



**Assessment of the Procedure (methodology)  
determining the amount of penalties imposed by  
the National Energy and Utilities Regulatory  
Commission**

**by the Energy Community Secretariat**

**June, 2024**

# PURPOSE STATEMENT

**Assessment of the “Procedure (methodology) determining the amount of penalties imposed by the National Energy and Utilities Regulatory Commission” adopted according to the Law of Ukraine “On Amendments to some laws of Ukraine regarding the prevention of abuse in the wholesale energy markets” of June 10, 2023 No. 3141-IX (hereinafter - the “REMIT Law”).**

## TABLE OF CONTENT

|   |          |
|---|----------|
| <b>Introduction</b>                                 | <b>1</b> |
| <b>Background</b>                                   | <b>1</b> |
| <b>Impact on market and stakeholders in Ukraine</b> | <b>4</b> |
| <b>Compliance assessment</b>                        | <b>4</b> |
| <b>Conclusions and recommendations</b>              | <b>5</b> |

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## Ukraine Energy Market Observatory

Assessment 10/24

### **Assessment of the Procedure (methodology) determining the amount of penalties imposed by the National Energy and Utilities Regulatory Commission**

## Introduction

The present assessment follows a request of the National Energy and Utilities Regulatory Commission (hereinafter “NEURC”) to the Secretariat to provide a compliance assessment of the draft “Procedure (methodology) determining the amount of penalties imposed by the National Energy and Utilities Regulatory Commission” (hereinafter, the Methodology for penalties calculation, the Methodology) developed by the NEURC as required by the REMIT Law transposing into Ukrainian legislation provisions of the Regulation of the European Parliament and Council (EU) No. 1227/2011 of October 25, 2011, on wholesale energy market integrity and transparency (hereinafter, REMIT Regulation). This assessment summarises comments to draft Methodology for penalties calculation as provided by the Secretariat to the NEURC in its communication of 01 September 2023 and provides a detailed assessment of the finally adopted act.

## Background

### a) Penalties under REMIT Law

The REMIT Law amended, among others, Article 17 of the Law of Ukraine “On the National Commission that carries out State Regulation in the Sphere of Energy and Communal Services” and tasked the NEURC to develop and approve the Methodology for penalties calculation. Such a procedure, when determining the amount of the penalty, should take into account the nature, duration and seriousness of the violation, the amount of damage caused and the amount of potential income that could be gained due to the violation. Methodology for penalties calculation shall be approved by the Regulator after consultation with the Energy Community Secretariat.

The REMIT Law also sets the maximum penalties for market manipulation and insider trading<sup>1</sup>. At the same time, REMIT Law limits the maximum penalty at up to 10% of the annual revenue of the wholesale market participant on the relevant market. The Secretariat raised concern over this provision in terms of compliance with the principle of effectiveness of penalties from Article 18 of the REMIT<sup>2</sup>. While this continues to be a compliance issue for the Energy

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<sup>1</sup> REMIT Law significantly increased the maximum level of penalties for market abuse compared to the licensing penalties. I.e. from previous max of UAH 1.7 million (~EUR 40 000) for licensing to max around EUR 11 500 000 (EUR 6 000 000 in first two years) for REMIT abuse.

<sup>2</sup> For more details on penalties under REMIT Law please refer to the Assessment Note 14/2023; [https://www.energy-community.org/dam/jcr:42be4f40-e842-430d-b7cb-40939ca935ed/20072023\\_UEMO\\_REMIT\\_Law\\_final\\_clean.pdf](https://www.energy-community.org/dam/jcr:42be4f40-e842-430d-b7cb-40939ca935ed/20072023_UEMO_REMIT_Law_final_clean.pdf).

Community Secretariat, it is important to note that this assessment specifically focuses on the methodology used by NEURC to determine the penalties imposed.

Chapter II Final and Transitional provisions of the REMIT Law also provides that within two years from its entry into force the Regulator, in the event of an abuse being committed on the electricity market and/or on the natural gas market, is entitled to impose penalties on market participants for abuse regarding the wholesale energy market after consultation with the Energy Community Secretariat.

In order to implement the above-mentioned provisions of the REMIT Law, the “Memorandum of Understanding on consulting the decision to impose penalties for abuse in the wholesale energy market on market participants” was signed between the Secretariat and the NEURC on 27 July 2023 (hereinafter, MoU).

b) Methodology for penalties calculation<sup>3</sup>

The Methodology for penalties calculation establishes two different mechanisms for calculating penalties:

- 1) violations of legislation in the fields of energy and communal (utilities) services and relevant license conditions, and
- 2) abuse on the wholesale energy market under the REMIT Law.

In terms of REMIT, the Methodology for penalties calculation applies to all wholesale energy market participants (hereinafter, WEM Participant) which are registered by the NEURC. It applies also to electricity and gas market participants who carry out or intend to carry out activities on the electricity and gas markets, persons performing the functions of data transfer administrator or insider information platform administrator, consumers of electricity and/or natural gas with a total maximum consumption capacity of 600 GWh per year as well as officials of WEM Participants.

Under the Methodology, the penalties for breaches under the REMIT Law are calculated in the following stages:

- Calculation of the initial amount of the penalty depending on the severity of the abuse (the type of abuse committed on the wholesale energy market) and taking into account the damage caused and/or additional benefits<sup>4</sup> (if it is possible to establish such damage or potential benefits);
- adjustment of the amount of the penalty taking into account the duration of the abuse;
- adjustment of the amount of the penalty taking into account mitigating and/or aggravating circumstances;
- adjusting the amount of the penalty in order to ensure an adequate level of deterrence against future abuses and to ensure the proportionality of punishment for abuses;
- determining the final amount of the penalty and adjusting the amount of the penalty to avoid exceeding the maximum limit of the penalty set by the laws, which, as outlined above, remains a compliance concern for the Energy Community Secretariat.

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<sup>3</sup> <https://zakon.rada.gov.ua/rada/show/v1800874-23#Text>

<sup>4</sup> Additional benefit (potential benefit) - additional and/or potential income or benefit in another form that the market participant was able or intended to receive and/or losses or expenses that he was able to or intended to avoid as a result of the violation, directly or indirectly.



The severity of the abuse depends on the type of abuse defined by relevant provisions of the REMIT Law<sup>5</sup> and is rated with particular percentage for such type of violation applied to the maximum amount of penalty. For example, the severity rates for manipulation and insider trading are the highest and increase the penalty by 10%.

The damage caused and/or potential benefits resulting from the violation is considered by applying the relevant % to the sum of damage or benefits (considering the highest) according to the type of violation. Further adjustments (as described above) apply to the initial amount of penalty depending on the conditions of each particular abuse and investigation case. The nature of the committed abuse is also assessed by factor of intention<sup>6</sup>.

Penalty adjustments for duration factor and mitigating and/or aggravating circumstances are done based on the formulas and relevant rates provided in the Methodology.

Further, based on the Methodology the NEURC has the right to increase the amount of the penalty, calculated at previous stages, by 100% in case of its disproportion to the committed violation that shall be assessed in each individual investigation case. For violations where it is possible to determine the amount of damage caused/the received benefit, the disproportionality criterion may be assessed if the amount of the calculated damage/benefit exceeds by more than 10 (ten) times the amount of the calculated penalty.

In order to ensure the adequate level of deterrence against future abuses, the NEURC also has the right to increase the amount of penalty by 50% if it has reason to believe that the calculated amount of the penalty will not deter the offender from future abuse<sup>7</sup>.

At the same time, the Methodology for penalties calculation provides the option for the NEURC to reduce (in exceptional cases) the amount of the penalty by 80%, if the payment of the full penalty is reasonably impossible or would lead to a serious financial situation and further insolvency of the offender, or if the amount of the calculated penalty does not correlate with the severity of the abuse/degree of the damage that has been caused.

Finally, the calculated amount of penalty shall be compared to the maximum value of penalty provided for the particular type of violation under the REMIT Law and, in case the calculated amount exceeds the one of the law, the NEURC shall adjust the final amount of the penalty in accordance with its maximum amount (that is 10% of turnover of wholesale market participant on relevant energy market).

Finally, at the day of the publication of the draft decision on the official NEURC website, the calculation of the amount of the penalty, along with an explanation of the applied rates and adjustments, is sent to the WEM Participant in question.

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<sup>5</sup> Carrying out operations with wholesale energy products without registration as a wholesale market participant (15%); violation of prohibition on the use of insider information (25%), manipulation in the wholesale energy market (25%); an attempt to manipulate the wholesale energy market (20%); non-disclosure or disclosure of insider information in violation of the requirements established for the disclosure of such information (20%).

<sup>6</sup> Considers if the violation was intentional or not.

<sup>7</sup> According to the draft Methodology such grounds can be, in particular, the financial situation of the violator, the size of the expected benefit from the abuse, similar abuses by market participant in question in the past.

## Impact on the markets and stakeholders in Ukraine

Before the adoption of the REMIT Law, penalties fined by the NEURC, for violations detected in the course of licensing control of activities in energy and utilities sectors or investigations, were decided by discretion of the Regulator within the maximum limits set by the relevant primary legislation (e.g. Law of Ukraine “On electricity Market”, Law of Ukraine “On natural gas market”, etc.). As it was analysed in Assessment Note 14/2023, penalties introduced by the REMIT Law for abuse on wholesale energy market are not only comparable to those applied in the Energy Community and the EU, but are by far higher than in some countries of comparable or larger market size. The approval of the Methodology shall increase the transparency of penalties’ calculation and ensure non-discrimination in application of penalties by the Regulator. The Methodology will also enable market participants to understand their responsibilities in case of violation, as penalty regime serves not only as a punishing but also as a deterrent factor to prevent any type of market abuse.

## Compliance assessment

In this assessment, the Secretariat focuses on the compliance of provisions of the Methodology related to the calculation of penalties for abuse on wholesale energy markets with the provisions of the REMIT Regulation (in particular, Article 18), incorporated in the Energy Community by Ministerial Council of the Energy Community by Decision 2018/10/MC-EnC of 29 November 2018<sup>8</sup>.

In general, the Secretariat finds the draft Methodology compliant with the main principles of penalties calculation for infringements of REMIT provided in Article 18. In particular, the Methodology considers the adjustment of the penalty with conditions of proportionality, the nature of abuse, duration and seriousness of the infringement, the damage caused and the potential gains from trading based on inside information and market manipulation, which have been correctly transposed.

As Article 18 of REMIT sets the principles of penalties calculation specifically for infringements of REMIT requirements, the Secretariat supports the general approach proposed in the Methodology to separate penalties calculation under licensing control procedure from those under the REMIT Law. In the final Methodology this was improved as proposed by the Secretariat.

Under the Methodology (paragraphs 1.4 and 3.2.4), the NEURC calculates the amount of the penalty for each individual violation committed (if the abuse simultaneously falls under several types of violations in the wholesale energy market). The adopted provision took into account the proposal of the Secretariat that penalty for each violation shall be addressed separately to reflect the nature of the abuse and to ensure the proportionality in case of multiple different violations under REMIT committed by the same wholesale market participant.

The assessment of the seriousness of the concrete violation in question based on the type of the violation is simple and clear which may be justified in the initial phase of REMIT implementation. Nevertheless, solely relying on the type of violation may not be a sufficiently

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<sup>8</sup> [https://www.energy-community.org/dam/jcr:011d891f-6cef-4555-9e9a-53d88e54d4b1/Regulation\\_1227\\_2011\\_REMIT.pdf](https://www.energy-community.org/dam/jcr:011d891f-6cef-4555-9e9a-53d88e54d4b1/Regulation_1227_2011_REMIT.pdf).

determinative factor of seriousness. Also, the Methodology (paragraph 3.2.5.) sets the same rate of seriousness (5%) for non-disclosure and for incompliant disclosure of insider information that is non-proportionate in terms of the nature of abuse.

Provisions as regards adjustment of the amount of the penalty with the criteria of duration of the abuse are provided in a more practical and transparent way (now in days), as recommended by the Secretariat.

While section 3.4 clearly defines the size of penalty based on formulas, section 3.5 still allows the Regulator to adjust the final penalty by increasing it by 100% based on a more discretionary approach. Section 3.5 repeatedly takes into account the same criteria already considered in calculations under Section 3.4, such as the size of benefit or caused damage and recurrence of the violation of the same WEM participant. Moreover, both items 3.5.1 and 3.5.3 aim at proportioning the penalty with the violation; therefore, it is not clear if the penalty increment will be applied once or twice.

Provisions of paragraph 3.5.1(2) on penalty reduction are excessive in certain cases and affect the proportionality and effectiveness of the penalty, as REMIT Law provisions already limit the maximum amount of penalty for every market participants to 10% of its turnover on the relevant energy market.

Article 3 of REMIT sets the prohibition to trade with wholesale energy products for persons who possess inside information in relation to such products, in particular members of the administrative, management or supervisory bodies of undertakings, persons with access to the information through the exercise of their employment, profession or duties, etc. Additionally, paragraph 5 provides that such prohibitions shall also apply to the natural persons who take part in the decision to carry out the transaction for the account of the legal person concerned. Although the Methodology in paragraph 1.2 (2) recognises the officials of wholesale energy market participants, it is silent as regards the penalties calculation for the individual (natural) person that is required to enforce relevant provisions of REMIT.

## Conclusions and recommendations

The Methodology for penalties calculation is largely compliant with the Energy Community *acquis* in force, namely REMIT.

At the same time, the Secretariat provides the following recommendations for improvement of the Methodology to ensure its full compliance, clarity and transparency in application, including for the two-year transition period during which the penalties decisions of the NEURC shall be consulted with the Secretariat:

- The Methodology for penalties calculation shall apply to those entities who already carry out activity, not those who have intention to carry out activity (as provided in paragraph 1.2).
- Calculation of penalties for officials (individuals) of wholesale energy market participants for REMIT violation shall be reflected in Chapter 3 of the Methodology.
- It is recommended to develop more complex approaches for assessing the seriousness of violation, considering the following criteria: impact on the market, gain or damage caused by market abuse, intentionality, previous compliance history of the market participant, role of the market participant in the market abuse done in collaboration with other market participants, impact on wholesale energy markets and cross-border effects. Although some of the criteria are currently considered in the

Methodology it is done on an individual basis and does not reflect their cumulative effect on seriousness. Cross-border effect of a violation is currently missing from penalty calculation altogether. Definition of damage shall be clearly linked to the evidence obtained by the NEURC during relevant investigation.

- It is recommended in paragraph 3.2.5 to differentiate between the criterion on seriousness of violation for insider information non-disclosure and the criterion on seriousness of violation for insider information disclosure not in accordance with the defined set of requirements.
- Double counting of application of the same condition shall be avoided. Section 3.5, including both items 3.5.1 and 3.5.3, should transparently define the circumstances to consider for penalty adjustment, which are not considered under the previous stages according to the items 3.1 - 3.4.
- It is also recommended to add to the Methodology (in Section 3) the formula for calculation of the final penalty after all adjustments; to make clear how the adjustments are accounted for.
- Provisions of paragraph 3.5.1(2) on penalty reduction should not be applied, as the constraining factor of 10% from the REMIT Law already limits the penalty at that level.
- Specific provisions shall be introduced on how the results of consultations with the Energy Community Secretariat, performed in compliance with part 8 of Transitory Provisions of the REMIT Law, impact the final NEURC decision on REMIT penalty.
- In paragraph 3.6.2, the period for which the income (turnover) is taken for calculation of the maximum amount of penalty and the data that are used for such income calculation needs to be clarified. It is recommended to use data of the income statement of the previous year, as audited in line with the applicable legislation. Additionally, there is a need to consider new market participants that entered the market during the year. Although the REMIT Law does not have details on this, the Regulator shall specify its approach in the Methodology to ensure transparency.
- The Procedure altogether lacks the process of calculation of restitution, which is envisaged as one of the mitigating factor under item 3.4.6 (1) of the Methodology.