská plynárenská, a.s.**, and **RWE Transgas, a.s.** Remonstrances against the decisions were filed. Decisions on remonstrances upheld the first instance decisions. In respect of each of these companies two analogous decisions concerning a procedural question (the time limit under Section 36, subsection 1 of the Administration Code) were delivered in addition to the decision on the merits of the case.



8.1 Co-operation with central state administration authorities

In accordance with the Energy Act and other general and special laws and regulations the Office cooperates primarily with the Ministry of Industry and Trade (MPO), Ministry of Finance, Ministry of the Environment, Ministry of Education, Youth and Sports, Ministry of Foreign Affairs, Office for the Protection of Competition, the State's Energy Inspectorate (SEI) and other administrative authorities in the energy sector.

In 2006 the Office worked with the MPO's legal and energy experts in the assessment of the experience with the application of the Energy Act as the basic framework creating the environment for the operation of energy market participants. Analysis of common experience is the basis for drafting amendments to implementing regulations promulgated by the two authorities and also for drafting an amendment to the Energy Act, which is to be completed in 2007.

In its activities the Office proceeds from the framework established by the Czech Republic's National Energy Concept. The ERO Chairman informs the Minister of Industry and Trade about the Office's principal conceptual plans, and the drafting of its price and other decisions that might have social and macroeconomic impacts. The Office submits information about important price decisions to the Czech Government.

In 2006 the co-operation between the Office and SEI intensified; this co-operation stems from the legislative framework as well as the needs of the regulatory process. The Office and SEI communicated in respect of specific review actions conducted for the Office's needs and the preparation of documentation for administrative proceedings. This extensive co-operation and close consultations with SEI resulted in the signing of a programme of co-operation between these two authorities for 2007 and beyond. Review actions in the various cases addressed by the Office and a system of drawing conclusions from administrative proceedings were specified in detail. In twelve cases the Office referred the complaints to the SEI under ERO Measure No. 3/2006, which changes the Office's organisational arrangement.

For the Council for Economic and Social Consensus ("the tripartite council"), the Office prepared, at the beginning and at the end of 2006, a detailed report containing forecasts of prices in the electricity, gas and heat supply industries. With the Ministry of Foreign Affairs the Office continued the preparation of the briefs to be used for the Czech Republic's positions on various documents of European institutions.

8.2 Co-operation with the Czech Parliament

Under the Energy Act the Office has the obligation to inform the Czech Parliament about its activities in the form of the *Report on the Activities and Finances of the Energy Regulatory Office*. Throughout the calendar year the Office maintained continuous contacts with the committees of the House of Deputies, especially the Economic Committee and the Committee for Public Administration, Regional Development and the Environment, and, as the Czech presidency of the EU approaches, also the European Affairs Committee.

The Office also cooperates with Senate committees: the Committee for Economy, Agriculture and Transport and the Committee for Regional Development, Public Administration and the Environment, and the EU Affairs Committee. In the committees of both houses the Office's representatives regularly attended debates and technical seminars on the energy sector and renewable resources.

8.3 Public relations

8.3.1 Information provision

The Office's scope of competencies provides broad room for promoting a communication strategy vis-à-vis both expert circles and lay public, and the media.

In compliance with Act No. 106/1999 on free access to information, as amended, the Office provides information on its activities falling within its terms of reference.

The Office provided all the information requested under the above law free of charge, as in the previous years.

Table 12 Number of received and handled requests for information in 2006

Area	Licensing	Regulation	Other	Total
Number	5	46	1	52

The requests for information under the above law concerned mainly the Office's activities in regulation, particularly in relation to market liberalisation, and also its Price Decisions. Many questions also concerned issues related to the Energy Act and related regulations. A smaller part of questions asked about licences and the Office's further competencies. All requests for information were answered within the statutory time limit. In 2006 the Office did not receive any appeal against a decision in writing refusing to provide the information requested.

In 2006 the Office's relevant technical units also handled several thousand additional (technical) questions as part of their everyday correspondence.

The Office presents its activities, and its status among central state administration authorities, through press conferences, press releases, interviews and articles in the media and notices in the press or on its website. In 2006 it organised four press conferences at which its senior officers provided information about the Office's most important decisions, in particular as regards prices and regulation.

The Office continuously communicated with all media. Its specialists answered journalists' questions without any undue delay and responded to all requests for technical articles intended for publishing. During the year the ERO Chairman and other senior officials appeared on all television stations; participated in technical discussions on Czech Radio and other radio stations, both national and regional, and in technical conferences held by respected economic periodicals. The Office pursued systematic co-operation with the Czech Press Agency and other news agencies, and trade press titles.

The development of the Internet, which has become a tool of quick communication and information, causes increased requirements for easy access to, timeliness, and content of the information provided.

In 2006 the Office's website (www.ero.cz) was changed somewhat; particularly in its Czech version the basic menu was arranged more clearly to be as user friendly as possible and to support quick access to the most frequently visited pages (their list is based on statistical research). On the basis of a user survey an additional, graphically distinctly laid out, horizontal pull down menu was created, offering the most interesting and current information (for example, FAQ, supplier switching for each of the energies, etc.).

The Office made it possible for the expert circles and lay public to provide their comments on the forthcoming legislation. This service has turned out to be highly beneficial, and both the technical units of the Office and the respondents appreciate it. Also the English version of the website was adjusted in relation to the Czech version.

The autumn of 2006 saw the launch of an application that makes it possible to place some information on the Office's website via remote access directly, without any assistance by an external company. This application now covers the most important and most frequently visited pages, such as Legislation, Price Decisions, and ERO Communications. The Office will continue this process also next year.

8.3.2 Publications

The Office produces its publications under the Energy Act. Among others, it publishes the *Energy Regulation Gazette*, which appeared with a circulation of 1,000 in 2006 (there were 814 subscriptions). In 2006 eleven issues of the *Gazette* were published; four of them carried a list of holders of licences awarded for business in the energy industries, including a list of licences that had terminated, or were revoked or expired. Twelve price decisions were published, of which five on electricity prices, four on natural gas prices, and three on thermal energy prices. The *Gazette* also carried three notices of the approval of the rules for the operation of energy systems, on the assessment of the share of electricity produced from renewable resources in gross electricity consumption, and the expected impacts of support for electricity generation from renewable resources on the overall price to final customers, a public announcement, an overview of the total annual revenues from licensed activities for 2005, classes of typical natural gas supply profiles, a report on the management of the Energy Regulation Fund for the previous calendar year, and an overview of disputes and administrative proceedings conducted by the regulation section and licensing department in 2006.

Owing to a change to Act No. 526/1990 on prices, of 29 May 2006, the Office has a new obligation to publish in the Collection of Laws, with effect from 1 June 2006, communications on the price decisions it has issued and announced in the *Gazette*.

The Office is the central point for the processing of operating and technical data for the Czech electricity industry; it is supplied with this data mainly by the entities that hold licences for business in the electricity industry. These include 1,298 electricity generators having an aggregate installed capacity of less than 0.5 MWe, 201 electricity generators having an aggregate installed capacity of 0.5 MWe and more, 281 electricity distributors, 292 electricity traders, and the electricity transmission licence holder and the electricity market operator. This data is used in monthly reports on the operation of the Czech electricity grid, which are posted on the Office's website and their abridged versions are provided to the energy trade press and other media. Once a year the Office produces an *Annual Report on the Operation of the Czech National Electricity Grid*, which appears in the printed and electronic forms (an executive summary offering the most important data is also published in English). Both expert circles and the lay public show increasing interest (particularly in connection with the liberalisation of the energy markets) in information from this area; the number of questions is rising and also consultation activities related to electricity industry statistics are growing.

The Office's important position as regards statistical research is also borne out by the fact that it has become the coordinator for state administration in statistics on the electricity industry. The Czech Statistical Office accepts the Office's output completely. The Office has also established close contacts with the Ministry of Industry and Trade in respect of the processing of information supplied by licensed electricity generators, especially with emphasis on data on renewable resources for electricity generation.

In co-operation with EGÚ Brno, a.s., a unique compilation of maps, schemes of the Czech national grid's 110 kV, 220 kV and 400 kV networks, was produced.

Both as hard copy and on CD-ROM, in both Czech and English, *The 2005 Report on the Activities and Finances of the Energy Regulatory Office* was produced. The Office submits this Annual Report to the Czech Government and the Chamber of Deputies of the Czech Parliament every year in accordance with the Energy Act.

8.4 The Chairman's Advisory Corps

As in previous years in 2006 the ERO Chairman's Advisory Corps included experts delegated by governmental authorities, consumer and business associations, and trade unions; on the basis of their own expert opinions and assessments they contributed to the Office's positions and supported the Office's and its Chairman's decisions, primarily in strategic regulatory issues and unbundling.

In 2006 the Advisory Corps held four meetings.

At the January meeting they took due note of the report for the Czech Prime Minister on the development of energy prices, and recommended further steps in the area of information processing, supported the unbundling process followed by the Office in electricity distribution companies, and received information about preparations for the unbundling process in gas distribution companies.

In April they took due note of information about the assessment of the conclusions of the sector inquiries into the electricity and gas industries in the EU member states and supported the Office's steps conducive to the development of electricity and gas markets in the Czech Republic; took due note of information about the development of gas prices in the second quarter of 2006, about the EU's new energy policy – the Green Paper, and about the European Commission's formal letter on the implementation of EC Directives in Czech legislation.

At the September meeting they took due note of information about gas prices in the third and fourth quarters of 2006 and outlooks for the first quarter of 2007 and supported the Office's regulatory steps after 1 January 2007. They received information about the conclusions of the MPO/ERO task force, which had been set up to clarify the causes of the situation that prompted ČEPS, a.s. to declare a situation of emergency on 25 September 2006.

In November the advisory corps supported the principles of the provisions on support for electricity generation from renewable resources for 2007 and the principles of the new market rules, and took due note of the conclusions of the European Commission's public consultation on the Green Paper.

8.5 Activities related to membership of commissions

In 2006 the Office cooperated with the Ministry for Regional Development in connection with the drafting of the Czech Republic's Regional Development Policy, and regularly attended the meetings of the Consultation Committees for the drafting of the Czech Republic's Regional Development Policy.

ERO officials regularly attended meetings of the Inter-departmental Expert Commission for Electronic Communication in EU Agendas, which is an advisory body working for the Czech Government; its task in 2006 was to resolve the question of the operation of a secure system, the EU Extranet ČR, and options for domestic electronic communication of documents classified as "restricted".

As part of the updating of the institutional provisions for the Czech Republic's membership of the European Union, the Office formally joined the existing institutional framework, provided that from 1 June 2006 it was, similarly as the other state administration authorities, an associated member of the Committee for the European Union (V-EU). Through this inclusion the Office obtained an opportunity to effectively monitor and influence the development of opinions on issues falling within its remit at V-EU meetings and for a fully-fledged involvement in state administration's preparations for the Czech presidency of the EU in 2009.





The Czech Republic's accession to the European Union caused the Office to become a full member of the non-profit Council of European Energy Regulators (CEER) and the European Regulators Group for Electricity and Gas (ERGEG), the European Commission's advisory group on matters of the general monitoring of the activities arising, above all, from Directive 2003/54/EC¹⁾ concerning common rules for the internal market in electricity and Directive 2003/55/EC⁴⁾ concerning common rules for the internal market in natural gas, and Regulation 1228/2003/EC²⁾ on conditions for access to the network for cross-border exchanges in electricity. In 2006 the Office's representatives took an active part in the meetings of these two organisations, as well as those of other European groups and advisory committees that had been set up to tackle key issues, such as the allocation of cross-border capacities, regional initiatives, and the new energy policy for Europe.

9.1 The Czech National Report

As part of the reporting and notification obligations arising for the Czech Republic as an EU member state from Directives 2003/54/EC¹⁾ and 2003/55/EC⁴⁾, and also Directive 2004/67/EC⁵⁾ concerning measures to safeguard security of natural gas supply, by 30 July 2006 *The Czech Republic's National Report on the Electricity and Gas Industries for 2005* was delivered to the European Commission. This already second national report described the progress in the development of the competitive environment in the electricity and gas markets achieved by the Czech Republic from the first national report to July 2006. The Energy Regulatory Office took on the role of the coordinator in the Czech Republic; the Ministry of Industry and Trade and the Office for the Protection of Competition contributed to the preparation of the national report. The national report outlines the key changes in the legislative environment and the position of the major participants in the domestic market, and also covers important events and issues on the energy market in the period under review.

The Czech Republic will submit the national report under the above Directives every year until 2010, and thereafter once every two years.

9.2 CEER and ERGEG

The Office cooperated with CEER and ERGEG in the period under review. Their activity focuses on achieving a single competitive European energy market. This co-operation mainly consisted in taking an active part in meeting of working groups and task forces (electricity, gas, single energy market, information exchange and training, customers), which addressed, among others, issues of transparent and competitive markets, cross-border interconnection, consumer protection, and security of supplies. The Office devoted considerable attention to the new mechanism of CBT compensation payments between the national TSOs. The Office's representatives also took an active part in the activities of the group set up in connection with the massive blackout in the European electricity network on 4 November 2006 and in the preparation of a number of documents. In the electricity industry these included, for example, the Guidelines of Good Practice for Electricity Balancing Markets Integration (general recommendations for creating the opportunity to trade in balancing energy between TSOs), Congestion Management Guidelines (methodology of implicit and explicit auctions) and Guidelines for Good Practice on Information Management and Transparency in Electricity Markets (recommendations on the provision of information intended for wholesale market participants). In the gas industry the Office contributed to the Guidelines for Good TPA Practice for Storage System Operators.

9.3 Regional initiatives in the electricity and gas markets

The end of February 2006 saw the launch of regional initiatives on the electricity market, aimed at removing the barriers preventing free trade on the regional level and a gradual creation of a single European electricity market. The Czech Republic was included in the Central - East European Regional Market, presided over by the Austrian regulator. The Office's representative attended the meetings of the Regional Coordination Committee attended by regulators, and meetings of the Implementation Group for Congestion Management and Transparency attended by regulators and TSOs. Of the key priorities that were set out for the region, primarily Coordinated Congestion Management was important for the Office. During these meetings the Office supported the efforts of ČEPS, a.s., which played the role of the auction office for the region in 2006, for the expansion of coordinated explicit auctions to the whole region. The meetings also devoted considerable attention to differences in the competencies held by the various regulators in the region, and transparency issues.

With a four-month delay also regional initiatives in the gas market were launched, pursuing similar objectives. The Czech Republic was included in the South-South East Regional Market, presided over by the Italian and Austrian regulators. In 2006 meetings of the Regional Coordination Committee, attended by regulators, and of the Implementation Group for Congestion Management and

⁴⁾ Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003, concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC.

⁵⁾ Directive 2004/67/EC of the European Parliament and of the Council of 26 April 2003 concerning measures to safeguard security of natural gas supply.

Transparency, attended by regulators and TSOs, took place. Both groups aimed at ensuring co-operation with regulators, ministries and key investors from the various countries. The Office took an active part in the preparation of documents on progress in the implementation of Directive 2003/55/EC⁴ and the steps taken to implement Regulation 1775/2005/EC³. Issues of transparency, interoperability and storage facilities were also important for the Office

9.4 The Czech Republic's positions on EU institutions' activities

The Office closely cooperated with the Ministry of Industry and Trade's department responsible for international relations in energy, on materials for the Czech Republic's delegates to the meetings of the energy task force and on preparing the mandate of the Minister of Industry and Trade for meetings of the Transport, Telecommunications and Energy Council (EU Council) focused on energy. These documents dealt primarily with the liberalisation of energy markets and the related strengthening of competition, and the harmonisation of regulatory authorities' powers in cross-border trading.

The Office also worked with the Ministry of Industry and Trade on preparing the answer to the European Commission's letter of formal notice concerning the initiation of infringement procedure under Article 226 of the Treaty. In its letter the European Commission argued that the Czech Republic did not correctly transpose Articles 15(2), 3(6), 3(9) and 9(e), and Articles 13(2), 19(3), 3(6) and 18(1) of Directives 2003/54/EC¹ and 2003/55/EC⁴, respectively.

In co-operation with the Ministry of Industry and Trade and the Ministry of Foreign Affairs the Office also prepared the documentation for public service notification to the European Commission on the introduction of measures consisting in imposing control on prices of natural gas supplies to eligible customers. An analysis of the reasons for these measures was attached to the notification.

9.5 Twinning with the Ukraine

In August 2006 the ERO, AEEG (Italian regulator) and E-Control (Austrian regulator) were selected as winners in the call for proposals for a Phare Twinning-out Project, "Regulatory and Legal Capacity Strengthening of Energy Regulation in NERC" in the Ukraine. The project's objective is to strengthen the position of the Ukrainian energy regulatory authority, NERC, help draft primary and secondary legislation complying with the EU *acquis*, and also to help implement a new model of the wholesale electricity market.

In addition to AEEG, also the Italian ministry of finance and economy is a contracting partner in the position of the Phare Twinning-out Project leader; together, they are in charge of the administrative aspects of the project. The ERO and E-Control have the roles of the junior partners. In the second half of 2006 several meetings were held to prepare the Twinning Contract, which is to be signed between the project leader (AEEG) and project beneficiary (NERC). In November 2006 the first draft of the Twinning Contract was sent to NERC and Delegation of the European Commission in Ukraine for approval.

9.6 Trips to other countries

During 2006 the Office's staff attended a number of international meetings, meetings with partner regulators, and technical seminars and study visits in line with the Office's mission in the area of international co-operation and involvement in the activities pursued by international groups and associations. Another objective of these meetings was to gain new experience related to issues such as the development of regulation and its models, and new knowledge on issues such as support for renewable energy resources, unbundling, and market functioning from the European and global perspective.

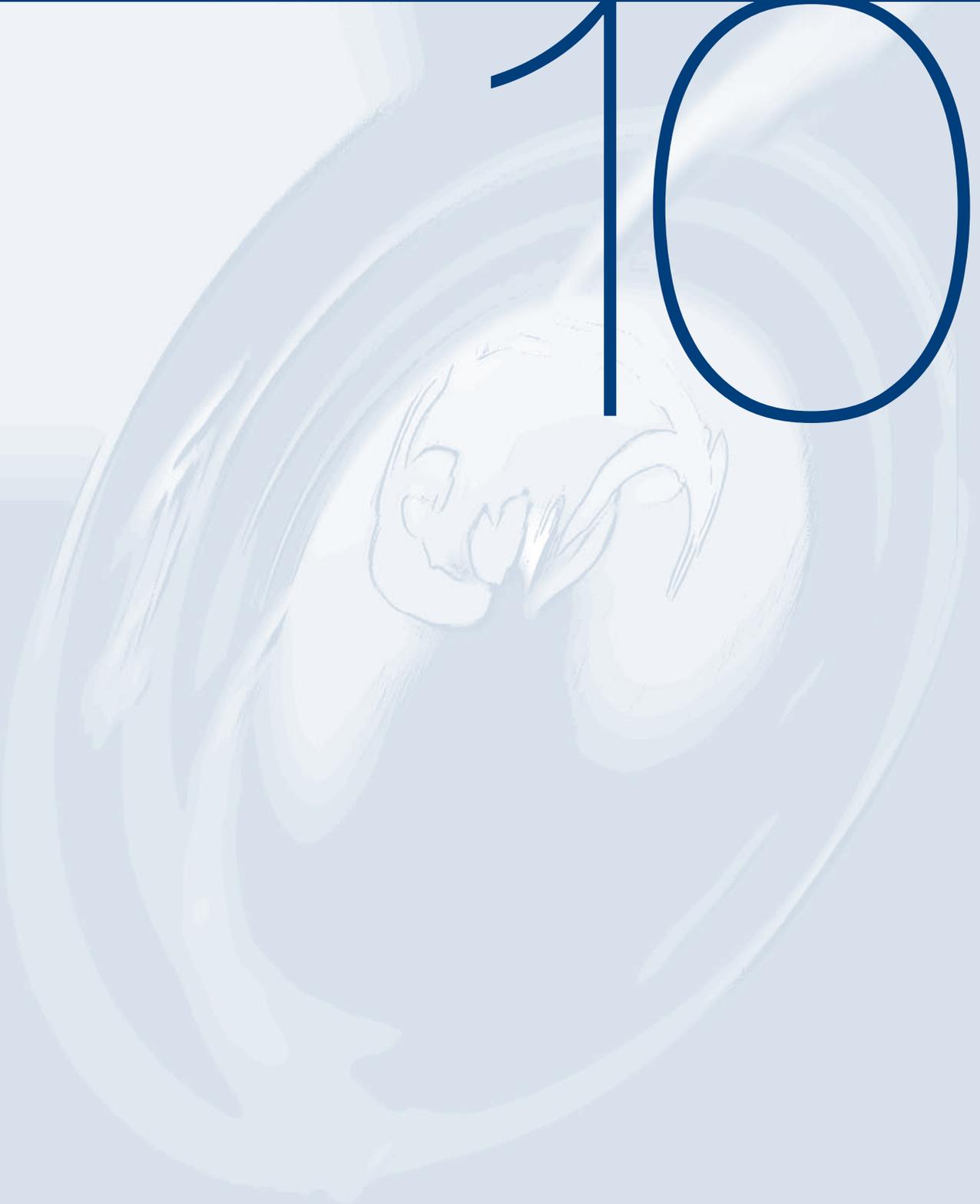
Almost one-half of business trips abroad were to Brussels, where the Office's delegates participated in the deliberations held by the CEER and ERGEG working groups and task forces.

The Office's representatives also attended important international conferences abroad. For example, a conference in Madrid organised by International Feed-In Cooperation can be regarded as very beneficial; it concerned support for electricity generation from renewable resources in Europe and provided a forum for exchange of experiences from the perspective of the updating of the technical and economic data on renewable resources.

Equally beneficial was the third World Forum on Energy Regulation in Washington, D.C. The conference was an important event in the world of regulators and the Office's participation in the conference helped it to hear about the current developments on the natural gas and electricity markets in both EU and non-EU member states. Among the key topics were the financing of energy projects and the regulatory environment, the regulator's role in gas and electricity supply security, market liberalisation and benchmarking regulatory methods.

The Office's new employees had an opportunity to broaden their knowledge and experience at a technical workshop organised by the Florence School of Regulation. The workshop dealt with the basic theoretical principles of regulation and licensing in the energy sector, and offered case studies and practical examples. The course was dedicated to the basic theoretical principles in various regulation areas and licensing in the energy sector, and case studies and practical examples through which the degree to which the energy market had been opened in the EU member states was presented to the course participants.

10



10.1 Personnel management agenda

In the area of personnel and organisation the Office focused on the following tasks in 2006:

Personnel agenda – Achieving the required number of qualified employees to provide for all of the Office's activities in all sections; ensuring their further professional development and providing them with the required and adequate social environment and facilities for their work. During the year mostly university graduates filled vacancies on the basis of competitions;

Education – Education was governed by two documents adopted by the Office at the beginning of 2006: the rules for training ERO employees, and the ERO plan of training and education. Both documents are based on Czech Government Resolution No. 1542/2005 of 30 November 2005 on the rules of administrative authority staff training.

10.2 Education and training

Initial training

a) Introductory initial training

All employees took this course during the three-month trial period after joining the Office. Examination of the knowledge of the regulations required for carrying out technical activities and their practical application during the trial period is a part of performance assessment by managers at the end of the three months.

b) Continued initial training

The new employees study the structure of state administration and government finance, Czech law, basic regulations of the labour law, code of conduct for civil servants, and also the rules of administrative procedure. Environmental studies and EU affairs are also included in this training.

In view of the new Act No. 500/2004, Administration Code [rules of administrative procedure], training courses were organised for all employees who participate in administrative proceedings or contribute to their preparations.

Special training was provided in the form of e-learning combined with two six-hour tutorials. A test helped to examine the knowledge of the rules of administrative procedure acquired by course participants. A total of 17 employees attended the course, which is accredited by the Ministry of Education, Youth and Sports of the Czech Republic.

Advanced training

a) Advanced management training

Focused on acquiring and deepening certain knowledge and skills required in managerial positions.

Managers took courses in time management, performance motivation, delegation of powers, assessment, effective negotiation, assertion of authority, task solving and group communication. The modern concept of instruction had the form of training courses and team-building activities.

b) Language training

Based on Czech Government Resolution No. 1542/2005 on the rules of administrative authority staff training, it involved sitting standardised language examinations.

As at 31 December 2006 the qualification requirement of the command of a foreign language was met by 71.4 per cent of the employees (up by 5.4 per cent in comparison with 2005). Language training takes place in accordance with the approved principles and the Office's relevant internal regulation that provides for this area of education in detail.

The ERO Chairman specified a group of official posts for which the command of a selected foreign language is a prerequisite; see Table 13.

Table 13 Employees' command of languages

Language	Number of selected posts subject to the qualification requirement of a standardised language examination, in the order of proficiency				Total number of requirements set for posts
	1st level	2nd level	3rd level	4th level	
English	25	22			47
French	3				3
German	5	1			6
Total	33	23			56

c) Other advanced training covered the following:

- Instruction and training in teamwork and communication as support for the implementation of the Office's information system;
- Ongoing training in the updating of legislation as a prerequisite for the employees' technical activities, and in IT user skills;
- Participation in technical seminars, workshops and conference on the technical issues of energy regulation;
- A course on Act No. 500/2004;
- Filing and archiving service in the AXAPTA IS;
- A course on Act No. 262/2006, the Labour Code, and the related regulations;
- Training of drivers of the Office's cars, and training in health and safety at work.

Altogether 101 training events were held, i.e., specialist courses, seminars and conferences. In the system of training important positions were held by the technical courses on Act No. 500/2004 and the filing service in the AXAPTA IS and the related preparations for adopting new filing and safe destruction rules, and, at the end of the year, a course on the new Labour Code and related regulations. A total of 116 employees attended these events.

Education and training expenses totalled CZK 1,793,670, accounting for 4.73 per cent of the actual payroll costs.

The structure of the outlays on education, training and professional development can be seen in Table 14.

Table 14 Structure of training expenses

Type	Language training [CZK '000]	Other training [CZK '000]	Total [CZK '000]
Amount	913.96	879.71	1,793.67

In 2006 thirty-five employees attended 13 foreign and 22 domestic conferences and seminars dedicated to regulation in the energy sector, licensing issues and trading on the energy market.

Internal regulations – organisational standards are documents required for supporting the Office's mission and business and all of its agendas. In 2006 organisational activities focused on the innovation of internal regulations as new laws and Government Orders entered into force. In 2006 the Office issued 26 internal regulations, i.e. 6 decisions, 17 measures of the ERO Chairman, and 3 methodological guidelines.

The 'mandatory target' of salaries and other payments for work was met at a level of 89.93 per cent, CZK 38,465,740, of which the mandatory target of employees' salaries was met at 91.14 per cent, CZK 37,953,450.

In 2006 the actual average number (FTE) of the Office's employees was 93, and the planned number was 102; the annual index was 103.33 per cent (i.e. plus three employees). The Office therefore did not manage to have the planned staffing level of 102, which means meeting the plan at 91.18 per cent. As at 31 December 2006 the Office had 98 employees, i.e. six more than as at 31 December 2005.

The staffing level was increased on an ongoing basis, and the need for employees in terms of their number and qualifications in the various organisational units and under the Chairman's decisions in this area was met.

Table 15 Incoming and outgoing employees in 2006

	New staff	Leaving staff
Number	14	8

Of the overall number of 98 employees, 59 worked in Jihlava and 39 in Prague; these are actual numbers as at 31 December 2006.

The structure of workforce is described in detail from several aspects in Tables 16 and 17.

Table 16 Employee structure by age and sex as at 31 December 2006

Age	Men	Women	Total	Per cent of total [%]
Up to 20 years	0	0	0	0
21 to 30	20	6	26	27
31 to 40	10	12	22	22
41 to 50	14	15	29	30
51 to 60	12	5	17	17
61 years and older	4	0	4	4
Total	60	38	98	100
Percentage [%]	61	39	100	

Table 17 Employee structure by education and sex as at 31 December 2006

Education	Men	Women	Total	Per cent of total [%]
Elementary	0	0	0	0
Vocational	2	0	2	2
Secondary vocational	0	1	1	1
Complete secondary	0	0	0	0
Complete secondary vocational	8	19	27	28
College	0	0	0	0
University	51	17	68	69
Total	61	37	98	100

The single largest number of employees falls within the 41 to 50 years age brackets, while those aged 21 to 30 years form the second largest group. The employee structure by age is favourable, i.e. a prevailing trend can be observed in the recruitment of young employees, mostly with tertiary education. In comparison with 2005 the 21 to 30 years age brackets were stronger, by three per cent, while the number of staff in the 61 years and over category dropped by 2.4 per cent.

In 2006 the category of employees with tertiary education increased by 3.1 per cent to 69 per cent. The predominance of staff with tertiary education corresponds to the structure of salary categories and the challenging nature of the Office's work. This favourable trend is expected to continue in 2007.

The distribution of the duration of employment, shown in Table 18, reflects the time for which the Office has been in existence. The Office was established on 1 January 2001.

Table 18 Duration of employment as at 31 December 2006

Employment	Number	Share of total staff [%]
Up to 5 years	58	59
Up to 10 years	40	41
Total	98	100





11.1 The Chapter's budget

The budget for Chapter 349 – The Energy Regulatory Office, was approved in Act No. 543/2005 on the Czech Republic's National Budget for 2006, passed by Czech Parliament's House of Deputies in its Resolution No. 2016 on the Government's bill on the national budget of the Czech Republic for 2006 of 2 December 2005.

The budget was approved at CZK 113,919,000. This budget was later adjusted through a budgetary measure in co-operation with the Ministry of Finance (MF) and the Ministry of Informatics (MI). In respect of the 'mandatory target' expenses, the budget was reduced by **CZK 1,067,000**. It was a budgetary measure intended to correlate Chapter 349 ERO with Chapter 338 MI. Through this budgetary measure MI's budget was increased to finance the new data services MI is providing to meet the Office's needs. The funds for this budgetary measure were found inside the Chapter's approved budget through savings in certain other expenditure items.

After the budgetary measure the budget totalled CZK 112,852,000.

A staffing level of 102 was approved for 2006.

No income was planned for the Chapter.

11.2 Revenues to the Chapter

No targets were planned or set on the income side. The revenues to the Chapter are listed in Table 19.

Table 19 Revenues to the Chapter

Budget item	Type of revenue	Budget [CZK '000]	Actual [CZK '000]
	Total non-tax revenues, capital revenues, and subsidies	0.00	338.15
	of which:		
2111	income from services		0.02
2141	interest accrued on accounts – Reserve Fund, FKSP, deposit account		3.02
2322	insurance compensation received		184.10
2324	damages received from employees		103.91
2329	overpayment credit notes (printer's services cancelled)		6.26
3113	proceeds from sale of assets		8.00
4132	transfer of undrawn funds for wages, including insurance for 12/2005, from the deposit account		32.84

These funds on the income side were transferred to the national budget through the Chapter's income account. They are one-off, non-recurring revenues to the Chapter.

11.3 Meeting the mandatory targets

The Office complied with all the mandatory targets. The planned amount of funds was not exceeded under any of the mandatory targets, see Table 20.

Table 20 Meeting of the mandatory targets

Mandatory targets	Approved budget [CZK '000]	Budget after changes [CZK '000]	Actual [CZK '000]	Actual/ budgeted [3/2] [%]
	1	2	3	
Aggregate targets				
Total income			338.15	
Total expenditure	113,919.00	112,852.00	98,556.37	87.33
Standard targets				
Salaries for employees and other payments for work	42,772.00	42,772.00	38,465.74	89.83
of which: Salaries for employees	41,645.00	41,645.00	37,953.45	91.14
Statutory insurance premiums paid by the employer	14,970.00	14,970.00	13,294.19	88.81
Allocation to the Fund of Cultural and Social Needs (FKSP)	833.00	833.00	763,58.00	91.67
Salaries to employees and other payments for work in state administration	42,772.00	42,772.00	38,465.74	89.93
of which: Salaries to employees in state administration	41,645.00	41,645.00	37,953.45	91.14
Specific targets – income				
Non-tax revenues, capital revenues and subsidies received			338.15	
Specific targets – expenditure				
Outlays to support the ERO's tasks	113,919.00	112,852.00	98,556.37	87.33
Transfer of undrawn funds to the reserve fund Organisational Component [Instrumentality] of the State as at k 31 December 2006				

Average salaries of CZK 34,024 were planned for 2006. The actually achieved average salary was CZK 34,008, index 99.95 per cent. The 2006/2005 index of actually achieved average salaries was 104.27 per cent. In 2006 the average salary under tariffs, including reimbursements, amounted to CZK 21,065, the average salary including personal performance supplements and management allowances, without bonuses, was CZK 28,495.

As regards expenses on other payments for work (item 502) the budgeted costs were not exceeded and the draw down was 45.46 per cent, CZK 512,290.

The above amount can be broken down as follows:

- Work related to the preparation of regulatory statutory instruments, forms, expert calculations and consultations 80,000
- Activities related to the remonstrance commission and expert services 208,240
- Other work 107,080
- Cleaning work 39,750
- Severance 40,150
- Undrawn funds in the deposit account (i.e. income in 2007) 37,070

11.4 Cash Funds

Fund of Cultural and Social Needs

During 2006 the Fund of Cultural and Social Needs (FKSP) was accumulated and drawn down in line with the internal regulations. The principles of drawing down and using funds from FKSP are provided for in the Office's internal directives in compliance with the legislation on this area of financial management. As at 31 December 2006 the funds in the Office's FKSP account amounted to CZK 297,500.

Reserve Fund

Under Section 47 of Act No. 218/2000 on budgetary rules and changes to certain related laws ("the budgetary rules"), as amended, undrawn budgetary funds were transferred to the Reserve Fund in the previous years. Under Section 48 they will be used to support expenditure in the years to come. From January to December 2006 no drawdowns or allocations were made. The Reserve Fund balance as at 31 December 2006 was therefore at the same level as at the beginning of 2006 in accordance with Government Resolution No. 1090 of 25 September 2006 on the bill on the national budget of the Czech Republic for 2007 and on proposals for the medium-term outlook of the national budget of the Czech Republic for 2008 and 2009 and medium-term expenditure frameworks for 2008 and 2009, and with Government Resolution No. 1262 of 1 November 2006 that changed Government Resolution No. 1090 of 25 September 2006.

As at 31 December 2006 the funds in the Office's Reserve Fund totalled CZK 34,594,550.

There were no individual subsidies, or expenditure reviewed on a case-by-case basis, in the budget.

Table 21 Funds transferred to the Reserve Fund and their use

Item	Amount [CZK '000]
Balance of undrawn funds transferred to RF under Section 47 as at 1/1/06	34,594.55
of which: included in income in 2006	0.00
used in 2006	0.00
Transfer of funds under Section 47 for 2006	0.00
Balance of undrawn funds transferred to RF under Section 47 as at 31/12/06	34,594.55
of which: national budget funds allocated to finance programmes	3,039.04
other	31,555.51

11.5 The Energy Regulation Fund

In accordance with the Energy Act the Office held the ERF funds in a separate current account kept with the Czech National Bank, account number 3029001/0710.

As at 1 January 2006 the opening balance in the ERF stood at CZK 50,235,240. No significant payments or other financial operations took place from/in the ERF during 2006 (only one payment was made). After adding the interest (see the Energy Act and the new rules for the ERF put in place in 2005), the closing balance in the ERF was CZK 50,449,810 as at 31 December 2006.

Under Section 14, subsection 10 of the Energy Act, the Energy Regulatory Office is obliged to present an audit of the Fund for the respective calendar year. In compliance with these provisions an audit was performed in keeping with the guidelines issued by the Chamber of Auditors of the Czech Republic. According to the auditor's report the ERF books were kept in accordance with the legal regulations in force and present fairly the ERF's financial position for the fiscal year 2006 (Appendix 2).

11.6 Administrative fees and fines

In addition to the income mentioned in the foregoing, the Office also collected CZK 8,541,540 through its administrative fee account no. 3711-2421001/0710 for January to December 2006. These are administrative fees collected by the Office from businesses in connection with licensing under Act No. 458/2000, the Energy Act, and Act No. 634/2004 on Administrative Fees. This income is not a part of the Chapter's income. It is therefore not included in the reports and statements on the management of the Chapter's funds.

The Office also imposed, by its four decisions of 26 May 2006, administrative fines on gas companies, totalling CZK 14,692,420 (revenues to the national budget, account no. 3754-2421001/0710). Since remonstrances were filed and the decisions did not become final, the administrative proceedings continued in the second half of 2006. The decisions became final on 7 September 2006. On 30 September 2006 the following amounts were received:

CZK 8,569,390 from Severomoravská plynárenská, a.s., and

CZK 3,557,760 from Východočeská plynárenská, a.s.

The remaining amounts, CZK 1,409,930 from RWE Transgas, a.s. and CZK 1,155,340 from Středočeská plynárenská, a.s. were paid, upon the ERO's reminders, on 9 October 2006 and 12 October 2006, respectively. This income is not a part of the Chapter's income. It is therefore not included in the reports and statements on the management of the Chapter's funds.

11.7 Budget management results

The total actual drawdown on the budget, including transfers to the Reserve Fund, can be seen in Table 22.

Table 22 Total actual drawdown on the budget

Drawdown on budget	Expenditure [CZK '000]	Percentage drawn [%]
Total expenditure	98,556.37	87.33
of which:		
capital expenditure drawn	9,259.25	67.37
current expenditure drawn	89,297.12	90.10

Performance vs. budget for January to December 2006 and total savings on the expenditure side of CZK 14,295,630 are mainly attributable to moving the drawing of the funds for programme financing to 2007 (about CZK 5,736,000), savings of funds intended for payroll costs due to the lower than planned staffing level (about CZK 6,051,000) and savings of other current expenditure (about CZK 2,509,000). The drawdown on the expenditure items in 2006 is summarised in Appendix 1, Expenditure from the National Budget.

11.7.1 Operating expenditure savings

Significant operating expenditure savings were achieved, see Table 23.

Table 23 Operating expenditure savings

Item number	Description	Amount [CZK '000]
	Total operating expenditure savings	14,295.63
	of which:	
501	Salaries to employees	3,691.55
502	Other payments for work	614.71
503	Statutory premiums paid by the employer	1,675.81
513	Purchase of materials	390.04
515	Purchase of water, fuels and energy	295.85
516	Purchase of services	1,801.43
517	Other procurement	1,187.46
534	Transfers to internal funds	69.42
611	Procurement of intangible fixed assets	3,732.27
612	Procurement of tangible fixed assets	752.48
	Other items of the budget	84.61

11.7.2 Programme financing

In 2006 the Office continued to finance its projects in keeping with the approved programme financing documentation, which had been prepared in detail for 2003 to 2007.

In line with the Office's priorities the largest amount of funds was earmarked for IT. To finance the supply of the new information system the Office had sufficient funds to finance the project without any problems.

Financial management results in 2006, from the perspective of the sub-programmes and current and capital expenditure, are shown in Tables 24 and 25, respectively. During the year minor changes were made to the budget to reflect current developments and the Office's new needs.

Table 24 Results by the sub-programmes

	Plan [CZK '000]	Actual [CZK '000]	Percentage [%]
Total, Programme No. 249 010	21,741.00	16,005.64	73.62
of which:			
Sub-programme 249 011 – ICT	19,011.00	13,991.72	73.60
Sub-programme 249 012	2,730.00	2,013.92	73.77

Table 25 Results by current and capital expenditure

	Plan [CZK '000]	Actual [CZK '000]	Percentage [%]
Total programme financing	21,741.00	16,005.64	73.62
of which:			
Current expenditure	7,997.00	6,746.39	84.36
Capital expenditure	13,744.00	9,259.25	67.37

The mandatory target was not exceeded. The basic needs and the running of the Office were met and provided for, and the preconditions for its further development were created.

In 2006 intensive work continued to build a new comprehensive information system, which was one of the Office's priorities. The original specifications of the system were expanded to reflect the development of the situation, the complexity of the jobs to be run, and the Office's new needs. The scope of supply was extended to include new modules; an addendum to the original agreement was therefore signed. This caused the postponement of some delivery milestones to 2007. The Office expects to have all deliveries completed in the first half of 2007. The cost of this supply amounts to about CZK 4,460,000, and this amount is provided for in the relevant part of the budget of the ISPROFIN programme financing for 2007.

11.7.3 Outlays on business trips abroad

Outlays on business trips abroad totalled CZK 3,407,580 and are shown in Table 26.

Table 26 Outlays on business trips abroad

Item number	Description	Amount [CZK '000]
	Total outlays on business trips abroad	3,407.58
	of which:	
5136	Books, teaching aids, printing	0.29
5163	Financial services (insurance)	0.20
5167	Education and training services (technical training, language courses)	34.00
5169	Purchase of other services	2.18
5173	Travel expenses (subsistence, pocket money, air fare, accommodation)	3,061.78
5176	Conference registration fees	295.33
5179	Other purchases (visas)	13.80

In comparison with the previous year there was a significant drop in cost item 5167 – education and training services, and cost item 5176 – conference registration fees. Compared with 2005 overall outlays on foreign business trips were CZK 669,940 lower.

In the area of 'non-investment transfers to international organisations', item 5511, the actual expenditure reported at CZK 832,790 relates to the annual membership dues to CEER, Brussels, for 2006 – see Government Resolution No. 781 of 17 August 2004 on the payment of the membership dues to the Council of European Energy Regulators (CEER) from 2004.

Since the total annual membership dues for 2006, amounting to EUR 28,926, exceeded the EUR 24,624 that had been approved by the Government earlier (by EUR 4,302), the Office draw up a new paper for the Government, requesting an increase in the volume of contributions to international organisations.

In its Resolution No. 996 of 23 August 2006, on the payment of the annual membership dues to CEER in 2006 to 2008, the Government approved the new amount of the contributions for both 2006 and the following period of 2007 and 2008.

The Office then carried out the relevant budgetary measure in the respective expenditure item within the approved budget, without requiring any increase in the Chapter's budget.

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12.1 External inspections

In 2006 no external inspection was carried out.

12.2 Internal audit

The requirement for the internal audit department's functional independence was fully provided for in the ERO's Rules of Organisation in 2002.

The annual plan of audit actions is compiled in relation to the medium-term internal audit plan and risk analysis under the ISMS (information security management system) in line with internationally recognised standards and the recommendations for practice included in the guidelines of the Czech Institute of Internal Auditors.

In accordance with the internal audit plan, 2006 saw twelve audit actions as follows:

- Audit of incoming invoices, relation to accounting documents, keeping due dates
- Audit of the process of permitting different calculation of heat prices – internal rules
- Audit of the completeness of documentation for public contracts
- Audit of the security policy, completeness of documentation on facilities, risk places
- Audit of correlation between meal voucher issue, records of attendance and records of business trips
- Audit and analysis of the use of the "financial stability control" project
- Audit of agreement between the content of contracts and service purchase orders with the content of ERO units' work,
- Audit of compliance with the Administrative Code in handling licence applications
- Audit of the authorisation of contracting parties' representatives, as contained in the contracts in place
- Audit of the completeness of accounting documents and business trip reports in the file of business trips abroad
- Audit of the use of external services to achieve cost savings in business trips abroad
- Audit of the completeness of IT records at the ERO (software, hardware)

During the year internal audit also carried out the relevant provisions on management inspections, checked the meeting of the education and training plan and prepared the report on the results of financial audits.

The reports on the audits carried out, and the recommendations following from them, were discussed with the responsible managers. The audit team discussed a total of 35 audit recommendations with managers. Thirty of them were accepted for implementation. Managers' approach can be viewed as accommodating and businesslike. For each of the audits the ERO Chairman approved the final results and the recommendation adopted. The efficacy of the adopted recommendations is verified during the monitoring carried out as part of the planned new audits.

Another component of the internal audit system is the management inspections (*ex ante*, ongoing, *ex post*) carried out by managerial personnel under their powers and responsibilities. The shortcomings identified were remedied on an ongoing basis. ERO managers consistently develop and fine-tune the system of financial control in their subordinated sections and departments. The Office's management meetings regularly discuss the following topics: budgeting, performance vs. budget in each quarter, economy of business trips abroad, adequacy, necessity and efficiency of co-operation with external consultancies, structure and gravity of complaints, use of business cars, etc. The principles of *ex ante*, ongoing and *ex post* management inspections are provided for in internal organisational and control standards (Rules of Organisation, Signature Authority Rules, Directive on Accounting Document Circulation).

The main purpose of both components of the internal audit system is to prevent potential damage and unfavourable development of risks. The Office therefore continues to standardise all work procedures under the relevant standards and regulations, using a precisely defined organisational structure.

The report on the results of financial audits and reviews in 2006 was prepared and sent to the Ministry of Finance in the electronic form in January 2007 in keeping with the relevant law on financial control and the respective implementing regulation.



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Expenditure from the National Budget

Period: January to December 2006

Chapter: 349, the Energy Regulatory Office

in CZK'000

Expenditure item	Description	2006 budget		2006 actual	% drawn (3:2)
		approved	after changes		
		1	2	3	4
501	Wages and salaries	41,645	41,645	37,953.45	91.14
502	Other payments for work	1,127	1,127	512.29	45.46
503	Statutory insurance premiums paid by the employer	14,970	14,970	13,294.19	88.81
513	Purchase of materials	3,425	3,535	3,144.96	88.97
514	Interest paid and other financial costs	60	60	26.55	44.25
515	Purchase of water, fuels and energy	1,610	1,710	1,414.15	82.70
516	Purchase of services	26,944	25,684	23,882.57	92.99
	of which:				
	5164 rental	2,400	2,700	2,377.52	88.06
	5166 consulting, advisory and legal services	10,600	10,850	10,543.91	97.18
	5167 education and training services	4,450	2,300	1,793.67	77.99
	5169 purchase of other services	6,300	7,250	7,006.98	96.65
517	Purchase of services	8,711	8,644	7,456.54	86.26
	of which:				
	5171 repairs and maintenance	2,350	3,400	3,145.69	92.52
	5172 software	400	250	116.23	46.49
	5173 travel expenses (domestic and abroad)	4,114	4,114	3,554.98	86.41
518	Advances, sureties, guarantees and government loans provided				
519	Costs of non-investment purchases, contributions, etc.	10	10		
534	Transfers to internal funds	833	833	763.58	91.67
	of which:				
	5342 non-investment transfers to FKSP	833	833	763.58	91.67
	5346 transfers to funds of the State's agencies				
536	Other non-investment transfers to other public budgets	30	30	7.65	25.50
542	Compensations paid to citizens	10	10	8.40	84.00
551	Non-investment transfers to international organisation and multinational bodies	800	850	832.79	97.98
5	Total current expenditure	100,175	99,108	89,297.12	90.10
611	Intangible fixed assets purchased	8,468	7,568	3,835.73	50.68
612	Tangible fixed assets purchased	5,276	6,176	5,423.52	87.82
636	Investment transfers				
	of which:				
	6361 investment transfers to the Reserve Fund				
6	Capital expenditure	13,744	13,744	9,259.25	67.37
0	Total	113,919	112,852	98,556.37	87.33



Auditor's Report

On the audit of a fund established under Section 14 of Act No. 458/2000 on the Conditions of Business and State Administration in the Energy Industries and Changes to Certain Laws (hereinafter referred to as "the Energy Act"), as amended.

Recipient of the Report: Management of the Energy Regulatory Office

Name of the accounting unit: Energy Regulatory Office

Registered office: Masarykovo náměstí 5, 586 01 Jihlava

Reg. No. 70894451

Period under review: 2006

The auditor's opinion intended for the institutor of the Energy Regulatory Office

I have audited the fund set up pursuant to Section 14 of Act No. 458/2000 on the Conditions of Business and State Administration in the Energy Industries and Changes to Certain Laws (hereinafter referred to as "the Energy Act"), as amended, in relation to the annual financial statements. The audit was performed in accordance with the International Accounting Standards and covered the period of 2006.

The statutory body of the accounting unit is responsible for bookkeeping and for complete, true and correct accounting. The auditor's responsibility is to obtain all information required for examining the way in which the fund is maintained and relates to the annual financial statements. The audit has been carried out with regard to the extent of the accounting, by examining all evidence supporting the amounts and disclosures while respecting the significance of all disclosures.

In my opinion the fund was maintained in accordance with the legal regulations in force, and is truly and fairly reflected in the annual financial statements of the Energy Regulatory Office for the accounting period of 2006.

A-CONT, s.r.o., represented by its Managing Director

Ing. Jiří Makaj
Auditor, Licence No. 152




Encl.: Balance Sheet,
breakdowns of the balances
in the Fund

At Jihlava, on 29 January 2007



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