



**Assessment of the Resolution of the Cabinet of Ministers of Ukraine of May 30, 2023 No 544 "On amendments to the resolution of the Cabinet of Ministers of Ukraine of June 5, 2019 No. 483"**

**by the Energy Community Secretariat**

**December, 2023**

## PURPOSE STATEMENT

Assessment of the amendments, adopted by the Resolutions of Cabinet of Ministers of Ukraine No 544 of 30 May 2023 to the Resolution of the Cabinet of Ministers of Ukraine No. 483 of 5 June 2019 “On the approval of the Regulation on the imposition of special obligations on the electricity market participants to ensure the general public interests in the process of functioning of the electricity market” as regards the new electricity prices for households.

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## Ukraine Energy Market Observatory

Assessment 20/23

### **Assessment of the Resolution of the Cabinet of Ministers of Ukraine of May 30, 2023 No 544 “On amendments to the resolution of the Cabinet of Ministers of Ukraine of June 5, 2019 No. 483”**

## Introduction

The Resolution of the Cabinet of Ministers of Ukraine (hereinafter, CMU) No 483 of 5 June 2019 “On the approval of the Regulation on the imposition of special obligations on the electricity market participants to ensure the general public interests in the process of functioning of the electricity market” (hereinafter, the PSO Act)<sup>1</sup> has been in force since the very beginning of the operation of new electricity market model (launched on 1<sup>st</sup> July 2019) imposing public service obligations (hereinafter, PSO) on the electricity market participants in terms of ensuring the affordability of electricity for household consumers based on the Article 62 of the Law of Ukraine “On Electricity Market” (hereinafter, Electricity Market Law)<sup>2</sup>. The PSO Act continued the practice of household price regulation and fixed electricity prices for households already under the legal framework of the new electricity market.

On 22 March 2023, the Energy Community Secretariat (hereinafter, the Secretariat) was notified by the National Energy and Utilities Regulatory Commission (hereinafter, NEURC) about the draft amendments to the PSO Act initiated by the Ministry of Energy. The amendments proposed to extend the validity of the PSO Act in force for one month, until 30 April 2023, without amending its substance and were approved by the CMU Resolution No. 262 of 24 March 2023<sup>3</sup> in order to address the social protection of households from increase of electricity prices in the martial law conditions in Ukraine and for the duration of the autumn-winter period of 2022/2023. Later, on 25 April 2023, the CMU took a new decision to prolong the PSO Act<sup>4</sup> for one month more (till 31 May 2023). None of the decisions was notified and consulted with the Secretariat as required by the Energy Community acquis (Article 3 of Directive 2009/72/EC) and Article 62 of the Electricity Market Law.

By letter of 9 May 2023 (hereinafter, NEURC Letter) NEURC submitted to the Secretariat the proposals to the PSO Act that stipulate introduction of the first stage of adjustment of electricity prices for households via application of a single price, undifferentiated by consumption volumes, starting from 1 June 2023 at the level of 2.88 UAH/kWh (with VAT) in order to address: a) unbalanced PSO model resulting from low electricity prices for household consumers leading to constant accrual of debt by electricity market participants; b) expiration of current PSO by 1 June 2023; c) household tariffs covering only 25% of costs of electricity

<sup>1</sup> <https://zakon.rada.gov.ua/laws/show/483-2019-%D0%BF#Text>

<sup>2</sup> <https://zakon.rada.gov.ua/laws/show/2019-19#Text>. While the Electricity Market Law does not directly designate PSO for HH prices in a list of PSOs on electricity market, the law designates criteria under which the CMU can introduce PSO additional to those listed in the law. Under such criteria HH PSO by the CMU has been designed and implemented

<sup>3</sup> <https://zakon.rada.gov.ua/laws/show/262-2023-%D0%BF#n2>

<sup>4</sup> CMU Resolution of 25.04.2023 No. 384

production, transportation and taxation. Later, by letter of 11 May 2023, as an alternative, NEURC proposed to retain current household electricity prices, but provide a compensation to electricity producers for PSO functioning from the State Budget of Ukraine in the amount of UAH 34 billion (excluding VAT).

The Secretariat in its letter of 12 May 2023 supported the first proposal of NEURC as an appropriate and overdue first step towards cost-reflectivity of end-user prices. Also, the Secretariat encouraged NEURC to follow up with developing a pathway for bringing household prices to cost reflective levels and to develop clear vulnerability criteria for the consumers affected.

On 30 May 2023, the CMU adopted amendments<sup>5</sup> to the PSO Act based on which the fixed electricity price for households was increased to 2.64 UAH/kWh (including VAT) as of 1 June 2023.

## Background

### a) Legal framework governing household electricity prices

According to Article 72 of the Electricity Market Law the supply of electricity to consumers is carried out at free prices by any supplier of their choice and households and small non-household consumers may be supplied also by universal service suppliers (hereinafter, USS). Article 63 of the Electricity Market Law provides that the universal services shall be provided at economically justified, transparent and non-discriminatory prices, which are formed in accordance with the Procedure for the formation of prices for universal services<sup>6</sup>, approved by NEURC, and include, in particular, the price of purchasing electricity on the electricity market, the price for the services of the USS, prices (tariffs) for the services of the transmission system operator (hereinafter, TSO) and the distribution system operator (hereinafter, DSO).

At the same time, Article 62 of the Electricity Market Law empowers the CMU to impose PSO on market participants (except consumers) for a specified period of time. Proposals regarding the scope and conditions of PSO are prepared by the NEURC and are submitted to the CMU for adoption after consultations with the Secretariat.

The PSO Act determines the general public interest as ensuring the affordability of electricity for household consumers and sets the fixed electricity prices for HHs together with the conditions as regards prices and volumes of electricity to be sold (bought) by dedicated market participants as well as the level of financial payments (for provision of services) to compensate for electricity supply to households. The key provisions of the PSO mechanism are summarized in the Annex.

The PSO Act imposes special obligations as regards the household prices on state-owned electricity producers (State Enterprise “National Atomic Energy Generating Company “Energoatom” (Energoatom) and PrJSC “Ukrhydroenergo”), USSs and guaranteed buyer (hereinafter, GB). Under the PSO Act, individual households, collective households, dormitories, multistore buildings (for technical needs) and others equal to household categories of consumers are benefiting from fixed prices under the PSO (the full list of categories is provided in the Annex).

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<sup>5</sup> CMU Resolution No.544 of 30.05.2023

<sup>6</sup> NEURC Resolution No.1177 of 05.10.2018

Since the adoption and amendments of the PSO Act the Secretariat constantly repeated<sup>7</sup> the call for cost-reflectivity in household electricity prices. Without taking the Secretariat's opinion<sup>8</sup> into account, the PSO Act has been amended by adoption of CMU Resolution No. 1206 of 28 October 2022. The draft decisions of March and April 2023 on PSO Act prolongation were also not consulted with the Secretariat as it is required by Article 62 of the Electricity Market Law.

Under the current war conditions due to the Russian aggression the issue of household energy and utilities prices has become even more sensitive. CMU<sup>9</sup> and the Verkhovna Rada<sup>10</sup> took decisions prohibiting the increase of tariffs/prices<sup>11</sup> during the applicability of the martial law and six months after its end; there are also proposals to establish a moratorium on increase of household utilities tariffs<sup>12</sup> including household electricity price.

#### b) Household electricity prices in Ukraine

The level of end-user prices for households in Ukraine has been gradually increasing for already ten years, with the recorded increase of 25% in the period 2017-2021, however they still have not reached a cost-reflective level. Moreover, after a slight increase since 2021 for some categories of households, electricity prices even decreased<sup>13</sup>. The Table 1 in the Annex summarizes the development of household electricity prices in Ukraine in the period 2017 to 2023.

Until the increase of 1 June 2023, the Ukrainian households paid almost five times less than the households in the EU on average and two thirds of the average household prices in other Energy Community Contracting Parties (Fig.1).<sup>14</sup>

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<sup>7</sup> Assessment of draft proposal for imposing public service obligation(s) for ensuring availability of electricity to household customers in Ukraine, 30.04.2019 (on the very first draft), COMPLIANCE NOTE by the Energy Community Secretariat Ukraine – electricity Public Service Obligations Act 2020 (CN 03/2020 / 28 May 2020), Secretariat Assessment of the draft received from the NEURC for the PSO Act related to supply of electricity to household customers proposed by the Ministry of Energy on 12.07.2021, etc.)

<sup>8</sup> The letter of the Secretariat dated 28 October 2022

<sup>9</sup> CMU Resolution No. 502 of 29.04.2022 “Some issues of regulation of activities in the field of communal services in connection with the introduction of martial law in Ukraine” where CMU recommended to the authorities setting tariffs not to increase tariffs (e.g. for heat energy and hot water supply, centralized water supply and of centralized water drainage) for HHs and apply them as of February 24, 2022

<sup>10</sup> Law No. 2479-IX “On the Peculiarities of Regulation of Relations in the Natural Gas Market and in the Field of Heat Supply During the Effect of Martial Law and the Further Restoration of Their Functioning”

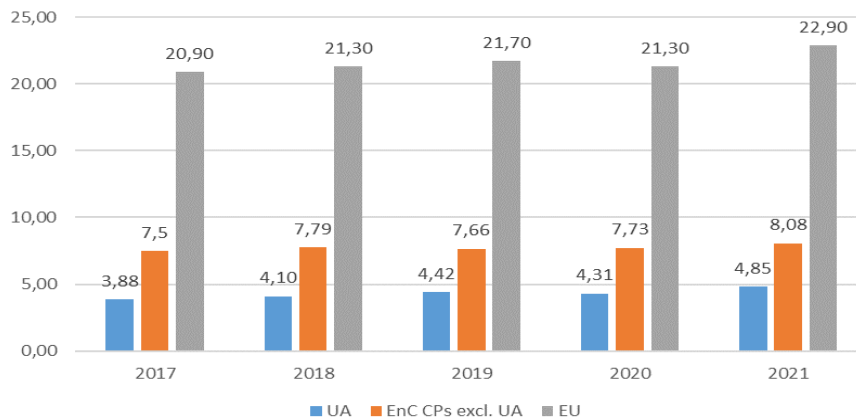
<sup>11</sup> In particular as regards tariffs for natural gas distribution services, thermal energy (its production, transportation and supply) and services for the supply of thermal energy and hot water supply

<sup>12</sup> <https://itd.rada.gov.ua/billInfo/Bills/Card/41527>

<sup>13</sup> Resolution of the CMU of 11.08.2021, No. 859

<sup>14</sup> [https://www.energy-community.org/dam/jcr:1be3ccce-7262-45c5-b17c-a9c020c0b651/ECRB\\_RetailMMR2021\\_approved.pdf](https://www.energy-community.org/dam/jcr:1be3ccce-7262-45c5-b17c-a9c020c0b651/ECRB_RetailMMR2021_approved.pdf)

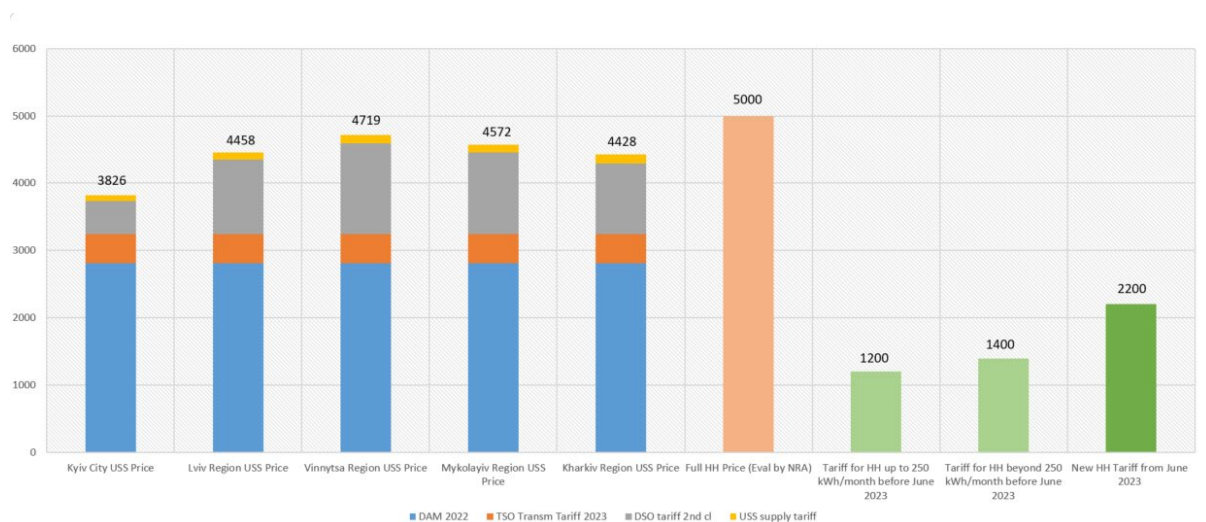
Fig 1. Final electricity prices in nominal terms for household consumers in Ukraine, the EnC Contracting Parties without Ukraine and the EU - 2017-2021 (euro cents/kWh)



Note: The Energy Community Secretariat calculations based on Eurostat. Band DC: 2,500–5,000 kWh (household electricity consumption), September 2022

Full cost recovery price of USSs is determined compliant to the Procedure for formation of prices for universal service. Both regulated (network tariff, USS supply tariff) and commodity (cost of electricity) components of a full cost recovery of USSs' price for households are currently much higher than the fixed price for households. According to the NEURC Letter *the market [end-user] price for electricity for households, depending on the price dynamics on the spot electricity market, amounts to approximately 6 UAH/kWh (with VAT)*. Figure 2 below demonstrates the structure of a full cost recovery price of selected USSs for households and compares their levels to the fixed prices of households applied in practice.

Figure 2. 2023 Estimated regulated cost-reflective price by selected USSs for household consumers compared to regulated household price, UAH/MWh (excl. VAT)



Source: ECS calculations based on publicly available data

However the wholesale electricity price increase as well as all additional costs throughout the supply chain – TSO, DSO and USS tariffs - have not been reflected in the final household electricity prices. Thus, even after the increase, the currently approved household electricity price covers only 44% of costs for its production, transportation and taxation, allowing conclusion that the prices are still regulated at the level below cost.

### c) Protection of vulnerable customers

The Electricity Market Law (Article 61) defines that household consumers shall be defined as vulnerable consumers in accordance with the procedure for protection of vulnerable consumers approved by the CMU, which also shall define special measures to protect vulnerable consumers from disconnection in certain periods and the amount of targeted subsidy for categories of vulnerable consumers. However, this procedure has not been adopted since the Electricity Market Law entered into force.

In May 2023, NEURC sent<sup>15</sup> the draft Procedure for the protection of vulnerable electricity consumers to the CMU. Also the Ministry of Social Protection published for public consultations<sup>16</sup> the draft proposal of CMU act on the approval of the Procedure for the application of special additional protection measures for categories of vulnerable consumers of electricity. However the CMU adoption is still pending.

As a result, the low level of retail prices is applied to all households regardless of the capacity to pay and benefits wealthy household consumers as much as vulnerable and poor ones. That was constantly recalled by the Secretariat in earlier communications.

## Impact on market and stakeholders

### a) General PSO impact

The issues of below cost household electricity prices is a long lasting issue in the Ukrainian electricity market, mostly inspired by the political impact and sufficient amount of generation capacities in Ukraine, with almost 50% nuclear generation in the generation mix, that was treated for a long time as a cheap electricity. Such an approach withdrew the resources from the energy sector that could have been invested in its infrastructure development. Extension of below cost recovery prices for all household consumers after electricity market reform in 2019 prevented the development of a competitive retail market and kept the situation for households as it was before the reform.

From the beginning of its implementation in 2019, the HH PSO mechanism has been changed several times. A positive aspect was the replacement of the “commodity based” PSO with the “financial” PSO in 2021<sup>17</sup>, but it was accompanied with simultaneous further reductions of the lowest PSO price for household consumers (see Table 1 in the Annex). Launching of new approach to HH PSO functioning required advance cash flow payment by “Ukrhydroenergo” of UAH 1 billion to the state enterprise “Guaranteed Buyer”. This advance payment was additional to “Ukrhydroenergo’s” regular role in the HH PSO mechanism functioning, performed jointly with another generating company – Energoatom.

The Secretariat was not provided with detailed information on the impact of the prolongations of the PSO Act in March and April 2023, and relevant amendments were not complemented

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<sup>15</sup> <https://www.nerc.gov.ua/news/nkrekp-iniciyuye-posilennya-zahodiv-zahistu-vrazliviv-spozvivachiv-elektroenergiyi>

<sup>16</sup> <https://www.msp.gov.ua/projects/838/>

<sup>17</sup> CMU Resolution #859 of 11.08.2023, <https://zakon.rada.gov.ua/laws/show/859-2021-%D0%BF/ed20210817#n2>  
The “commodity” PSO model was based on provision of electricity volumes (i.e. commodity) by Energoatom and “Ukrhydroenergo” to USSs to ensure a special service under the PSO mechanism, while “financial” model replaced this mechanism with a compensation in form of funds (money) from Energoatom and “Ukrhydroenergo” to USSs. Current “financial” PSO model is described in the Annex hereto

by the proposals as regards financial funds to cover the PSO costs for market participants that may face relevant financial losses due to the PSO obligations.

Later, the NEURC's proposal to the PSO Act submitted in May 2023 indicated that, in case of no household electricity price increase, the forecasted deficit of funds for both producers with the PSO obligation will account for more than 40 billion UAH in 2023.

Finally, the current Russian aggression have a distortive impact on the power system. The energy system of Ukraine (including networks and generation) is highly damaged after the Russian targeted attacks and requires sufficient funding for reconstruction and operational security. Below-cost electricity price restrains the market and power system from rebuilding and further integration with the EU market.

#### b) Wholesale market

Current PSO Act impacts overall market liquidity withholding significant part of the volume (in the amount of minimum consumption of electricity by household consumers of USS of the previous year) from trading on other market segments (including DAM). Also, USS buy this volume at the historical monthly BASE price of DAM (M-3), thus the producers may face economic losses selling their energy at a price that does not reflect the market price at the time of production.

Moreover, from the beginning of the military aggression by Russia on 24 February 2022, the electricity market was stressed facing the sharp decrease of consumption and damages of the energy infrastructure that highly impacted its financial liquidity. From the beginning of March 2022, producers with PSO obligations (Energoatom and Ukrhydroenergo) practically stopped making payments for GB services. As a result, GB payments for USS services were stopped, and USSs began to accumulate debts for electricity purchased from producers with PSO obligation and for transmission and distribution services.

In order to prevent a total crisis of non-payments after the introduction of martial law, producers with PSO were imposed with the obligation to provide additional volumes of electricity to GB for its sale to USSs. The DAM price is applied to such additional volumes, and payment can be made by USSs by offsetting against the value of provided services. Thus, in the current version of the PSO, de facto, an element of "commodity PSO" again appeared<sup>18</sup>.

Based on publicly available information, the overall amount of funds covered by the current PSO mechanism<sup>19</sup> in place is approximately UAH 136 billion per annum (EUR 3.3 billion) in 2022. This estimation is also confirmed by NEURC. As of April 2023, the amount of accumulated debt in the functioning of PSO mechanism stands at approximately UAH 30 billion (EUR 0.74 billion).<sup>20</sup> A chain of debt has been deepened between the participants of the PSO mechanism (producers, GB, USSs) and also between the USSs and the TSO and the DSOs.

Without the adjustment of the household fixed price to dynamics of commodity prices in the market, the financial stability of market participants (involved in performance of HH PSO) is constantly at risk. This is clearly demonstrated by a deepened debt throughout the supply chain (generators, TSO, DSOs, USSs), especially impacted by other regulatory and resulting

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<sup>18</sup> Order of Ministry of Energy No. 132 dated 21.03.2022

<sup>19</sup> Difference between the cost of electricity for household consumers, which is calculated according to the USS prices, and the cost of electricity for household consumers, defined at to fixed prices of the PSO Act

<sup>20</sup> [https://www.gpee.com.ua/news\\_item/1187](https://www.gpee.com.ua/news_item/1187)



market developments. A key example is increase of DAM price caps<sup>21</sup> and resulting increase of the DAM prices, which is a commodity component of price for households, while fixed and applied in practice household prices remain the same. Thus, gradually, PSO obligations wash out the financial resources from state owned producers (Energoatom and Ukrhydroenergo), network operators and USSs, that is an even more critical issue in the current situation of low market liquidity.

### c) Retail market and energy efficiency

The PSO Act obliges only USSs to supply household consumers (and other equated to them) at fixed (below market) electricity prices, which constitutes an economic barrier for the households to choose other supplier on the retail market and de facto ties these groups of consumers solely to the USSs.

In the absence of the abovementioned procedure for protection of vulnerable consumers, the existing schemes of subsidies and abatements are still in use. The subsidies are provided for housing and utility services and paid in cash to the service providers, while the abatements represent a discount in the utility bill and are applied to the volume within the established consumption norms. As of January 2021, more than 3.1 million households receive housing subsidies and additional 1.8 million receive abatements of 25% to 100%, depending on the beneficiary category<sup>22</sup>. This means that close to 30% of Ukrainian households receive some kind of compensation for energy and communal services. Recipients of both protection schemes belong to a wide range of social categories, low- income being only one of the eligibility criteria. Furthermore, the existing schemes are based on a great number of legal acts, which makes it difficult to capture the households in need in a harmonized way.

A preliminary assessment of the number of households in energy poverty suggested that the share of energy-poor households in Ukraine ranged between 13% and 18% at the end of 2021, depending on the indicators in use. A more precise and up to date assessment of number of households in energy poverty, but also the thorough revision of criteria for eligibility to support them need to be performed within the process of market reform and clean energy transition.

The situation with the below cost household electricity prices distorts also other useful and timely legislative developments<sup>23</sup> to increase demand response and system flexibility, grid decentralization and decarbonisation. The concept of active customers and their deep engagement into the market operation and provision of services, net billing scheme, development of smart grids, and the development of small scale generation installations at customer side (e.g. PV) aims to give customers a number of tools to react and adjust their consumption behavior in response to the market price. Without market- based prices these tools may be misused and give wrong incentives for consumers to generate unfair profit using the difference between regulated and market price. For example, the situation when households pay low price for electricity but at the same time sell electricity from PV installation at much higher price. This is a widespread case, as according to the data of NEURC<sup>24</sup>, by the end of 2021, total installed capacity of solar stations in private households is 1,200 MW

<sup>21</sup> NEURC Resolution No. 1126 of 27.06 2023

<sup>22</sup> Study on addressing energy poverty in the Energy Community Contracting Parties, 2021, [https://www.energy-community.org/dam/jcr:f201fef9-3281-4a1f-94f9-23c3fce4bbf0/DOOREIHP\\_poverty\\_122021.pdf](https://www.energy-community.org/dam/jcr:f201fef9-3281-4a1f-94f9-23c3fce4bbf0/DOOREIHP_poverty_122021.pdf)

<sup>23</sup> Law of Ukraine #3220-IX of 30.06.2023 "On Amendments to Certain Laws of Ukraine on the Restoration and Green Transformation of the Energy System of Ukraine"

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[https://www.nerc.gov.ua/storage/app/sites/1/Docs/Byuleten\\_do\\_richnogo\\_zvitu/byuleten\\_do\\_richnogo\\_zvitu\\_nkre\\_kp-2021.pdf](https://www.nerc.gov.ua/storage/app/sites/1/Docs/Byuleten_do_richnogo_zvitu/byuleten_do_richnogo_zvitu_nkre_kp-2021.pdf)

(44,961 units), out of which the majority of connections (34,063) has the connection capacity of 30-50 kW. These investments evidently require substantial financial solvency of such household that also have an incentive to profit from price differences. Also, during the last winter, when the Ukrainian system was attacked by the Russia and that lead to the application of load reduction schedules and shutdowns, a lot of households invested in generators and thus consumed electricity at cost that is up to ten times higher than the current HH prices.<sup>25</sup>

The energy price is also one of the key factors for developments of energy efficiency and energy saving measures. Low household electricity price does not incentivize consumers to save.

## Compliance assessment

### 1) Procedural aspects

Based on the requirements of the Energy Community acquis (Article 3 of the Directive 2009/72/EC), Article 62 of the Electricity Market Law, provisions of Roadmap for further market integration following the synchronisation of the Ukrainian (and Moldova's) electricity networks with the Continental European Network (hereinafter, the Roadmap) and the Memorandum of Understanding between NEURC and the Energy Community Secretariat on mutual cooperation in the area of public service obligations of December 1, 2022 (hereinafter, the MoU), the draft of any new PSO Act shall be consulted with the Secretariat prior to submission of the revised draft to the CMU<sup>26</sup>. When preparing the revised draft, NEURC takes utmost account of the Secretariat's opinion.

NEURC submitted to the Secretariat the proposals to the PSO Act according to the Article 62 of the Electricity Market Law and the MoU although without the draft resolution amending the PSO Act. The CMU decision of 30 May 2023 amending the PSO Act highly reflected the principles proposed by NEURC, but the fixed household electricity price was adopted at the lower level proposed by the Ministry of Energy. Thus, the Secretariat could not provide a compliance assessment of such proposals and the decision with the Energy Community law.

### 2) Directive 2009/72/EC<sup>27</sup>

The CMU decision of 30 May 2023 introduced a single electricity price for households, undifferentiated by consumption volumes, at the level of 2.64 UAH/kWh (with VAT). Although the household electricity price still does not reflect the full cost, this adjustment represents a significant increase in household electricity prices, particularly acknowledging the war conditions.

The CMU decision defines the duration of the amended PSO until the end of 2023 that is in line with temporality requirements of the Energy Community acquis. The elimination of the block structure of household electricity prices depending on the volume of consumption may be justified having in mind that this is the state intervention in the prices under the PSO Act and the equal treatment of all households irrespectively of the consumption level.

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<sup>25</sup> Price of electricity produced from diesel generators varies from ~30 to 40 UAH/kWh (w/o VAT) depending on the price of diesel and generator technical characteristics

<sup>26</sup> In contravention of Article 62 of the Electricity Market Law and the MoU, the Secretariat was not given the possibility for review and assessment of the amendments to the PSO Act as of 24 March 2023 and of 25 April 2023

<sup>27</sup> As adapted and adopted in Energy Community, [https://www.energy-community.org/dam/jcr:1af4857c-9985-4c2a-baff-95c5bf1ee38b/Directive\\_2009\\_72\\_EL.pdf](https://www.energy-community.org/dam/jcr:1af4857c-9985-4c2a-baff-95c5bf1ee38b/Directive_2009_72_EL.pdf)

At the same time, the Secretariat is obliged to note that there is still a room for PSO Act improvement to ensure compliance, considering the following:

- the new level of household electricity price of 2.64 UAH/kWh (with VAT) is still far from the full cost reflective level of retail prices. Although this is a very important step on the way towards household electricity prices adjusted to the market based retail price, the CMU decision lacks transparency and predictability in terms of next steps to be made for further household electricity price increase<sup>28</sup>;
- the PSO Act has no methodology or principles as regards the calculation of the household fixed prices, which is not transparent and cannot be verified as required by the Article 3 of the Directive 2009/72/EC;
- the PSO goes beyond its aim to ensure the *affordability* of electric energy for household consumers as it fixes the electricity price for all households (and equaled to them customer categories, as defined by the PSO Act), irrespectively of social vulnerability. Furthermore, the concept of vulnerable customers is still not defined as required by Article 3 of the Directive 2009/72/EC. That does not resolve the non-compliance of the PSO Act in terms of its *proportionality* as regards beneficiaries;
- obligation to supply households at fixed prices put only on USSs creates an economical barrier for household to switch supplier as well as restricts the competition on the retail market among suppliers. This contributes to non-compliance of the PSO Act in terms of equality of access for electricity undertakings to consumers;
- the issue of cost compensation of the imposed PSOs on market participants (electricity producers, TSO, DSOs, USSs) still needs to be resolved, as the financial balance of the PSO even in case of an increase of household electricity price to 2.64 UAH/kWh would not cover the financial losses of producers resulting from the PSO obligation.

### 3) Clean Energy Package

Recently adopted in Energy Community Directive 2019/944 of 5 June 2019 on common rules for the internal market for electricity (hereinafter, Directive 2019/944)<sup>29</sup>, that shall be implemented by Ukraine until 31 December 2023, clearly states in Article 5 that suppliers shall be free to determine the price at which they supply electricity to customers and that protection of energy poor and vulnerable household customers shall be ensured by social policy or by other means than public interventions in the price setting for the supply of electricity. Only as a **derogation** from these provisions, the Contracting Parties may apply public interventions in the price setting for the supply of electricity to energy poor or vulnerable household customers, or, for the purpose of a transition period to establish effective competition for electricity supply contracts between suppliers, and to achieve fully effective market-based retail pricing of electricity, to household customers and to microenterprises that do not benefit from public interventions.

Such public interventions shall be subject to the following conditions:

- (a) pursue a general economic interest and not go beyond what is necessary to achieve that general economic interest;
- (b) be clearly defined, transparent, non-discriminatory and verifiable;
- (c) guarantee equal access for Energy Community electricity undertakings to customers;
- (d) be limited in time and proportionate as regards their beneficiaries;
- (e) not result in additional costs for market participants in a discriminatory way.

<sup>28</sup> Although this may be appealed by the martial law conditions in Ukraine

<sup>29</sup> [https://www.energy-community.org/dam/jcr:4dd35c70-91d7-4219-8396-7637a0cef7c7/DirectiveEU2019\\_944.pdf](https://www.energy-community.org/dam/jcr:4dd35c70-91d7-4219-8396-7637a0cef7c7/DirectiveEU2019_944.pdf)

While addressing energy poverty is a comprehensive and challenging task, it is the requirement of the Energy Community legislation<sup>30</sup> to define the concept of vulnerable consumers, take measures to protect them, assess the number of households in energy poverty and design policies and measures to address energy poverty in the integrated national energy and climate plan (hereinafter, NECP). In order to facilitate this process, the Secretariat conducted the Study on addressing energy poverty in the Energy Community Contracting Parties<sup>31</sup> and provided the corresponding Policy Guidelines.

To be compliant with Directive 2019/944, the current PSO Act requires further substantial changes to be put in force before the expiry of the implementation deadline (31 December 2023).

The Communication of the European Commission REPowerEU: Joint European Action for more affordable, secure and sustainable energy<sup>32</sup>, published following the energy crisis as a result of sharp gas prices that was additionally triggered by the invasion of Ukraine by Russia, confirms that price regulation and transfer mechanisms to help protect consumers and economies are possible. Thus, the Commission provided guidance on Application of Article 5 of the Electricity Directive during current situation (Guidance)<sup>33</sup> to help Member States devise schemes for regulated prices. The Guidance sets out reasons why high and volatile wholesale gas and electricity prices may currently be restricting competition and harming customers. These could serve as the basis to identify the conditions under which to use the flexibility in Article 5 in relation to price interventions at retail level. Although it does not constitute a legal basis for the Energy Community, this Guidance may be taken into consideration when designing the new PSO Act in order to be in compliance with the Energy Community and EU acquis.

## Conclusions and recommendations

The Secretariat welcomes CMU decision No 544 as a significant step towards fully cost-reflective household electricity prices.

However, even after the increase, the electricity retail prices in the household segment are still by far the lowest in the Energy Community and the EU and do not cover the full cost of electricity production, transportation and supply. The financial amount of PSO is triggered by the fact that all households regardless of whether they are vulnerable and energy poor benefit from the low electricity price. Without narrowing the state support to the extent needed for protection of vulnerable customers as well as without the gradual household electricity price increase, any amendments to the PSO Act will only tackle the symptoms of the lack of financial liquidity of the sector and entrench cross-subsidization, lower competition to the detriment of market efficiency and solvency of its participants.

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<sup>30</sup> Please see the summary of legal obligations in the Secretariat's Policy Guidelines on Identifying and Addressing Energy Poverty in the Energy Community Contracting Parties, August 2022 ([https://www.energy-community.org/dam/jcr:56632fbf-baf6-49c5-ad23-d997b552e1e6/PG2022-02-ECS\\_poverty-082022.pdf](https://www.energy-community.org/dam/jcr:56632fbf-baf6-49c5-ad23-d997b552e1e6/PG2022-02-ECS_poverty-082022.pdf))

<sup>31</sup> [https://www.energy-community.org/dam/jcr:f201fefd-3281-4a1f-94f9-23c3fce4bbf0/DOOREIHP\\_poverty\\_122021.pdf](https://www.energy-community.org/dam/jcr:f201fefd-3281-4a1f-94f9-23c3fce4bbf0/DOOREIHP_poverty_122021.pdf)

<sup>32</sup> <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2022:108:FIN>

<sup>33</sup> [https://eur-lex.europa.eu/resource.html?uri=cellar:71767319-9f0a-11ec-83e1-01aa75ed71a1.0001.02/DOC\\_2&format=PDF](https://eur-lex.europa.eu/resource.html?uri=cellar:71767319-9f0a-11ec-83e1-01aa75ed71a1.0001.02/DOC_2&format=PDF)

An appropriate price signal is essential also to give an incentive to save electricity as well as to invest in demand response and self-production technologies. The past winter showed that there is room for energy saving at household level incentivized by a number of energy efficiency measures and information campaigns (including supported by the EU). Also, it showed that there is a sufficient number of households that are willing to pay high price for electricity subject to its availability.

The Secretariat encourages the Government and the NEURC to start working on revision of the PSO Act and the development of the retail electricity market in order to ensure full cost-reflective retail electricity prices, combined with the targeted measures to protect vulnerable customers. The speed of bringing household electricity prices to full cost reflectivity shall also take into consideration the social and economic conditions in Ukraine as impacted by Russian war of aggression against Ukraine.

To ensure compliance with Directive 2019/944, the new design of PSO should apply starting from 01 January 2024. In particular it would be recommended to consider the following:

- clear criteria for vulnerable and energy poor household customers should be defined and could take into account current severe conditions that Ukrainian people face due to the Russian aggression. Also, the PSO Act should not extend the scope of definition of households with the categories that are not considered as households by the Energy Community acquis. This will allow to support vulnerable and energy poor customers with limited financial resources. The indicators of energy poverty from the Secretariat's Policy Guidelines on Identifying and Addressing Energy Poverty in the Energy Community Contracting Parties and in the EU may be of reference<sup>34</sup>.
- An approach for increase of household prices towards full cost reflectivity has to be designed and implemented with an ultimate goal to completely phase out the end-user price regulation while simultaneously ensuring protection for energy vulnerable household consumers directly from the social security system. Ukraine has positive experience in the gas market where the retail market was opened and the PSO was suspended<sup>35</sup>, at the same time the mechanism of social security system was developed to ensure energy supply for people with low income. The legal framework and experience in the gas sector could be extended to the electricity.
- One of the sources for the state budget to finance expenses associated with the protection of vulnerable and energy poor consumers may be an external macro-economic aid provided to Ukraine specifically for this purpose. A similar macro-economic tool has been provided by the EU Commission<sup>36</sup> to Western Balkans in 2022-2023, in a form of direct budget support, to ease the impact of the energy crisis on vulnerable households and small and medium enterprises and to Moldova, including for the purposes to ensure energy security in 2022-2023<sup>37</sup>.
- As a transitional solution, the application of Art 5 of the Directive 2019/944 may follow the Guidance.
- Regulated prices, if applied, should be cost-reflective. The methodology for setting regulated prices should be transparent and cover the reasonably incurred costs of suppliers. As one of the references, the NEURC's methodology for calculation of prices of USSs may be used. This would also be in line with the Article 62 (3) of the Electricity Market Law.

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<sup>34</sup> Commission Recommendation (EU) 2020/1563 of 14 October 2020 on energy poverty, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32020H1563>

<sup>35</sup> CMU Resolution No. 867 of 19.10.2018

<sup>36</sup> <https://balkangreenenergynews.com/eu-launches-eur-1-billion-energy-support-package-for-western-balkans/>

<sup>37</sup> [https://ec.europa.eu/commission/presscorner/detail/en/ip\\_23\\_343](https://ec.europa.eu/commission/presscorner/detail/en/ip_23_343)

- The PSO design should not restrict households from switching to other (than USSs) suppliers. Furthermore, it should incentivize them to look for better services and find a more proper commercial offer on the market. This shall be supported by measures that ensure equal access of all suppliers to available resources.
- The mechanism shall be open for participation of all interested suppliers (not only USSs) and should not increase the market concentration of individual participants. At the same time, the PSO shall consider operational and financial liquidity of market participants and ensure cost compensation for financial losses resulting from the PSO obligations.
- Any price intervention shall be temporary, thus from the very beginning the criteria (method) of assessing the need to further proceed with the price regulation is needed. A roadmap for removing regulated prices and moving to fully competitive markets will increase transparency and predictability for market participants and allow for planning the state resources ahead.
- The electricity price increase shall be accompanied with additional tools for consumers to respond to price fluctuations, e.g. to use self-generation scheme and/or to store energy or to sell energy, to apply energy efficiency measures to reduce demand.
- The policies and measures to address energy poverty shall be designed in the NECP as required by the Regulation (EU) 2018/1999<sup>38</sup>.
- The procedural aspects of the PSO Act drafting and consulting with the Secretariat shall be duly followed.

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<sup>38</sup> [https://www.energy-community.org/dam/jcr:e24c911e-f0f6-4f26-a152-ec79d85ee1a4/Regulation\\_EU\\_2018\\_1999.pdf](https://www.energy-community.org/dam/jcr:e24c911e-f0f6-4f26-a152-ec79d85ee1a4/Regulation_EU_2018_1999.pdf)

## Annex

### 1) Summary of main PSO Act provisions:

#### 1. Categories of consumers who are supplied with electricity at fixed prices under HH PSO are:

- Individual HH consumers;
- Collective HH consumers;
- Dormitories;
- Technical goals of multistore buildings such as emergency and evacuation lighting, operation of individual heating points, boiler rooms, elevators, pumps, intercom devices, fire protection systems, ventilation, smoke removal and air conditioning systems, alarm systems, aviation beacons belonging to owners of apartments in an apartment building on joint property rights) and lighting of yards, stairs and number plates;
- Cottage and cottage-building cooperatives, garden societies, garage-building cooperatives for technical purposes (pump operation) and lighting of the territory;
- Legal entities that are owners (balance sheet holders) of property used for the compact settlement of internally displaced persons (towns made of prefab modules, dormitories, health camps, rest houses, sanatoriums, boarding houses, hotels, etc.), in terms of meeting the own household needs of internally displaced persons;
- Religious organizations in terms of electricity consumption for communal and household needs.

#### 2. Key aspects of PSO mechanism:

- USSs procure electricity from Energoatom for standard BASE\_M products in the amount of the minimum consumption of electricity by HHs of the relevant USSs per hour in the same month of the previous year at the DAM price BASE M-3, where M is a billing month;
- USSs buy "additional" volumes of electricity necessary to meet the needs/consumption profile of HH consumers under bilateral contracts, on the DAM, intraday market (IDM);
- Each USS provides "services" to ensure the availability of electricity for HH consumers (hereinafter - USS services) to GB;
- The value of the services is equal to the difference between the cost of electricity for HH consumers, which is calculated according to the USS prices, and the cost of electricity for HH consumers, defined at to fixed prices of the PSO Act;
- USS prices are calculated in accordance with the Procedure for the formation of prices for universal service and includes the price of electricity (based on volumes and procurement prices from Energoatom, and "additional" volumes at DAM prices), transmission tariffs, distribution tariffs, tariffs for USS services. In this way, regulatory approach ensures that USS price reflects the total cost of service of supplying electricity to the USS's consumers.
- GB provides services for ensuring the availability of electric energy for HH consumers (hereinafter - GB services) to the producers specified in Appendix 1 of CMU Resolution 483, namely Energoatom and Ukrhydroenergo.
- Sum of the Cost of USS Services equals the sum of the value of GB Services

- The cost of the GB services is distributed between Energoatom and Ukrhydroenergo in proportion to the conditional profits of each producer, taking into account the weighting factors (per Annex 6 of CMU Resolution 483 is 0.95 for Energoatom and 0.6 for Ukrhydroenergo);
- From July 2022 and until the day of termination or cancellation of martial law, also electricity exporters pay 80% of the profit from electricity exports to GB (per CMU Resolution No. 775 of July 7, 2022). Thus, the cost of the GB Service, which is distributed for repayment between Energoatom and Ukrhydroenergo, is reduced by this amount. However, currently there is no export of electricity from Ukraine.

2) Development of household electricity prices in Ukraine in the period of 2017 to 2023<sup>39</sup>:

Table 1 Household electricity prices in Ukraine from 2017 until 2023 (excl. VAT)

Period/ Categories of consumers	01.03.2017-30.06.2019 and 01.07.2019 <sup>40</sup> - 31.12.2020	01.01.2021-30.09.2021 <sup>41</sup>	01.10.2021 <sup>42</sup> – 30.05.2023	01.06.2023 – 31.12.2023
for the amount consumed up to 100 kWh of electricity per month (inclusive)	75 kop/kWh <sup>43</sup> (~2,4 euro cents/kWh) <sup>44</sup>	140 kop/kWh	120 kop/kWh (up to 250 kWh, including, for the entire volume of consumption)	264 kop/kWh (~5.6 euro cents/kWh)
for the volume consumed over 100 kWh of electricity per month	140 kop/kWh <sup>10</sup> (~4,5 euro cents/kWh)		140 kop/kWh (up to 250 kWh, including, for the entire volume of consumption)	

<sup>39</sup> Based on consumption criteria, not include other categories (e.g, large families, foster families and family-type children's homes, dormitories etc., see Annex)

<sup>40</sup> <https://www.nerc.gov.ua/sferi-diyalnosti/elektroenergiya/naselennya/cini-ta-tarifi-na-elektroenergiyu-dlya-pobutovih-spozshivachiv-naselennya-v-ukrayini/fiksovani-cini-na-elektrichnu-energiyu-dlya-pobutovih-spozshivachiv-naselennya-z-01072019>

<sup>41</sup> <https://www.nerc.gov.ua/sferi-diyalnosti/elektroenergiya/naselennya/cini-ta-tarifi-na-elektroenergiyu-dlya-pobutovih-spozshivachiv-naselennya-v-ukrayini/fiksovani-cini-na-elektrichnu-energiyu-dlya-pobutovih-spozshivachiv-z-01012021>

<sup>42</sup> CMU Resolution No 859 of 11.08.2021

<sup>43</sup> For the period from October 1 to April 30 the eligible amount is 3000kWh/month

<sup>44</sup> At National Bank of Ukraine (NBU) average exchange rate UAH/EUR for 2020, [https://bank.gov.ua/files/Exchange\\_r.xls](https://bank.gov.ua/files/Exchange_r.xls)