

**ANNUAL REPORT 2004
to the European Commission**

Hungarian Energy Office

Budapest, July 2005

Contents

1. Foreword

2. Summary \ Major Developments in the last year

2.1 System of Institutions, Mandate and Organization of the Hungarian Energy Office

2.2 Main Characteristics of the Development of the Gas and Electricity Markets

2.3 Major Tasks of the Office

3. Regulation and Performance of the Electricity Market

3.1 Regulatory Issues

3.1.1 General

3.1.2 Distribution of cross-border capacities and mechanism management

3.1.3 The Regulation of the tasks of transmission and distribution companies

3.1.4 Unbundling of activities

3.2 Competition Issues

3.2.1 Description of the wholesale market

3.2.2 Description of the retail market

3.2.3 Measures to avoid abuses of market dominance

4. Regulation of the natural gas market and implementation of the regulations

4.1 Regulatory Issues

4.1.1 General

4.1.2 Management and allocation of interconnection capacity and mechanisms to deal with congestion

4.1.3 The Regulation of the tasks of transmission and distribution companies

4.1.4 Access to storage, linepack and other ancillary services

4.1.5 Unbundling of activities

4.2. Competition Issues

4.2.2 Description of the wholesale market

4.2.3 Description of the retail market

5. Security of Supply

5.1 Electricity

5.2 Gas

6. Public service obligation, customer protection

6.1 Electricity

6.2 Natural gas

1. Foreword

This report has been created based on Section 9 of Article 3, on Article 4 and on paragraph (8) of Article 23 of Directive 2003/54/EC concerning common rules for the internal market in electricity and repealing Directive 96/92/EC, furthermore on Section 6, Article 3, on Article 5 of Directive 2003/55/EC concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC.

The establishment of a competitive market for line transmitted energy carriers is stipulated in Act CX/2001 (Electricity Act, hereinafter: VET), as well as Act XLII/2003 on natural gas supply (hereinafter: GET), as well as secondary provisions stipulating the execution thereof. Regulatory measures related to the operation of the natural gas and electricity energy market are provided for by the Hungarian Energy Office (the Office).

The VET issued in 2001 and entering into force mainly in 2003 was passed by the Parliament in accordance with the EU (96/92 EC) Directive in effect at that time. Harmony with the provisions of Directive 2003/54/EC had been ensured by amending individual sections of certain decrees (eligibility decree, enforcement decree of the Act, decree on cross-border electricity transmission etc.), and is being ensured by the amendment of the VET. When developing each provision of the GET, we had taken into account the contents of the draft EU Directive which had been known in the beginning of 2003. Integration of the specific provisions of the Directive 2003/55/EC into the statutory system of Hungary has in part been completed with the modification of the decrees. Further required changes are being ensured by the modification of the GET.

The competitive market and the public utility market are operating simultaneously with the gradual opening of the Electricity market, which started on January 1, 2003. The independent system operator, Magyar Villamosenergia-ipari Rendszerirányító Rt. (hereinafter: MAVIR Rt.) has become a separate licensee as of January 1, 2003. From the 1st of January 2003 customers with a consumption exceeding 6.5 GWh at a single site had been eligible to enter the competitive market. Starting with July 1, 2004, eligibility covers 70% of the customers. Until the end of 2004, 187 customers left public utility suppliers. Their consumption is 6,939 GWh/year, representing approximately one fourth of the national consumption. A part of customers had been able to enter the market by implementing „profile” based purchasing. Eligible customers are supplied by 10 active market participants from among the 25 licensed electricity traders. Electricity traders, as well as the 5 eligible customers requested and received a license to transmit electricity across the borders. Spare capacity of cross-border interconnection lines has been sold by MAVIR Rt. within the framework of an auction since April 2003. The extension of market opening is hindered by the fact that supply on the competitive market is still limited, as the capacity of power plants has been mostly contracted by the public utility wholesaler (MVM Rt.) within the framework of long-term power purchase agreements. Most of the free market electricity has been made up of import.

In 2003, required statutory provisions have been issued for opening the natural gas market as of January 1, 2004, and codes were completed. The Office issued operating licenses to companies, based on the GET, and therefore the official conditions for the new operation of the natural gas market were established by January 1, 2004. Starting with July 1, 2004, all non-household customers have become eligible customers. 23 eligible customers abandoned public utility supply by the end of 2004, which represented 6% of total gas consumption.

The Minister of Economy and Transport acts as the price authority, while the Office performs price preparatory activities for both energy carriers in the public utility sector, furthermore in the case of monopolistic activities that remain within the scope of authority of administrative price determination.

The electricity and natural gas markets have been operating smoothly since the opening of the competitive market. When regulations concerning the competitive markets had been issued, the requirements of European Union Directives set forth in regulations in effect at that time, or published in drafts had already been taken into account. Amendments of Directives are being applied to the statutory system of Hungary on a continuous basis and have on part been completed.

Our report provides an overview of the current status of the liberalization of the competitive markets of electricity and natural gas, as well as the operation of the competitive market.

Budapest, July 2005

Ferenc J. Horváth
President

2. Summary \ Major Developments in the last year

2.1 System of Institutions, Mandate and Organization of the Hungarian Energy Office

Legal background of the regulation of the energy market

The objectives of Hungarian energy policy were passed by the Parliament in 1993. Act XLI/1994 on gas supply (hereinafter: Gszt), Act XLVIII/1994 on the generation, transmission and supply of electricity (the former VET), as well as Act XVIII/1998 on district heat supply (hereinafter: Tszt), together with decrees associating with these laws were published following this. The Hungarian Energy Office (hereinafter: the Office) was established in July 1994. The statutory provisions mentioned above provided sufficient basis for the restructuring of the energy sector between 1994 and 1996, and the operation of a market regulated by the state.

In 2001, the Parliament passed Act CX/2001 (VET) on electricity, and in 2003, Act XLII/2003 on natural gas supply (GET) was issued, and by the 1st of January 2003 the lower level legal acts and the associating governmental and ministerial decrees were issued for the implementation of the Act of CX/2001 in order to assure the operation of the liberalized gas market. A new chapter was opened up in the regulation of energy industry companies in 2003. The liberalization of the electricity market started on January 1, 2003, and the liberalization of the natural gas market started on January 1, 2004. The electricity market gradually expands, while the competition in the natural gas market unfolds only slowly and compared to the size of the market, in a small degree.

The Ministry of Economy and Transport (hereinafter: GKM) drafted Act XVIII on district heat supply (Tszt) with the cooperation of the Office in 2004, which was passed by the Parliament in 2005, as well as the modification of the Electricity Act (VET) and the Gas Act (GET).

The Office has played and is playing a dominant role in the restructuring of the energy market, the operation of the regulated market, and later in the development of the competitive market, issuing the license for market players, regulating companies being in monopolistic positions (natural or legal monopolies), as well as in supervising the market and the gradual extension of the competitive market.

System of institutions of regulation

In the frame of secondary rules, based on legal regulations;

The Government determines

- the rules pertaining to the operation of the organized energy market,
- detailed rules of the licensing procedure, the conditions of conducting activities subject to license and of the amendment of the operating license, the detailed rules of the procedure to be followed in case of unlawful conduct of the owners of lines,
- detailed rules pertaining to the codes of licensees, the order of elaboration and reconciliation of codes, their elements of content and the scope of licensees responsible for the development of the code,

- the scope of eligible customers, the conditions and the time of becoming eligible customer,
- energy policy requirements of the establishment of power plants,
- rules of cross-border transmission of electricity and natural gas,
- the order of the utilization of social electricity supply, as well as the scope of those eligible,
- detailed rules of the legal relationship between the public utility supplier and public utility customer, mandatory elements of content of the public utility contract,
- detailed rules of the legal relationship between the network licensees and system users, minimum elements of content of the agreement pertaining to the use of network services,
- rules of access to natural gas transmission and distribution pipelines and underground gas storage facilities, the minimum elements of content of the agreement pertaining to the use of the pipeline and the storage facility,
- the general rules of the access to the natural gas system, the order of publishing available spare capacity, as well as the order of satisfying requests in case of lack of capacity,
- tasks of the natural gas system operator and the general rules of the cooperation with the licensees,
- the mandatory elements of content of the unbundling method applied by the natural gas companies pursuing activities unbundled from the aspect of accounting,
- detailed rules of the specification and management of stranded costs,
- general principles of the curtailment of district heat supply,
- detailed rules of the management of energy supply emergencies,
- the date of the introduction of the green certificate,
- detailed rules related to the foundation, content, licensing, termination, and compensation for damages pertaining to third party real estate rights,
- the upper limit of the penalty that may be imposed by the Hungarian Energy Office, the detailed rules of imposing penalties.

The Minister of Economy and Transport (hereinafter: the Minister) determines

- the rules pertaining to the publication of resolutions of the Hungarian Energy Office of public interest,
- financial and technical conditions of connecting to the public network, the amount of tariffs to be paid by customers in relation to network development, network extension, as well as the connection of customers and the rules of the procedure,
- the scope of data to be submitted in the course of price review,
- rules of data to be provided by licensees and system users, as well as the order of data to be provided by the Hungarian Energy Office based on international commitments of the country and aimed at non-governmental organizations and other organizations representing the interests of customers, and the rules pertaining to the protection of data classified as confidential,
- the scope of customers the consumption of whom is based on the electricity demand curve prepared with statistical analysis,
- the smallest extent of energy stocks of power plants with an output of 50 MW or more,
- the authority issuing the license for preparatory works and lines,
- technical safety requirements of the electricity works,
- rules pertaining to the security zone surrounding the electricity works,
- rules of technical and safety classification, provisioning, and commissioning of connection, interconnection, and customer equipment,

- detailed rules of electricity transit,
- mandatory feed-in rules of renewable electricity generated using waste, from co-generated electricity, and well as from electricity generated in other ways as specified in statutory provisions, and establishes the order of subsidizing electricity generated in this manner in agreement with the Minister of Finance,
- rules of reporting and the official inspection of serious breakdowns occurring on the natural gas transmission, distribution, and direct pipeline, as well as in storages ,
- rules of distribution of liquefied propane and butane gases and their mixtures in tanks or vessels, and the official supervision of those,
- the scope of customers the supply of which has a priority when accessing storage facilities, transmission and distribution pipelines,
- the method of defining and providing evidence to insurmountable economical and financial difficulties caused by long-term natural gas purchase agreements, as well as the rules pertaining to the distribution of burdens between natural gas market players that are a result of long-term agreements and eligible customers entering the market,
- detailed rules of the use of discount natural gas supply,
- detailed rules of the use of discount line transmitted propane and butane gas supply, resulting in actual customer prices exceeding the price of natural gas by not more than 20% under consumption corresponding to the heat value of natural gas per customer impacted by the supply of discount natural gas,
- rules pertaining to electricity supply for public lighting purposes in agreement with the Minister of the Interior and the Minister of Environmental Protection and Water,
- The amount of administrative service tariffs to be paid to the Hungarian Energy Office as well as detailed rule of payment in agreement with the Minister of Finances,
- administrative prices and tariffs, as well as the conditions of applying the prices and the tariffs, together with the framework of price regulation in agreement with the minister of finance,
- may determine a separate tariff system for the employees and retired staff of electricity industry enterprises in agreement with the minister of finances, together with detailed specification of the use,
- rules of approaching and crossing by network licensees based on line property rights, related to path facilities, rivers, streams, lakes, channels, and strictures in agreement with the Minister of Environmental Protection and Water, as well as the Minister in charge of the Prime Minister's Office,
- the organization providing technical and safety supervision,
- detailed rules pertaining to certifications issued by the Office for power plants using renewable energy or energy generated from waste, to reporting and data supply obligation of generators and small power plant operators selling green certificates, as well as to the sale and reception of green certificates.

Mandate and Organization of the Hungarian Energy Office

The Office provides for the licensing, official control and supervision, as well as customer protection tasks related to the supply of electricity and gas and district heat generation of power plant.

The Office is a public administration organization controlled by the Government, and supervised by the Minister of Economy and Transport, having its independent mandate and authorizations. The Office is a legal entity functioning as a state budget organization with own finances.

Regarding the procedures of the Office, the provisions of Act IV/1957 on administrative procedures is to be observed with the difference that the deadline of administration is 90 days. Legal remedy against the decision of the Office shall be exclusively sought in front of a Court of Law. The Court of Law has the right to change the decision of the Office.

Within the scope of its official tasks, the Office issues, amends, and revokes operating licenses in the area of electricity supply, natural gas supply, and district heat generation, approves the restructuring of licensees, the acquisition of influence in licensees, as well as changes in the value of registered capital and the codes made by licensees. It verifies adherence to statutory provisions, licenses and codes, and has the right to impose penalties upon the infringement of these.

The Office has the right for price preparation as regulated by law in the area of electricity supply, natural gas supply, and district heat generation.

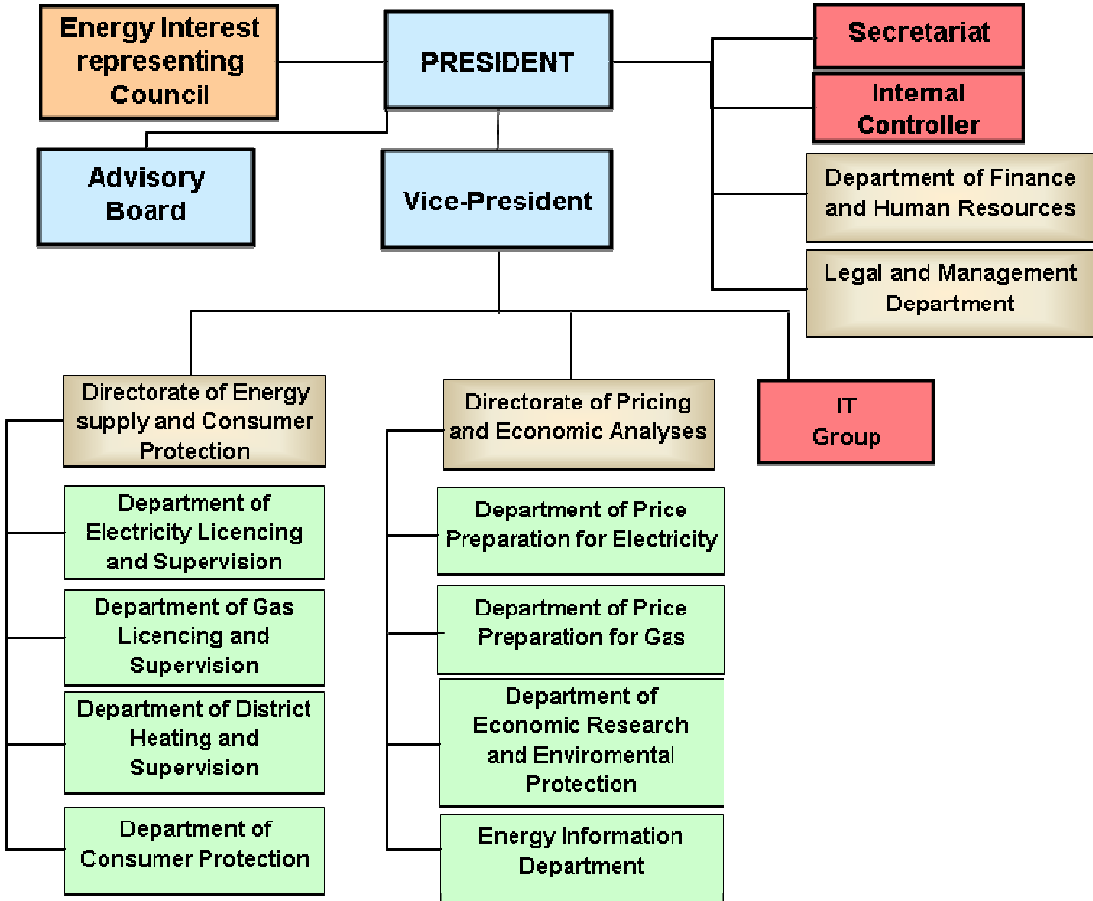
In order to enforce the interests of the customers, the Office performs consumer protection tasks in cooperation with the Chief Inspectorate for Consumer Protection and regional inspectorates. Within the framework of this, is investigates consumer complaints, and cooperates with non-governmental organizations providing for the representation of consumer interests. It verifies the quality of service in order to provide safe supply to customers.

In order to facilitate the allocation of greenhouse gas emission units, the Office provides a professional opinion to the environmental protection authority in the area of electricity and district heat supply.

Figure 1 demonstrates the organizational structure of the Office.

Figure 1

Organizational Structure of the Hungarian Energy Office



2.2 Main Characteristics of the Development of the Gas and Electricity Markets

2.2.1 Electricity market

Act CX/2001 on electricity (the VET), which was issued in 2001, was passed by the Parliament in accordance with the EU (96/92 EC) Directive in effect at that time. Partial harmony with the provisions of Directive 2003/54/EC which has been issued afterwards was ensured by amending individual sections of certain decrees (eligibility decree, decree on cross-border electricity transmission etc.). Any further required changes are contained in the amendment of the Act (and in its lower level implementation acts), which has been adopted in June 2005 and is to enter into force in September 2005.

Based on Governmental Decree 181/2002 (August 23) amended by Governmental Decree 107/2004 (April 27) on the eligibility of electricity consumers, the purchase of electricity based on free agreements has become possible for all non-residential customers as of July 1, 2003. A part of these customers, however, is not supplied with remote consumption meters equipped with registers that make schedule based settlement possible, and therefore they can only enter the competitive electricity market if their settlement can be managed. This makes it possible to perform settlement (based on ministerial decree) based on the electricity demand curve prepared with statistical analysis. Thus in accordance with the directive costfree change can be pursued.

Following the market opening on January 1, 2003, by the end of May 2003, the number of free market balance circles reached 11, while the number of eligible customers grew to 22. By the end of the first half of the year, the number of eligible customers entering the market in practice doubled. By the end of May 2004, a total of 85 eligible customers entered the competitive market, the consumption of which is 6,643 GWh on an annual level, amounting to more than 20% of the total electricity consumption of the country. Starting with July 1, 2004, providing eligibility to all non-residential customers has multiplied the number of potential market entrants. By the end of 2004, 546 eligible customers purchased at 832 customer sites on the competitive market and their overall consumption was 24.84% (8,188 GWh) of the total consumption. In the first half of 2005, 928 customers consumed 31.54% (10,810 GWh) of the total annual consumption at 1,413 consumption sites. The considerably large proportion of the already allocated capacities at the public utility encumbers the further dynamic increase. The Office has modified the Commercial Code this year for the third time, for the proposal of the system operator. The Office approved the Grid Code of the public utility supplier on July 30, 2004 and the Business Conduct Rules of the six distribution licensees on September 1, 2004.

From the point of view of the customers, the electricity system is divided into two parts: the segment supplying public utility customers, and the competitive market supplying eligible customers entering the free market.

2.2.2 Gas Market

The gas market was opened up on January 1, 2004. According to the governmental decree, eligible customers could request to be put on record until March 31, and had to confirm their intention to leave the public utility segment by April 15. Statutory extent of the opening of the market: with the exception of household customers all customers are eligible to enter the market, according to their own decision, their number is approximately 180,000, and their consumption makes up 67% of total national gas consumption. From the eligible customers only 23 decided to enter the competitive market. Their consumption is 6% of the total consumption of the country. The number of traders on the competitive market is 13, but only 3 out of those are actually conducting commercial activities. During the one year that the Hungarian gas market has been opened up, only approximately 3% of the natural gas market moved from the scope of supply of the dominant market player (MOL Földgázellátó Rt.).

The Office compiled and published the Temporary Network and Commercial Code (hereinafter: IÜKSZ) as far back as October 2003, which regulates the access to networks and storages, the schedule and the co-operation rules among the participants of the system. Based on the problems and experiences that were arisen, the IÜKSZ was modified twice during the year. Based on Governmental Decree 111/2003 (July 23) on the enforcement of certain provisions of the GET (hereinafter: GET – Vhr), the Code Committee - established from the representatives of the licensees in order to create the ÜKSZ (Network and Commercial Code) - was established after the Office had issued the operational licenses, however, they submitted the ÜKSZ, elaborated by them, to the Office for approval only at the end of 2004. It was the IÜKSZ that first stipulated that spare capacity of the transmission system and storages shall be published 15 months in advance, provides detailed rules for contracting capacity, and describes the scope of basic services provided by system operators. It identifies possible and mandatory contractual relationships of the new market structure, including not only commercial agreements, but also those of various forms of cooperation.

Market participants needed more time after the publication of the regulations to answer the interpretational problems and all the specific questions deriving from the dual hybrid market model. This regulation required the longer lasting refinement of the regulations, which did not promote the willingness of customers to enter the market. Besides, expectations of customers intending to enter the competitive market were generally excessive. When leaving the public utility segment, they were unsatisfied with the capacity provided based on the relevant decree and the IÜKSZ regulation, as well as with the rules of exit and return, submission of consumption demand, nomination and balancing, which mainly arose from the limited import possibilities (scarce eastern border capacities) and from the absence of the supply market, but it was also caused by the legal preference of the public utility sector against the customers of the competitive market.

Based on the experiences of the first year it can be stated that the opening of the market is made harder by the lack of spare transmission pipeline capacity at the „cheaper” eastern border, by the fact that 97% of gas sources playing role in the supply of the country are in one hand, the management separation, unbundling of activities at vertically integrated companies is inappropriate due to ownership interest, and that the public utility sector and the competitive market are operating simultaneously and public utilities have priority.

2.3 Major Tasks of the Office

On request of the Ministry of Economy and Transport the Office have launched analysis to determine those issues where the current statutory background needs to be refined or supplemented in order to comply with Directives. The Office considers the safeguarding of competition and the prevention of the abuse of the monopolistic situation as a key task on the energy market.

In the area of the electricity market, the Office assigns high priority to the development and introduction of the model following the complete opening of the market. We wish to amend and refine the statutory provisions, as well as to create new statutory provisions in two steps. During the first step (in 2005) regulations pertaining to the TSO, and all regulations of European Parliament and Council Directives that do not require the change of the model are to be developed and introduced as of January 1, 2006. During the second step, those stipulations of the Directives are to be developed and introduced as of 2007, which require the modification of the current dual, hybrid model.

In the area of the natural gas market, the Office considers the following as its key tasks: the amendment of GET to support further opening of the competitive market; the implementation of the market experiences of the former period in lower level statutory provisions; the continuous development of the Network and Commercial Code, including the refinement of the capacity allocation related to capacity bottlenecks, and further improvement of transparency; the development of the nomination system; and the development of the uniform system of daily commercial and hydraulic balancing.

A key task is to eliminate the bottlenecks of the national supply system based on long-term requirements.

3. Regulation and Performance of the Electricity Market

3.1 Regulatory Issues

3.1.1 General

Regulation of the Electricity Market

Hybrid model

From the point of view of the customers, the electricity system is divided into two parts: one segment supplying public utility customers using regulated final customer prices, and the competitive market supplying eligible customers entering the free market.

Public utility segment

Public utility customers automatically include all customers not yet eligible, as well as all eligible customers based on their own decision (those who do not wish to make use of their opportunities resulting from being eligible or re-enter the public utility). Public utility customers are supplied with electricity in a regulated manner, in line with statutory provisions. Public utility customers may only be supplied with electricity by the territorially competent public utility supplier (the electricity supplier before the formulation of the competitive market) at a price and quality determined by the price authority. The public utility supplier can mostly only buy the electricity required for supplying the public utility customer from the public utility wholesaler.

The electricity required to supply public utility customers is purchased by the public utility wholesaler from import resulting from cross-border electricity transmission and mainly from national generators, typically within the framework of long-term agreements. At the same time the public utility wholesaler passes the purchasing of electricity generated by small power plants to the public utility suppliers. The public utility wholesaler has the exclusive right and obligation to supply public utility suppliers supplying to end users up to the extent of compliance with the public utility contracts entered into by the public utility supplier and the public utility customer. Public utility suppliers cannot purchase energy from sources other than small power plants beside the subsidy of electricity produced of renewable source and cogeneration within the framework of obligatory acceptance.

The trade between the public utility wholesaler and the public utility suppliers, as well as the supply of the public utility customers runs at an officially regulated price.

Competitive market

Eligible customers may purchase electricity from electricity traders as well as generators with free capacities (not allocated by PPAs), or may import it from across the border. Companies active in the public utility sector (public utility suppliers performing public utility tasks) cannot be active in the competitive sector, and therefore cannot sell electricity to eligible customers who entered the competitive market. In case the public utility wholesaler in the public utility sector has excess capacities, then it has to be sold in a way (by way of auctions) that all competitive market traders have access to it.

In case if in the public utility sector the capacity required by the public utility wholesaler is bigger than the demand of the public utility costumers and this electricity is not sold as

available to everyone, this electricity can be sold at the free market but stranded cost can not be applied.

Public utility supply and the operation of the distribution network are currently being conducted within the framework of the same companies based on separate licenses. The two activities are unbundled from accounting (not organizational) point of view. The distribution licensee provides for the majority of DSO (Distribution System Operator) functions. Traders of the competitive market can only trade based upon a licence. These traders can be companies for limited responsibility (ltd) or shareholding companies having a registered headquarter in Hungary as defined in the Act CXLVI/1997 on corporations if they meet the requirements of the VET and its related implementation decrees (e.g. in case of the financial caution). The unbundling requirements (legal and management) according to the public utility supplier, distributor, TSO and public utility wholesaler are specified by the modification of the law, approved by the Parliament in June 2005.

Table 1 shows the ownership structure.

Table 1

Breakdown of the Registered Capital According to Proprietary Categories in the Electricity on December 31, 2004

Proprietors	Producers	Transmitter	Suppliers	Traders	Total (%)
Hungarian State	2.83	99.87	0.03		36.88
Local authorities	0.23	0.11	2.70		1.30
Other hungarian investors	60.56	0.02	8.09	30.05	5.90
Hungarian participation, in total	63.62	100.00	10.82	30.05	44.08
German investors	10.22		77.66	27.60	38.13
French investors	5.04		9.43		6.46
Belgian investors	9.21			37.15	4.62
USA investors	10.10			1.80	4.91
Switzerland investors	1.81				0.88
Other foreign investors			2.09	3.40	0.92
Foreign participation, in total	36.38	0.00	89.18	69.95	55.92
TOTAL	100.00	100.00	100.00	100.00	100.00

Licensing of the new installed capacities and the possibility for a tendering procedure

License has to be applied for from the Office for the establishment of power plants with an output of 50 MW and more, while the Office has to be informed of the establishment of power plants with an output exceeding 1 MW but below 50 MW. The new, modified law on electricity (CX/2001) prescribes a simplified licensing procedure for small power plants from September 2005. Conditions of licensing, and its objectivity, transparency and non-discrimination are ensured by statutory provisions. The order of proceedings and the system of requirements of licensing complies with the considerations set forth in Directive 2003/54/EC.

Since the VET entered into force on the 1st of January 2003 the Office may call for a tender to establish power plant based on the VET, if the capacity available in the country is unable to satisfy the expected electricity demand of customers on the long-term. There has not been made a call for tender yet. The VET authorizes the Government to regulate the method and conditions of the call of the tender in a decree. The Government has yet to issue this decree,

within the framework of which it will be possible to develop the conditions of the tender not regulated by law in accordance with the requirements of the EU Directive.

The Office issued a total of 256 resolutions pertaining to the electric industry in 2004. Amongst these, resolutions issued to the system operator play a key role and all regulations that were relevant to the electricity supply codes*. This is because these are the official resolutions within which the Office defined the rules of access to the public network for eligible customer based on Section e), Article 10 of the VET.

Amendments of the commercial code for the sake of the refinement of the TPA regulations

Upon the proposal of the system operator, the Office amended the commercial code three times during 2004. Resolution 309/2004 contained technical modifications approving a partial modification of former resolutions issued by the Office, stipulating the insertion of such principles (that are well known in European practice) into the regulation like the „use it or lose it” principle to be applied during transmission through contracted cross-border intersections.

In its resolution 355/2004, the Office approved the secondary trade of cross-border capacity usage rights sold by licensees at auctions – with the application of Governmental Decree 182/2002 (August 23) amended by Governmental Decree 200/2004 (June 23) on the regulation of the cross-border transmission of electricity. Based on the amendment of the decree, it became possible to modify the detailed order of proceedings regulated in the commercial code, and to limit the cancellation of capacity rights included in the current rules and regulations.

In resolution 606/2004, the Office approved the amendment of cross-border capacity allocation rules, amongst which the most important change is relevant for the Austrian section. In this instance, the system operator was able to enter into an agreement with APG (VERBUND - Austrian Power Grid AG) based on which annual and monthly capacity auctions are held by the Austrian partner for both directions, while daily auctions to be launched during 2005 will be held by the Hungarian system operator. In this resolution, the procedure related to agreements to be entered into between neighboring system operators has been defined, based on which the Office can still participate in the preparation of agreements in appropriate time and relevance, as an allocation system that is transparent and ensures equal treatment for all market players has a key role from the point of view of more efficient operation of the electricity market.

Application of load profiles

Based on the Governmental Decree 181/2002 (August 23) amended by Governmental Decree 107/2004 (April 27) on the eligibility of electricity consumers, the purchase of electricity based on free agreements has become possible for all non-residential customers July 1, 2004. A part of these customers, however, is not supplied with remote consumption meters equipped with registers that make schedule based settlement possible, and therefore they can only enter the competitive electricity market if their settlement can be managed. This makes it

* The regulation of supply is a collective notion, which involves the Grid Code, the Commercial Code, the Business Conduct Rules of distributors and the standardised distribution rules referring to all distributors.

possible to perform settlement based on the electricity demand curve prepared with statistical analysis. GKM Decree 92/2004 (July 9) on the scope of customers the consumption of whom is based on the electricity demand curve created by statistical analysis amongst other things defines the requirements of content related to supply codes, as well as the framework of application and settlement rules of profile curves. The decree has secured the costfree entry to the market.

The application of load profiles means the introduction of a settlement method never before applied in the electricity system. During the preparatory process, it has become evident that the framework ensured by the VET does not make it possible to introduce a regulation based on any EU member state's practice, without any modifications. As a result, a methodology had to be developed related to the method of settlement that can be applied without significant IT development within the framework defined by the VET and the VET-Vhr. as of July 1, 2004. This consequently resulted in defining several conditions of simplification (the limit of profiling, the settlement of the public utility supplier and the distribution network licensee, the settlement and data supply obligation of the system operator, the system of possible settlement relationships). Since the regulation was created by the coming into effect of the eligibility obligation set forth in the EU Directive, the Office amended the distribution code and the operating code in addition to the commercial code so that required changes can be introduced.

Ancillary services

Since opening the competitive market the Office was forced to postpone twice the deadline of its temporary obligations, planned until the development of the market relations, set forth in the rules of the procurement, use, and settlement of ancillary services, as well as of the calculation method of the settlement price of balancing energy. Based on the experiences of the Office, the current system of long-term agreements between the power plants and MVM Rt. (Co.Ltd.) and the legal environment in short and long term do not provide proper incentives for licensees to develop a system that is more efficient than the current system of regulated price, especially since the price of balancing energy needs to provide incentives to market players to adhere to their schedules, but the price should not prevent eligible customers from entering the market. The formulation of appropriate regulations is especially hindered by the fact that in accordance with the legal practice of the Union, the system to be established needs to ensure equal treatment for all market players, including the public utility wholesaler, who cannot share its market risks in market terms with other companies within its balancing group due to the constraints of the contractual system established prior to the opening of the markets and valid for public utilities, and due to legal constraints. During the year, technical level discussions were conducted in the commercial code committee; these are however yet to be concluded.

Management of released capacities

The rule obliges the public utility wholesaler (MVM Rt.) to free the margin between the capacities that are tied up with generators (relatively rigid), deriving from PPAs (long-term power purchase agreements) and the capacities demanded for the public utility customers by the public utility suppliers and also to sell it for the market.

The law urges the renegotiation on PPAs in order to restore long-term capacities. This initiative has yielded no results at all in the past 3 years.

The public utility wholesaler is obliged to sell the surplus capacity above its public supply obligation for at least six months on generation capacity auctions (in case of surplus for shorter period auction can be held for shorter time than six months). In the event of selling surplus capacities on auctions the public utility wholesaler can claim stranded cost compensation (if it suffered losses on it).

The law, beside the public utility demands becoming more and more accurate, obliges the public utility wholesaler to call off capacity contracted for public utility purposes, but not used by the wholesaler and therefore released, for which the Commercial Code includes its detailed regulation, especially relative to the period prior to the timely day of the renouncement. This is because it has become evident at the consultation conducted so far that due to lack of statutory obligations, relevant licensees are unable to solve the question in the commercial code, thus this capacity release does not prevail in practise.

Changes in the regulatory background

The first phase of the regulation of energy industry companies that started in 1994 following the 1993 acceptance of the energy strategy conception concluded in 2002. However, the second phase started prior to this, in 1998-99, covering the preparation for the opening of the energy market, and primarily the electricity market. In December 2001, the Parliament passed Act CX/2001 (VET) on electricity, and in 2002, governmental and ministerial decrees required for the enforcement of the Act were completed.

Based on Governmental Decree 181/2002 (August 23) amended by Governmental Decree 107/2004 (June 27) on the eligibility of electricity customers, the purchase of electricity based on a free agreement has become possible for all non-residential customers as of July 1, 2004. Rules enable exemption from the schedule based settlement for a part of this customer group, so they can enter the competitive electricity market without having an electronic distance reading meter. This makes it possible to perform settlement based on the electricity demand curve made with statistical analysis.

Decree 92/2004 of the Minister of Economy and Transport (July 9) on the scope of customers the consumption of whose is based on the electricity demand curve made with statistical analysis amongst other things defines the requirements of content related to supply codes, as well as the framework of application and settlement rules of profile curves.

Regulation (EC) No. 1228/2003 of the European Parliament and Council on conditions for access to the network for cross-border exchanges in electricity came into effect on July 1 and based on its Article 15 was to be implemented in Hungary from the 1st of July 2004 as the country became member of the European Union from the 1st of May 2004. For the sake of the legal harmonisation the Government has amended its Governmental Decree 182/2002 (August 23) on the regulation of cross-border transmission of electricity, and as a result, the Commercial Code also had to be modified several times. The allocation of spare cross-border transmission capacity has been significantly modified; market-based methods were introduced.

3.1.2 Distribution of cross-border capacities and mechanism management

Governmental Decree 182/2002 (August 23), (hereinafter: the Decree) regulates the cross-border transmission of electricity. According to the regulation, a party may be eligible to import and/or export cross-border electricity if provided with a license by the Office. Electricity may only be imported and/or exported at cross-border transmission and distribution intersections if the value of the available transmission capacity (ATC) as defined in the Decree and the Operating Code is not zero. The Distribution Code contains the detailed rules of cross-border electricity delivery on the distribution network owned by the 6 distribution licensees (called *Distribution System Operator, DSO* in the EU regulation).

In Hungary, the system operator, the ISO (*Independent System Operator*) is responsible for the allocation of cross-border capacity usage rights (MAVIR Rt.), who has the obligation of announcing the capacity usage rights for allocation at regular intervals in accordance with the Commercial Code for standardized periods in time. The system operator announces annual auctions each year, and announces monthly auctions every month throughout the year. The Decree provides detailed regulation of which capacity may be considered as already allocated capacity (AAC).

According to the Decree, the system operator has the obligation to strive to have the ATC allocated at auctions held together with system operators neighboring the Hungarian regulatory zone. If this is not possible due to a lack of agreement, the system operator distributes transmission capacity within the framework of a unilateral auction. Annual and monthly auctions pertaining to Austrian intersection are organized by the Austrian system operator, which is a joint auction. A daily auction is also held here, which is organized by MAVIR Rt*. System operators have shared the NTC values in 50-50% on other cross-border points, and ATC allocation is performed by the system operator of the country. An exception from this is the Slovakian intersection, where a mutually recognized AAC value is deducted from the NTC before capacity is divided in two.

The system operator has the obligation to announce the result of the auction immediately on its home page and provide written information to the Office regarding the result thereof. If any of the participants of the annual auction requests so within a predefined period of time, the Office reviews the auction procedure and its result. According to the resolution of the Office there was no procedural or other failure in the capacity allocation procedure for the year 2005. Table 2 shows the characteristics of the capacity auctions held in 2004.

* Due to the deficits of the developed software, the introduction of daily auctions in 2005 is being dragged.

Table 2
(MW)

ATC values for 2004

Available Transfer Capacities of the Hungarian Power System

	Relation	Auction	TTC	TRM	NTC	AAC	ATC yearly (base)	ATC monthly
IMPORT	Austria-Hungary	Auction-A1	...350...	200	100...	0	100	0...50...
	Croatia-Hungary	Auction-H1	...500...	200	250...	150	100	0...50...
	Slovakia-Hungary	Auction-S1	...1300...	200	850...	600	250	0...250...
	Jugoslavia/Romania-Hungary ¹	Auction-JR1	-	-	-	-	-	-
	Ukraine-Hungary ²	Auction-U1	450	0	425...	425	0	0...25
EXPORT	Hungary-Austria ³	Auction-A2	900	200	700	-	-	-
	Hungary-Croatia ⁴	Auction-H2	...800...	200	500...	300	200	0...100...
	Hungary-Slovakia	Auction-S2	200	200	0	-600	600	0
	Hungary-Jugoslavia/Romania ⁵	Auction-JR2	250	0	250	0	0	250
	Hungary-Ukraine ⁶	Auction-U2	-	-	-	-	-	-

Source: MAVIR - HFO

Comment:

- ATC values applied to given time.
- ATC values are in different relation.
- ATC values should not be aggregated.

- 1 Permitted by MAVIR for cooperational limits
- 2 Stability bounds
- 3 Allocated by Austrian TSO
- 4 Shared allocation with Croatian TSO
- 5 Jugoslavian and Romanian output meant together
- 6 Permitted by Ukraine for cooperational limits
- ... Redefined every month

3.1.3 The Regulation of the tasks of transmission and distribution companies

On January 1, 2003, the regulation of the administrative price system underwent a significant change when the new Electricity Act came into effect, together with a ministerial decree providing separate specification of charges for system use in one of its enforcing provisions. These created one of the fundamental conditions for market opening, which is the opportunity of transparent, non-discriminative and regulated access to the network infrastructure, which is in a state of natural monopoly. This decree specifies the administrative tariffs of the transmission, distribution, system operation and ancillary services of electricity, together with other related rules. All customers of electricity must pay these tariffs directly or indirectly.

In the current practice, a price review, which is conducted every four years and focuses on the assets of and the justification of the costs of the relevant companies represents the basis of regulation for feed-in and distribution tariffs. This was last conducted in 2004, and was the basis of a new price regulation cycle in 2005, according to the regulation on mid-term rules and the decree on prices that entered into force on the 1st of February 2005. A factor that facilitated this was that based on a legal requirement, licensees introduced the unbundling of accounting according to their activities as of January 1, 2003. The review of the justification of operating costs of network companies was conducted based on the cost data of 2003 broken down by activities. The recognized amount of distribution company losses was specified by using a benchmark analysis including regional distribution companies. When calculating the depreciation and capital costs recognized in the price, network assets were taken into account at a corrected replacement cost. This was founded by asset groups, using an individual professional review also taking the extent of wear (technical state) into account.

The amount of weighted average capital cost (WACC) is 7.1%. During the four-year price regulation cycle, administrative prices are maintained based on price formulas specified in ministerial decrees. [Regarding network licensees, this is CPI-X, where the value of X may vary between 1.8 and 2.2.] Regarding distributors, the price formulas also contain a corrective factor pertaining to the quality of service. Table 3 contains the maximum administrative prices of the certain activities related to the use of the system, while Table 4 contains average charges for system use pertaining to type customers according to EEC Directive 90/377.

Table 3, Part 1

Regulated electricity system usage charges in Hungary, excluding VAT¹

I. Charges of system operation and ancillary services (HUF/kWh) as of February 1, 2005

A) To be paid to the distributor by those connected to distribution network		
1.1	System operation charge including: - charge for stranded costs - renewable & cogeneration support - system operation costs	1.237 0.3 0.7 0.237
1.2	Charge for ancillary services	0.701

B) To be paid to System Operator by those connected to transmission network			
1.1	System operation charge including: - charge for stranded costs - renewable & cogeneration support - system operation costs	1.125 0.273 0.637 0.215	
1.2	Charge for ancillary services	0.638	
After cross-border electricity transmission		Export	Import ²
2.1	System operation charge	0	0.25
2.2	Charge for ancillary services	0	0

II. Transmission charges (HUF/kWh)

A) To be paid to the distributor by those connected to distribution network		
1.	General transmission charge	0.968

B) To be paid to System Operator by those connected to transmission network			
1.1	General transmission charge	0.881	
1.2	Charge for transmission reactive power	0	
After cross-border electricity transmission		Export	Import
2.1	General transmission charge	0	0
2.2	Charge for transmission reactive power	0	0

Table 3, Part 2

III. Distribution charge

	Distribution basic charge	Distribution capacity charge	Distribution energy charge	Distribution reactive power charge	Distribution loss charge	
	HUF/connection point/year	HUF/kW/year	HUF/kWh	HUF/kVArh	HUF/kWh	
A) To be paid to the distributor						
A1) By those taking out from distribution network (7. § (4) aa), ab) and ac) points)						
a.)	High voltage connection	155 232	552	0.16	1.74	0.2
b.)	Connection to medium voltage transformer	77 616	1 716	0.72	2.1	0.28
c.)	Medium voltage connection	77 616	3 180	1.17	2.1	0.59
d.)	Low voltage connection					
	da) I. ³	2 592	---	6.81	2.91	1.73
	db) II. ⁴	852	---	1.3	---	1.3
	dc) III. ⁵	25 872	6 120	3.28	2.91	1.73
A2) By those feeding into distribution network (7. § (4) ad) point)						
a.)	High voltage connection	0	0	0	0	0
b.)	Medium voltage connection	0	0	0	0	0
c.)	Low voltage connection	0	0	0	0	0
B) To be paid to the distributor						
B1) In case of export from the distribution network (7. § (4) ba) point)						
a.)	High voltage connection	155 232	552	0.16	1.74	0.2
b.)	Connection to medium voltage transformer	77 616	1 716	0.72	2.1	0.28
c.)	Medium voltage connection	77 616	3 180	1.17	2.1	0.59
d.)	Low voltage connection	25 872	6 120	3.28	2.91	1.73
B2) In case of import onto the distribution network (7. § (4) bb) point)						
a.)	High voltage connection	0	0	0	0	0
b.)	Medium voltage connection	0	0	0	0	0
c.)	Low voltage connection	0	0	0	0	0

Remarks

- 1.: The amending decree [6/2005. (I. 21.) GKM] that contains the tariffs was published in Magyar Közlöny No. 8/2005.
Amended (original) decree: 57/2002. (XII. 29.) GKM.
- 2.: For countries not acting in accordance with the Decree 1228/2003 EC Article 3 (according to the system operators' contracts).
- 3.: With contracted capacity less than 20 kW or not exceeding 3x32 A.
- 4.: In case of controlled consumption.
- 5.: With contracted capacity not less than 20 kW or exceeding 3x32 A.

Table 4

System Usage Fees by Customer Types

Household Customers

Type	Average System Usage Fee (EUR/MWh)
Da	64.37
Db	55.55
Dc	41.71
Dd	40.53
De	29.22

Non-Household Customers

Type	Average System Usage Fee (EUR/MWh)
Ia	60.82
Ib	59.39
Ic	48.57
Id	24.49
Ie	22.45
If	13.96
Ig	13.71
Ih	13.79
Ii	13.67

Assuming an exchange rate of 245 HUF/EUR.

The Hungarian Energy Office makes the review of assets and costs of the Independent System Operator (ISO) which is 100% state-owned. The charge for system use (which separately includes the stranded cost payment, and furthermore the tariff component serving the support of renewable and co-generated generation of electricity) as well as the tariff of ancillary services is defined separately by the minister acting as the price authority each year. A change is expected in this area during the years to come, as we are striving to introduce a price cap type of regulation spanning several budget cycles regarding certain cost components during the years to come in order to provide incentives for more efficient budgeting. The higher capital intensiveness of the Transmission System Operator (TSO), which is to be established, will provide the appropriate background for such a type of change.

The regulator (HEO) plays a price preparatory role in the determination of tariff components (makes a proposal), tariff components are determined by the Minister of Economy and Transport (in accordance with the Minister of Finance) in a decree. The tether of the minister to precise the administrative prices of electricity supply and its conditions is based on the LXXXVII/1990 Act.

3.1.4 Unbundling of activities

System Operator

Regarding the transmission system operator, Hungary has opted for the ISO (Independent System Operator) model. According to this model, the company performing system operation activities is legally unbundled from the transmission licensee company, which owns and maintains the transmission network. Despite the fact that both companies performing these

activities (transmission and system operations) are state owned, ownership, functional, management and accounting unbundling requirements are fulfilled regarding the system operator by the assignment of functions to various state organizations. A single transmission system operator is in operation in the country. Article 102 of the Electricity Act (VET) contains the legal unbundling requirements, while Article 22 of the Enforcement Decree (Vhr) contains the requirements for functional and management unbundling (managers of the system operator may not be leading employees at other enterprises performing electricity industry activities, or at large customers, and they may only acquire ownership in such enterprises to a limited extent). The current regulation is mostly aimed at defining the details of the unbundling of accounting. The VET accordingly contains a separate chapter for the unbundling of activities (Chapter VIII, Articles 101-102 of the VET, Article 90 of the Vhr). The modification of the law that has been accepted by the Parliament in June 2005 keeps the two separate license notions, however, requires the legal unbundling between the system operator and the transmission licensee.

The quoted modification of the law along with the Government Decree that is under preparation, aims at the introduction of the rules for unbundling the market activities from the commercial ones, relative to the transmission and distribution system operators, which rules are also included in the EU Directives.

Distribution companies

Each of the 6 network licensees (Distribution System Operators, DSO according to the EU regulation) is a part of a vertically integrated company, without any drivers for legal unbundling for the time being. Statutory provisions in effect in 2004 do not contain rules of legal and/or functional unbundling for network companies (on the contrary, employees of traders on the competitive market may not be employed by network companies and may not be leading officers in those – Section (5), Article 90 of the Vhr). Companies comply with the mandatory rules of unbundling according to the statutory provisions as described in the section “System operator”.

Physical unbundling of each activity

The current ISO is also unbundled physically (headquarters, office building) from all other activities of the electricity industry. The system operator is currently not part of a vertically integrated company.

DSOs are generally in the same office building as the organizations performing various commercial activities (public supply or supply at regulated prices and competitive trading supply). The staff, assets and facilities belonging to a department (organizational unit) performing network activities are generally in the same area within the building or site, separately from the facilities of commercial activities, however it cannot be declared as complete physical unbundling.

Independent representation toward third parties

Due to the ownership unbundling, the ISO operates on the market with an independent name and image. Companies performing (also) DSO activities show independence in their communication towards third parties. They are using the name of the vertically integrated

company, with the same image, and without any independent website. It happens frequently that the same employee is representing both the network and the commercial organization at industry level meetings.

Publication of accounting reports

ISO, DSO-s: Activity reports created based on the Electricity Act in effect (unbundled accounts, balance sheets and financial statements) are published in a manner accessible to all third parties in the annex to the annual report of the company.

Rules of financial unbundling

Following technical level reconciliation conducted with companies, the national regulatory authority issued a non-binding Guideline (HEO Guideline 1/2002 (December 31) on the financial unbundling of enterprises of the electricity industry. In practice, all companies compile their own activity reports according to an internal accounting regulation, which is prepared based on asset and cost allocation rules specified in that Guideline.

Auditing of activity reports

Since activity reports are the part of the annual accounting report, the audit obligation pertaining to the annual report in line with the Accounting Act of Hungary also pertains to the activity report. The audit only covers whether the activity reports is compiled according to the rules of unbundling specified by the company - in line with the accounting provisions of Hungary in effect. The auditor does not issue any statement regarding the compliance of the applied rules of unbundling with the regulation of energy industry, which is whether cross-financing between certain activities may have occurred in the course of unbundling.

Sanctioning options

Since the rules of unbundling are set forth on a statutory level, all tools of sanctioning are available in practice to be imposed in the case of the violation thereof (warning, penalty, and withdrawal of license).

3.2 Competition Issues

3.2.1 Description of the wholesale market

According to the Electricity Act (VET), public utility customers are supplied by the public utility suppliers who are themselves supplied by the public utility wholesaler, MVM Rt. In theory, other traders could also be wholesalers on the liberalised market, but since it is MVM that is in possession of the vast majority of power plant capacity due to long-term agreements (approximately 80 to 85%), thus until this capacity allocation situation does not change, the other traders can acquire a role only on the wholesale market in a small market segment and mainly through import capacity.

MVM Rt. may sell at public auction the contracted generation capacity corresponding to the drop in public utility consumption that is due to eligible customers entering the market and it can reclaim the related stranded cost. In 2004, 1,052 billion kWh was auctioned, representing „stranded” costs to MVM Rt. counted with a cost of HUF 9 per kWh (3.67 Eurocent/kWh).

Public utility customers are supplied by public utility suppliers, who in turn purchase most of the electricity required for this purpose from MVM Rt. The rest of the energy is purchased within the framework of obligatory acceptance. This in effect can be considered as a „retail” deal, but on a market with administrative prices.

The organised wholesale market does not function (no organized power exchange exists).

3.2.2 Description of the retail market

As a first step, the Governmental Decree, which regulates the degree of the eligibility of the electricity costumers, opened up the electricity market on the 1st of January 2003 to 33-35 percent of the domestic electricity use, and then provided the opportunity of free purchase to all ‘non-household’ customers as of July 1, 2004, in accordance with Directive 2003/54/EC of the European Parliament and Council of June 26, 2003 concerning common rules for the internal market in electricity. The two-level eligibility ensured the opportunity for approximately three hundred and fifty thousand customers to enter the competitive market. The first year brought about lively changes on the market.

By the end of May 2003, the number of free market balance circles has reached 11, while the number of eligible customers grew to 22. By the end of the first year, the number of eligible customers that entered the market doubled, primarily due to the fact that there were trade licensees who scheduled their contracts with several market entrants being in similar situation in a manner that it could optimize the starting portfolio to the highest extent possible, thereby reducing commercial risks. The rest of the year brought about a slow rise and typical stagnation regarding the registered eligible consumption sites. Starting with January 1, 2004, the process temporarily temporarily (for one-two months) reversed, and a lot of customers returned to the public utility segment from the competitive one. Since the spring of 2004, the number of entrants to the market has once again been on the rise, and by the end of 2004, 546 eligible customers at 832 consumption sites purchased on the competitive market, representing 25% of the total national energy consumption. By the middle of 2005 the willingness to enter the market further increased; at 1413 consumption sites 928 customers represented 31.54% of the total national energy consumption on the competitive market.

Practically, all customers of above 100 GWh have entered the market, while in the case of smaller ones, the willingness to do so decreases linearly, and shows a strong correlation with the voltage level. According to experience gathered so far, eligible customers are applying a very careful and risk aversive strategy, and most of them have signed full supply based agreements, which stipulates the obligation of customers to submit schedules. From this point of view, the commercial code has a sufficient level of flexibility to allow trade licensees to create appropriate contract structures.

Starting with July 1, 2004, the eligibility of non-household consumers multiplied the number of potential market entrants. Most eligible customers, those who have not left public utility supply, are however fundamentally small customers where the installation of remote consumption metering is not economical. Load profile based measurement and settlement

provides a cost effective opportunity for these customers to participate on the competitive market.

The most important experience is that a vital precondition for eligible customers to enter the market was the liberalization of import, as this is what made it possible for them to purchase electricity at a competitive price. The explicit auction method of cross-border capacity, which is in line with international practice, created a framework since 2003, which represented a foreseeable import opportunity for customers.

Market building strategies applied by traders were considerably different. Four very different strategies could be identified. There are companies that concentrate exclusively on the largest customers where planning is relatively easy, thereby complementing their intensive commercial activity. This at the same time also means that the active trading was reinforced by an extensive international (typically Central European) portfolio. DSO network investors with properties in Hungary also established their trading companies on the competitive market. These companies are characterized by gathering their own customers entering the free market only from the public utility supplier, which belong to one ownership structure, but do not generally supply customers located in the area of a network licensee belonging to another interest group. According to the information of the Office, only one of the three relevant commercial licensees is conducting a practice, which includes the supply of both medium and high voltage customers. Activities of investor groups on the competitive market is presumably strongly influenced by the fact of whether the owner has a Central European portfolio from the EU member states that can provide efficient support for supplying domestic eligible customers with imported energy (this is required in the absence of the necessary national free capacity supply). There are two power plant investors that have established trading companies on the competitive market, but these companies had in practice been idle, which was however no surprise. This is because the generation capacity of licensed power plants is mostly contracted in long-term agreements in the portfolio of the public utility wholesaler. In aware of the current regulation, this naturally does not mean that it would not be possible to sell spare capacity possibly available in these units on the competitive market. From the point of view of the market, the unsold capacities naturally count as a failure. However, following an in-depth analyses it is evident that it is presumably more profitable for power plants to leave their spare capacity unsold than to commit it to a settlement system based on the submission of schedules and imposing „penalties” for any deviation from them, since this would be the only way to separate sales belonging to the public utility balance group from those belonging to other balance groups.

Therefore, traders can be classified into two groups from the point of view of growth. The majority has opted for gradual growth, convincing eligible customers of the advantages of switching with intensive work, practically one by one. There was a company that did not choose this path. During the first half of the year, it organized a portfolio that could be safely supplied by it, and only appeared on the market as of July 1, 2003. It was an interesting to see that as of January 1, 2004, those who returned to the public utility segment and then again to the free market, were mainly the customers of this trader.

Market price trends played a dominant role in the activities of market players. From this point of view, the processes of 2003 were unfavorable. The price of electricity that could be purchased from abroad soared. The public utility end-consumer officially regulated prices that were announced for „non-residential” consumers in 2004 and at the beginning of 2005,

provided an indirect impetus for the large and middle consumers to stay in the competitive market and also to enter the market in case they „find” a trader with free capacities.

3.2.3 Measures to avoid abuses of market dominance

The Office supervises the mechanisms managing the congestion of capacity within the electricity system, as well as the activity of transmission and distribution licensees related to the repair of breakdowns. It examines new information made public by the system operator regarding the use of interconnections, usage of the network, and network capacity allocated to stakeholders, regarding the actual unbundling of accounting by activities, as well as the conditions of new generators connecting to networks. In the case of the system operator, it monitors compliance with prescribed statutory provisions, codes and the requirements specified in the license. In addition to its mandate to monitor, it performs licensing activities in the area of the electricity and gas industry as well as district heat supply, approves electricity supply codes, business conduct rules of licensees, defines administrative prices and tariffs, may call for tender to establish power plant, and provides consumer protection tasks. Several statutory provisions ensure that the actions of the Office are non-discriminative (in general, Act IV/1957 on state administration and the VET, GET, and Tszt.)

The Competition Authority is responsible for the official monitoring of the competition (ex post).

4. Regulation of the natural gas market and implementation of the regulations

4.1 Regulatory Issues

4.1.1 General

The domestic natural gas consumption amounted to 14.5 billion m³ in 2004. The proportion of natural gas is 45% within the balance of primary energy carriers. The gas consumption ratio of households is 32.3%, while the ratio of natural gas used for the generation of electricity is 25.5% within the total amount of gas consumption.

Statutory extent of the market opening: all customers are eligible with the exception of household customers, their number is approximately 180,000, and their consumption makes up 69% of total national gas consumption. 23 such customers switched to the competitive market from the circle of public utility consumers with officially regulated prices. Eligible customers on record consumed 837 million m³ of natural gas, which amounts to 5.8% of the total amount used.

During the year of the Hungarian gas market opening, only approximately 3% of the natural gas market has moved from the scope of supply of the dominant market player (MOL Földgázellátó Rt.). The number of traders on the competitive market is 10, but only 3 out of those are actually conducting commercial activities. One eligible customer on record procures the natural gas supply that it requires on its own.

The rate of development of the competitive market in the future primarily depends on whether appropriate regulations' incentives can be implemented for the sake of free capacities and natural gas resources for customers in the competitive market. This rate cannot be estimated at this time. The internal resources, cross-border capacities and import sources are almost fully allocated by the public utility wholesaler who – contrary to the electricity market – releases neither capacity, nor resources for the customers who are willing to enter the competitive market.

4.1.2 Management and allocation of interconnection capacity and mechanisms to deal with congestion

Import arrives to the country through the pipelines called „Testvériség” (Brotherhood, from Russia and the Ukraine) and the HAG (from Austria). Their maximum capacity is 30 and 12 million m³/day respectively. Spare capacity only exists on the HAG pipeline. During the peak winter day in the years 2004/2005, the maximum consumed import capacity was 38 million m³/day. Capacity shortage occurs on the pipeline „Testvériség”, since demand at its intersection exceeds the available capacity. So far, capacity has been allocated by using capacity auction. Rules of the auction are included in the ÜKSZ.

On one hand the congestion of cross-border capacity is the result of the fact that eligible customers entering the market are due the capacity formerly provided to them in the public utility structure in the virtue of the governmental decree. Their capacity, however, was taken into account simultaneously in the public utility structure, which cannot be taken by them to

the competitive segment according to the currently effective regulations. On the other hand, these customers can primarily buy cheaper natural gas via the pipeline „Testvériség”. The third reason is that based on the price and tariff structures, these major industrial customers prefer import to storages.

Following the introduction of the Entry/Exit system of tariffs in 2005, the demand for cross-border capacity is expected to decrease, since the new system of tariffs will provide incentives to system users for better management of Entry capacity and making use of the opportunities provided by simultaneousness.

The annual development plan of the supplier contains the establishment of a third import feed-in. However, the decision regarding its implementation is expected following the submission of the development guidelines to be elaborated by the Office at the end of 2005. The pipeline would branch off from the transit pipeline in Slovakia.

The preparation of the Nabucco pipeline, designed for transmitting natural gas to Europe from Central Asia is also on the agenda. The related decision may also have influence on the concept of expanding import capacity.

According to the stipulations of the ÜKSZ, the natural gas transmission company has to publish on its homepage the available capacity for the following 12 month in a monthly breakdown at feed-in and off-take points of the network. The natural gas transmission company has to publish on its homepage the annual maintenance plan of the interoperable natural gas system by February 15 each year.

4.1.3 The Regulation of the tasks of transmission and distribution companies

There is one company operating the national transmission pipeline and 11 regional distribution companies.

According to the stipulations of the GET, licensed system operators and system users are to ensure the conditions of normal supply, and the execution of this regulation is to be monitored by the Office, which is mandated the system management tasks. There is currently no regulation that would also define quantifiable conditions assigned to the threshold of normal supply, and therefore management is carried out by the Office with the involvement of experts, but based on its own criteria. If required, the Office has the right to announce a tender for carrying out development deemed necessary, but not undertaken by the operators of the system. Although according to the statutory provisions, the development guidelines to be created every two years are to be created by the Office for the first time by the end of 2005, the Office carries out continuous assessment of the situation of the security of supply.

There is no new transit agreement. Current regulation does not cover transit transmission. The transmission pipeline entry capacity reserved for transit amounts to 22% of the total entry capacity.

Balancing

The rules of balancing is set forth within the ÜKSZ (network and commercial code), which is to be created and maintained by the Code Committee consisting of licensees, and approved by the regulating authority.

All parties eligible for access (network users) are to balance all their feed-in and off-take on a daily level. There is a single natural gas transmission licensee in Hungary, and the whole of the transmission system forms a single balancing area. In addition, all interconnected distribution networks connected to gas off-take stations stations form a separate balancing area.

The transmission system has two tapes of tolerance intervals depending on whether the party eligible for access (network user) has offered optional gas or not. If not, then the difference between total feed-in and off-take cannot exceed 2%. In case optional gas is offered (positive and negative options are both possible), the highest allowed difference is 8%. There is no tolerance interval in the distribution systems.

If the off-take of the party eligible for access (network user) exceeds its feed-in, balance is restored using balancing natural gas, which he must purchase at 1.25 times the price. In case feed-in exceeds off-take, the system operator purchases the gas unnecessarily fed into the system at a balancing price of 0.75 times. In addition, a balancing surcharge of 0.1 Ft/MJ (approximately 0.4 EUR/GJ) is to be paid for any difference exceeding the tolerance interval.

Settlement process on the transmission system:

- Daily operative data supply by 2 PM on the day following the gas day in connection with the balance of the gas day source consumption, the balancing surcharge, the amount and price of each gas item used for the balancing of feed-in and off-take, and their value.
- Preliminary monthly data supply by 9 AM on the third working day following the closing of the gas month in connection with the accumulated balancing surcharge and the total value of items used for settling the difference between feed-in and off-take.
- Final settlement by the 15th of the month following the closing of the gas month, followed by invoicing on the next day, as well as the sending of a credit entry notice to those eligible for access (network users).
- In case of an error in settlement, the party eligible for access (network user) may initiate a review and correction of the settlement at the system operator within 5 working days.
- The system operator sends a corrected settlement/data supply to those eligible for access (network users) or refuses correction in a written reasoning operator within 5 working days.

The ÜKSZ is to contain information related to the mechanism of crediting. The ÜKSZ is a public regulation also published on the home page of the Office and licensees.

The opening of the market carried out on January 1, 2004, brought about significant changes in the administered price system. Before that time, only public utility prices existed that had been paid for „complex” gas supply, consisting of two components (performance fee and gas tariff, or basic fee and gas tariff) in all sales categories, which also covered the costs of system

use that had not been unbundled. See table 5 for the natural gas system use charges. The Office plays a price preparatory role in the definition of tariff components (makes a proposal), tariff components are determined by the Minister of Economy and Transport and published by him in a decree.

Table 5, Part 1

**Administrative (maximum) Charges for Natural Gas System Use (excluding VAT^{1/})^{2/}
as of July 1, 2004**

1. Transmission tariff^{3/}

Transmission capacity charge		Transmission energy charge
To be paid by the public utility wholesaler	To be paid by eligible customers	
HUF/m ³ /day/year	HUF/m ³ /h/year	HUF/m ³
502.4	10 580	0.536

2. Distribution tariff^{4/}

System users subject to paying charge	Distribution lump sum charge	Distribution standing charge	Distribution standing charge	Distribution capacity charge	Distribution energy charge
	HUF/m ³	HUF/year	HUF/m ³ /h/year	HUF/m ³ /h/year	HUF/ m ³
Customers with no gas meter	9.12				
Customers with gas meter < 20 m ³ /h		3 144			7.31
Customers with gas meter 20-100 m ³ /h			2 073		12.35
Customers with contracted capacity 101-500 m ³ /h				11 892	5.77
Customers with contracted capacity above 500 m ³ /h				11 892	0.41

3. Storage tariff^{5/, 6/}

a)

Injection charge	Withdrawal charge
HUF/m ³	HUF/m ³
1.2661	0.582

b) Determination of mobile storage charge and peak storage charge is as follows:

(i) $TM = 3.36 * cm^{0.48}$ [HUF/m³]

(ii) $TCS = 151.1 * cm^{0.48}$ [HUF/m³/day/year]

where: TM: mobile storage charge (HUF/m³)
TCS: peak storage charge (HUF/m³/day/year)
cm = 100 * cs / m
cm: 100 million m³ based peak / mobile capacity contract of the customer entitled to access
cs: peak storing contract (m³/day) of the customer entitled to access
m: mobile storing contract (m³) of the customer entitled to access

Remarks:

- 1/. 15% from January 1, 2004
- 2/. The indicated prices are specified in the amending decree 90/2004. (VI. 26.) GKM on the modification of the ministerial decree 70/2003. (X. 28.) on the determination of charges for natural gas system use.
- 3/. In the case of captive customers - up to the proportion of the load of the interoperating natural gas system by captive customers - the public utility wholesaler pays the transmission charges (including system operation charges) to the transmission licensee.
- 4/. In the case of captive customers - up to the proportion of the load of interoperating natural gas system by captive customers - the public utility supplier pays the distribution charges to the distribution licensee.
- 5/. Eligible customers have negotiated access to storage (they are excluded from the scope of administrative pricing).
- 6/. In the case of captive customers - up to the proportion of the load of the interoperating natural gas system by captive customers - the public utility wholesaler pays the storage charges to the storage licensee. The charges paid by the public utility suppliers to the public utility wholesaler cover the transmission and storage charges paid by the public utility wholesaler to transmission and storage licensees as well.

On January 1, 2004, the ministerial decree determining charges for system use came into effect, creating one of the fundamental conditions for the opening of the market, which is the opportunity of transparent and non-discriminatory access to the infrastructure being in a state of natural monopoly. Charges for transmission and system operation, distribution, and storage carried out in the interest of public utility are therefore administered charges. These tariffs are paid by eligible customers on the record who ate otherwise not procuring natural gas at administered prices as a separate tariff (storage tariffs are subject to negotiations and are not regulated).

In accordance with this,

- transmission (including system operation) and storage tariffs are paid by
 - eligible customers on the record,
 - traders (in the name of [on behalf of] eligible customers on the record),
 - the public utility wholesaler,
 - the producer of natural gas, and
 - the system operator;
- distribution fees are paid by
 - eligible customers on the record,
 - traders (in the name of [on behalf of] eligible customers on the record),
 - public utility suppliers,
 - the producer of natural gas, and
 - the system operator.

In the current model, the regulation of transmission and distribution tariffs is carried out by price regulation cycles with the review of the assets and the reasoning behind the costs of relevant companies. The returns calculated for the net value of invested assets is a price calculation factor, which is in addition to justified operating and depreciation costs. The return rate is calculated based on domestic, risk free future yields and industry-specific risk premiums. The starting price preparation, which follows the review of assets and costs is followed by a price cap type of price maintenance mechanism spanning several years. On the tariff determination side, current incentives provided to customers for performance management are performance and basic tariffs depending on contracted capacity, as well as sanctions related to performance-exceeding.

See table 6 for the tariffs to be paid for the transmission and distribution of standard customers defined by EUROSTAT.

Table 6

Estimated national average network charges for the most recently available period corresponding to the "typical" customers:

Customer Type				
Annual Consumption		116300	116	23
Transmission		1.35	1.47	1.47
Distribution		1.43	3.17	3.17

Assuming an exchange rate of 250 HUF/EUR.

I4-1 116 300 MWh load factor 250 days, 4000 hours

Based on a statutory requirement, licensee companies introduced an unbundling of accounting based on their activities as of January 1, 2004. During the price regulation cycle, administered prices are maintained based on price formulas set forth in ministerial price regulation decrees.

4.1.4 Access to storage, linepack and other ancillary services

A regulated TPA exists for the public utilities, and one agreed by negotiations exists for the competitive market, and therefore regulated access is predominant due to the dominance of the public utility sector. There is no exemption from the TPA.

Underground gas storages have been established in worked-out natural gas fields, and are owned by MOL Földgáztároló Rt. Specifications of the five Underground Storage (UGS) Facilities:

	Working Gas million m ³	Withdrawal Capacity million m ³ /day
Hajdúszoboszló	1400	19.2
Kardoskút	180	2.3
Puszttaederics	330	2.5
Zsana	1300	18.0
Maros-I	150	2.2
Total	3360	44.2

Services offered for the integrated storage: seasonal firm, virtual firm, and seasonal interruptible. Interruptible peak storage capacity can only be contracted if all firm has been contracted and only for a party eligible for access (network user) who has previously also contracted firm capacity. Capacity can also be contracted for periods shorter than one year. Interruptible capacity can only be contracted for a maximum of one year. Unloading is only possible during the unloading season and loading is only possible during the loading season. Any demand different from this can be satisfied using virtual storage. Daily flexibility is limited by reservoir mechanical properties. The highest speed of the increase and decrease of unloading performance is published by the storage licensee on its home page.

In the case of capacity overbooking, the Vhr determines the order that new demand is satisfied in. According to this, the demand of the system operator and household customers has priority. This is followed by the demand on behalf of non-household public utility customers, followed by long term contracting, and finally by other demand on the competitive market. All customers are eligible with the exception of household customers. Capacity may only be contracted upon justified customer demand. The starting point for most of the agreements are regulated tariffs and tariff specification of the public utilities.

According to the governmental decree on eligibility, the storage capacity that was provided to entrants of the competitive market prior to switching shall be made available to them. From amongst customer that have switched, major industrial customers only made partial use of this right, as they had been able to replace a part of storage with import at better prices.

New entrants of the market contracted approximately 1% of total unloading capacity, and approximately 2% of mobile capacity. There is no secondary trade. Contracting of capacity and nominations are carried out in terms of the total storage. All the storage belongs to the same single transmission-line balancing zone. The development of the transmission system had been carried out in harmony with the development of underground storages. Therefore, the products that may be offered by the operator of the storage can be received by the transmission system. There is close cooperation between the two operators.

4.1.5 Unbundling of activities

General rules and information

Transmission System Operator

The transmission system operator in Hungary is a legally unbundled company of a vertically integrated natural gas industry enterprise (covering two activities for the purposes of licensing: transmission and system operation). Legal unbundling is mandatory according to Section (1), Article 8 of the Act on Natural Gas Supply (GET). A single transmission system operator is in operation in the country. Based on Article 6 of the Vhr., the transmission system operator activity is to be conducted in a separate organizational unit and within the course of an independent decision making process. Leaders of system operation may not participate in conducting other natural gas industry (licensee) activities either directly or indirectly. Regarding the flow of information, the system operator is to treat natural gas activities belonging to its sphere of ownership equally with other actors on the market. Article 51 of the GET, Article 35 of the Vhr., and Attachment 6 to the Vhr. contain the general rules of the unbundling of accounting.

Distribution companies

All distribution licensees (Distribution System Operators, DSO according to the EU regulation) are a part of a vertically integrated company, without any drivers for legal unbundling until July 1, 2007. According to Article 6 of the Vhr, leaders of the vertically integrated distributors may not participate in other natural gas industry activities, and the opportunity for independent decision-making is to be ensured for them. Companies are subject to the mandatory rules of unbundling of accounting according to the statutory regulation described for the transmission system operator. The rule of law does not require legal unbundling between the distribution, the public utility and the competitive market trade activities.

Physical unbundling of each activity

The current TSO is also unbundled physically (headquarters, office building) from all other activities of the natural gas industry.

DSO-s are generally in the same office building as the organizational units performing various commercial activities (public supply or supply at regulated prices and competitive trading supply). The staff, assets and facilities belonging to a department (organizational unit) performing network activities are generally in the same area within the building or site, separately from the facilities of commercial activities, but there is no complete physical unbundling to speak of.

Independent representation to third parties

In addition to using the name of the parent company, the TSO also uses the name „Natural Gas Transmitter", but lacks an individual image on the market.

Companies (also) performing DSO activities show practically no independence in their communication aimed at third parties. They are using the name of the vertically integrated

company, with the same image, and without an independent website. Frequently, the same employee is representing the network and commercial organization at industry level meetings.

Publication of accounting reports

TSO, DSO-s: Activity reports created based on the Natural Gas Supply Act in effect (unbundled accounts, balance sheets and financial statements) are published in the supplement to the annual report of the company in a manner accessible to all third parties.

Rules of unbundling of accounting

Following technical harmonization with the companies, the international regulatory authority did not issue a mandatory set of rules pertaining to the unbundling of accounting. Attachment 6 of the Vhr. contains the principles of unbundling the accounting of activities, the requirements set forth regarding unbundling, and the mandatory elements of content of the unbundling method. Based on these rules, companies establish their own detailed rules of allocation of assets and costs independently.

Auditing of activity reports

Since activity reports are the part of the annual accounting report, the audit obligation pertaining to the annual report in line with the Accounting Act of Hungary also pertains to the activity report. The audit only covers the fact whether activity reports had been created in line with the rules of unbundling set forth by the company in line with the accounting provisions of Hungary in effect. The auditor issues no statement regarding the compliance of the rules of unbundling applied with the rules of the energy industry that is regarding whether cross-financing of certain activities may have occurred during unbundling.

Sanctioning options

Since the rules of unbundling are set forth on a statutory level, all tools of sanctioning are available in practice to be imposed upon the violation thereof (warning, penalty, withdrawal of license). The vertically integrated company has the obligation to set forth its rules pertaining to the unbundling of functionality and management in an internal regulation. Any breach of these rules by an employee is classified as a grievous breach of the agreement according to the Vhr., triggering the legal consequence of the termination of legal relationship. The violation of functional and management rules of unbundling is classified as a grievous breach of the law when regulator penalties are imposed (Section (5), Article 6 of the Vhr.).

See table 7 for the ownership structure of natural gas industry companies.

Ownership structure of natural gas industry companies as of December 31, 2004.

[%]	Transmitter	Storage	Distributors	Traders
Domestic	100.00	100.00	32.05	90.28
State			5.64	
Settlement			18.54	
other*	100	100	7.87	90.28
Foreign	0.00	0.00	67.95	9.72
German			35.03	
Austrian			2.21	
French			19.25	
Italian			9.43	
English				1.36
Russian				0.82
Swiss			1.76	
Cyprian				7.54
other			0.27	

* Foreign institutional investors and domestic shareholders.

4.2. Competition Issues

4.2.1 Description of the wholesale market

In 2004, national consumption of natural gas amounted to 14.5 billion m³, covered by 11.5 billion m³ of import (80%) and 2.9 billion m³ of domestic production (20%). 90% of imported natural gas originated from Russia, and 10% from Turkmenistan. Distribution of import suppliers: Russian (83%), German (6%), Swiss (6%), French (4%), and Turkmenian (1%).

A single company is responsible for 97% of natural gas sales. The three companies with the highest share have the following share of the market: 96.74%, 2.78%, and 0.48%. The complete gas production capacity is allocated to a single company. Distribution of import capacity between the three companies with the highest share: 95.43%, 3.71%, and 0.86%.

The Hungarian gas market is a national market. From amongst member states, there is a line connection to Austria, on which the supply of import is conducted by suppliers other than Austrians. The procurement and sale of all natural gas is carried out based on long-term agreements.

Gas procurement data is not public, but the regulating authority has the right to view agreements, too. Strict capacity allocation rules are in effect covering all market players. The authority has temporarily suspended nomination sanctions valid for daily gas traffic, so as to help a nomination practice be established.

4.2.2 Description of the retail market

Public utilities amount to 94% of the retail market, while the competitive market amounts to 6%. The public utility market is location dependent. Public utility supplier may supply gas in settlements and districts specified in their license. These settlements are generally located in geographically coherent regions, typically bordered by county borderlines. The public utility wholesaler supplies customers directly connecting to the remote pipeline system as a public utility supplier. Competitive traders are not location dependent. A single, very large industrial customer switched to the competitive market, which procures natural gas for itself.

As a result of the above, the retail market is not characterized by competition today, the proportion of market players does not reflect a competitive situation in the supply of each customer group, but rather only the historic regional distribution reflecting the situation prior to the opening of the market, and the regional distribution of customer groups.

There are seven supply companies with a market share exceeding 5%.

The largest players in providing for power plants are MOL Földgázellátó Rt., FŐGÁZ Rt. and TIGÁZ Rt. (with a share of approximately 65%, 20%, and 10%, respectively).

Regarding the supply of household and small retail customers, TIGÁZ Rt. has 35%, ÉGÁZ-DÉGÁZ Rt. has 23%, and FŐGÁZ Rt. has a 21%- share. These market shares corresponding to medium sized industrial and commercial customers are: TIGÁZ Rt. 28%, ÉGÁZ-DÉGÁZ Rt. 26%, and FŐGÁZ Rt. 22%. These market shares corresponding to large and very large industrial customers are: MOL Földgázellátó Rt. 48%, FŐGÁZ Rt. 16%, and TIGÁZ Rt. 13%. Foreign ownership amounts to 63.5% in supply companies.

Eight retail supply companies have no subsidiary relationships with supplier and distribution companies.

MOL Plc. is the largest producer of natural gas. One of its 100% owned subsidiary, MOL Földgázellátó Rt, the largest importer, which is also one of the largest public utility supplier companies, also supplies large public utility customers directly supplied from the transmission pipeline.

During the past 12 months, the number of eligible customers who had been put on record amounted to 2. Since the opening of the market on January 1, 2004, a total of 25 eligible customers have switched from the public utility. Their annual consumption amounted to 837 million m³, which is 5.8% of the national consumption for 2004.

5. Security of Supply

5.1 Electricity

Security of electricity supply

One fundamental requirement of the opening of the market is for the security of electricity supply not to be endangered on the short or the long term. The energy carrier stocking decree pertaining to generators of 50 MW or more served this purpose. This stipulated a normative stocking obligation required for an 8-day schedule during the year of introduction. As of October 2004, this had been extended by another 8 days, called the security stock. However, these stocks may only be used upon permission by the system operator and the Office.

Longer term problems with the security of supply may arise if the regulatory environment (and the price that occurs of it) does not provide incentives to market players for carrying out power plant and/or network development investments of a required amount. The Office is submitting a proposal to the Minister for increasing incentives. In case when the increasing of incentives does not yield a result, there are rules that apply. According to this, the system operator creates a medium and long term capacity assessment based on its measurements and market information, and sends this to the Minister and the Office. Following this, if the Office, on the basis of a long-term estimation and adding the information received in connection with the power plant licences, is of the opinion that the extension of generation capacity on a market base is not ensured for supplying customer demand and ensuring the required reserves, a bid may be announced.

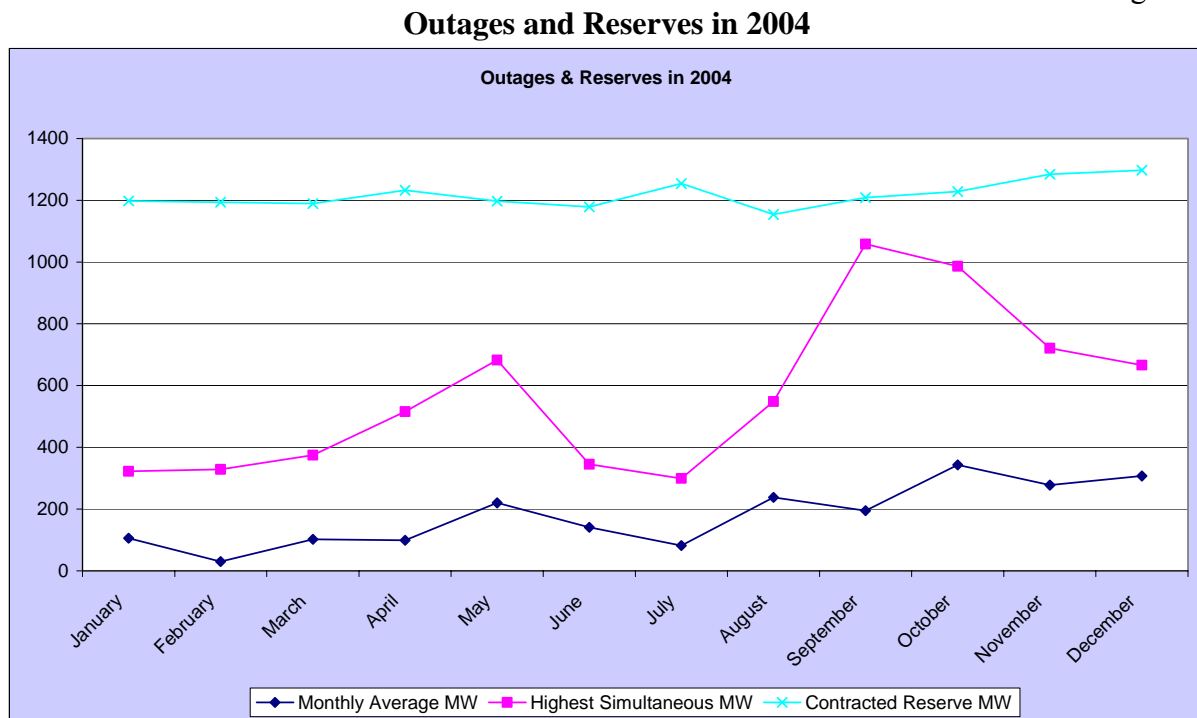
The Office reviewed in 2004 in cooperation with external, reputable advisors the internationally implemented power plant investment incentive methods that disturb the competitive market to a smaller extent. At the same time, methods have been selected that suit best the Hungarian conditions. It has been stated that the current capacity reserves do not require the application of these incentive measures as there is intention for investment in the current regulatory environment.

On December 31, 2004, the installed generation capacity of the Hungarian electricity system had been 8,831.4 MW, which was 405.1 MW more than the installed generation capacity of the previous year. The growth is due to the installation of the Kispest gas turbine (110 MW), the TVK (a large consumer) gas turbine (34 MW), as well as other gas engines. In addition, the proportion of distributed generation further increased with the spread of gas motors. Investors of several coal-fired power plants have switched to biomass instead of closing down the plant, thus they could maintain the already existing capacities.

During 2004, the peak load of the electricity system had been 6,357 MW, 3.5% more than the previous year (6,140 MW). Gross electricity consumption amounted to 40,603 GWh, representing a decrease of 0.1% compared to the previous year. Annual electricity generation of domestic power plants had been 33,131 GWh, out of which 11,914 GWh had been generated by the Paks Nuclear Power Plant. Power plant generation has shown a decreasing trend ever since 2001. The import & export balance of the electricity was 7,472 GWh, 7.7% more than in 2003 (6,939 GWh). The growth in electricity import resulted from a growth of import by eligible customers due to economic reasons. The average reserve contracted by the system operator was 1,214 MW in 2004. There had been no power plant outages leading to

customer curtailments in 2004. The following diagram helps track forced outages and the extent of reserves.

Figure 2



As the figure illustrates, the system had reserve capacity left in it in the case of even the largest simultaneous outages.

The development of reserve margin, meaning the difference between installed output capacity and the annual maximum peak, is important with regard to the security of supply. See Table 8 for relevant data.

Table 8

Output Capacity Data of Power Plant Equipment

	2002	2003	2004
Installed output capacity [MW]	8247.0	8426.3	8831.4
Maximum peak demand [MW]	5980.0	6140.0	6357.0
Reserve [MW]	2267.0	2286.3	2474.4
Reserve [%]	27.5	27.1	28.0

The amount of reserve is appropriate on an international scale even if we take into account that significant capacity is taken off from the installed output capacity due to the high permanent shortage (for example, the 450 MW "C" blocks of the Dunamente Power Plant are no longer operational, but have only been deleted from the operating license in 2005). Security is further increased by a significant import opportunity.

Generation

From the point of view of secure supply of electricity, the impact of the INES 3 level malfunction that occurred in shaft 1, block 2 of the Paks Nuclear Power Plant on April 11, 2003, as well as the scheduled progress of the repair project had a lasting significance during 2004, too. Block 2 received permission to restart underneath strict authority supervision of the

National Nuclear Energy Office, following among others the commissioning of the autonomous cooling cycle of shaft 1, of the autonomous emergency shutdown system, the training of skilled personnel, as well as the conducting of physical inspections of the reactor and chemical inspections. Based on this, following a successful test run, the block has become a part of electricity generation as of September 3, 2004 under normal operating conditions. The block has operated with a reactor output of 97% with a gross output of 445 MW until its planned shutdown on December 18, 2004.

Network

A new component has been added to the transmission network in 2004. The electricity supply of the Southern Transdanubia region is strengthened by the fact that MVM, as the transmission licensee, has commissioned the 400 kV electric transmission line between Paks and Pécs on November 17, 2004, following several years of preparation and implementation, together with the 400/120 kV new substation near Pécs, within the township of Bogdán, as well as with the new 120 kV electric transmission line between the new station and Pannon Hőerőmű Rt. (the Pécs Power Plant). Consequently, the network congestion in the country was ceased.

On October 10, 2004, the resynchronization of zones 1 and 2 of the UCTE was completed successfully (covering the Balkans: the electricity systems of Romania, Bulgaria, Serbia & Montenegro, Bosnia & Herzegovina, and Greece), resulting once again in a complete the UCTE electricity system integration. Resynchronization at the same time extended commercial opportunities in the direction of Serbia & Montenegro and Romania. The creation of the rules for commercial settlement will take place after the connection.

Based on Section (1), Article 27 of the VET, the system operator has the obligation to create the network development plan of the electricity system at least once every two years. The network development plan was created in 2004, for the first time after the opening of the market. The Office has no statutory mandate to approve the network development plan, but in the interest of ensuring the enforcement and credibility of the plan, it has initiated to receive legislative authorization for the approval of the plan - in line with Article 23 of 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.

Disturbance in the electricity system, crisis situation

Based on a mandate provided by Governmental Decree 281/2002 (December 21) on the measures to be taken in case of severe disturbance in the electricity system and an electricity supply crisis, the Office approved the crisis plan in its resolution 54/2002 and defined obligations for the system operator in order to make up for shortfalls in the plan. It has also approved the list of protected and vital customers based upon the rotational disconnection plan (resolution 318/2004) reacting to the submission of county disaster protection headquarters, as well as the Civilian Defense Headquarters of Budapest. Based on the preparation of the resolutions issued it can be determined that the opening of the electricity market raised new questions in the VET and related decrees from several new perspectives regarding the regulations pertaining to significant disturbances on the electricity system (the relevant decree leaves the definition up to the rules of supply) and a crisis in the supply of electricity, with special regard to legal harmonization within the Union.

5.2 Gas

National gas production is expected to decrease by 2008; the increase of import capacity is not planned for the next three years.

Table 9

Expected Trends of Natural Gas Sources and Demand

	2005	2006	2007	2008
Natural Gas Consumption	14.5	14.8	15.1	15.4
Production	2.4	2.2	2.2	2.1
Capacity	15.2	15.2	15.2	15.2

(billion m³)

Regarding the sources of natural gas, import is playing an increasing role. While the consumption of natural gas is increasing from year to year, the volume of domestic production is decreasing, and as a result, import needs to grow faster than the rate of growth in consumption. In 2004, the rate of import within all sources had been 79.5%. All of the import gas procured originated from Russia, but only 72.6% of it had been delivered to the country by Russian suppliers, while the rest had been delivered via Western European companies and subject to contingency warranties. The effective import agreements expire in 2010 and during the years to follow.

Regarding the feed-in of import, the transmission licensee is cooperating efficiently with both the Austrian and the Ukrainian supplier.

The TOP level of import deliveries is 85-100% of existing gas import agreements. Flexibility within the day is $\pm 5\%$ on the "Testvériség" pipeline. There is no flexibility on the HAG pipeline.

Considering the high proportion of temperature-dependent consumption, mainly comprised of household consumption, the flexibility of domestic production and import is not sufficient to cover seasonal and daily fluctuations. Consumption on a peak winter day may be as high as four times that of the consumption on an average summer day. In the case of household customers, this ratio is seven to eight times.

Underground natural gas storage facilities are important tools of compensating seasonal and daily fluctuations.

The five underground natural gas storages installed in worked-out natural gas fields are together capable of storing 3.36 billion m³ of natural gas. The peak capacity of daily unloading is 44.2 million m³. The unloading capacity on the peak consumption day during the winter of years 2004/2005 had been 41.8 million m³/day, covering 46.8% of the consumption of that day.

The institution of last resort does not exist yet. Eligible customers who have not switched to the competitive market are receiving public utility supply, together with household customers. Public utility customers currently have priority when contracting for spare capacity.

No tools are currently available for increasing the production/import capacity. The Office may announce a tender for performing the development not undertaken by system operators.

According to the GET, when contracting for free storage capacity, public utility customers have priority over customers on the competitive market.

The unloading capacity will be increased by 3 million m³/day in 2005.

6. Public service obligation, customer protection

6.1 Electricity

In Hungary, an administrative price control is in effect for end user prices in the case of public utility customers. Currently any customer may opt for remaining within the public utility sector, or may return there from the competitive market (the actual switch-back comes into effect within six months of announcing the intent to do so at the latest). This way, the public utility currently also operates as a price cap for the competitive market.

Prices are corrected annually, following a recommendation by the Office to that effect to the Minister of Economy and Transport exercising the right of the price setting authority. Special modification of the price within the year may happen if events on the electricity market or significant problems in regulation clearly call for such measures. The compensation of the supply obligation at administered prices is not required, since suppliers may purchase from public utility wholesalers at administered prices. See the data in Table 10 for administered price trends pertaining to public utility customers. See Table 11 for electricity prices defined based on Directive 90/377/EC for Hungarian public utility end users pertaining to standard consumers.

Table 10, Part 1
Public utility (maximum) average electricity prices excluding direct taxes (VAT, energy tax) in Hungary (1)

Categories	from	from	from	from	from	from	from	from
	January	January	January	February	August	January	January	February
	2000.	2001.	2002.	2003.	2003.	2004. (3)	2004. (4)	2005. (4)
Wholesale price (2)	9.05	10.23	10.47	10.03	11.22	10.92	10.89	12.10
End user price (including supplementary charges)	14.66	15.55	16.33	17.96	19.40	19.40	20.74	22.77
Residential	16.49	17.48	18.32	19.90	21.70	21.70	22.09	23.60
"A" tariff (general)	19.80	21.00	22.00	23.70	25.70	25.70	25.70	27.31
Block I (up to 1320 kWh/year) (5)							25.70	26.80
Block II (above 1320 kWh/year) (5)							25.70	28.00
"B" tariff (separately measured)	9.20	9.70	10.20	11.60	13.00	13.00	13.00	14.30
"C" tariff (electric industry employees)	5.40	5.70	6.00	6.60	7.20	7.20	7.20	8.10
Non-residential	13.77	14.61	15.35	17.01	18.55	18.55	19.81	22.20
According to voltage level								
high voltage	9.27	9.82	10.36	11.62	12.70	12.70	13.94	15.84
medium voltage	12.34	13.10	13.78	15.22	16.58	16.58	16.38	18.85
low voltage (with public lighting tariff)	18.14	19.24	20.20	22.35	24.33	24.33	23.35	25.80
According to tariff types								
tariffs with capacity charge	11.87	12.60	13.26	14.77	16.14	16.14	17.28	20.02
public lighting tariff	24.17	25.60	26.90	29.03	30.82	30.82	30.79	35.00
tariffs with standing charge	19.27	20.43	21.43	23.58	25.67	25.67	25.45	26.86

Residential electricity prices including VAT (6)

Categories	from	from	from	from	from	from	from	from
	January	January	January	February	August	January	January	February
	2000.	2001.	2002.	2003.	2003.	2004. (3)	2004. (4)	2005. (4)
Residential (average)	18.47	19.57	20.52	22.29	24.30	27.13	27.61	29.50
"A" tariff (general)	22.18	23.52	24.64	26.54	28.78	32.13	32.13	34.14
Block I (up to 1320 kWh/year) (5)							32.13	33.50
Block II (above 1320 kWh/year) (5)							32.13	35.00
"B" tariff (separately measured)	10.30	10.86	11.42	12.99	14.56	16.25	16.25	17.88

The numbered remarks are shown at the bottom of Table 10, Part 2.

Table 10, Part 2

Public utility (maximum) average electricity price changes excluding direct taxes (VAT, energy tax) in Hungary (1)

Categories	(%)						
	from January 2000.	from January 2001.	from January 2002.	from February 2003.	from August 2003.	from January 2004.	from February 2005.
Wholesale price (2)	5.9%	13.1%	2.3%	-4.2%	11.2%	-2.7%	10.8%
End user price (including supplementary charges)	6.0%	6.0%	5.0%	10.0%	9.0%	0.0%	9.8%
Residential	5.9%	6.0%	4.8%	8.6%	9.0%	0.0%	6.8%
"A" tariff (general)	5.9%	6.1%	4.8%	7.7%	8.4%	0.0%	6.3%
Block I (up to 1320 kWh/year) (5)							4.3%
Block II (above 1320 kWh/year) (5)							8.9%
"B" tariff (separately measured)	5.7%	5.4%	5.2%	13.7%	12.1%	0.0%	10.0%
"C" tariff (electric industry employees)	5.9%	5.6%	5.3%	10.0%	9.1%	0.0%	12.5%
Non-residential	6.1%	6.1%	5.1%	10.8%	9.0%	0.0%	12.1%
According to voltage level							
high voltage	6.1%	6.0%	5.5%	12.2%	9.3%	0.0%	13.6%
medium voltage	6.1%	6.2%	5.1%	10.5%	9.0%	0.0%	15.0%
low voltage (with public lighting tariff)	6.0%	6.1%	5.0%	10.6%	8.9%	0.0%	10.5%
According to tariff types							
tariffs with capacity charge	6.6%	6.2%	5.2%	11.4%	9.2%	0.0%	15.9%
public lighting tariff	6.1%	5.9%	5.1%	7.9%	6.2%	0.0%	13.7%
tariffs with standing charge	4.7%	6.1%	4.9%	10.0%	8.8%	0.0%	5.5%

Residential electricity price changes including VAT (6)

Categories	(%)						
	from January 2000.	from January 2001.	from January 2002.	from February 2003.	from August 2003.	from January 2004.	from February 2005.
Residential (average)	5.9%	6.0%	4.8%	8.6%	9.0%	11.6%	6.8%
"A" tariff (general)	5.9%	6.1%	4.8%	7.7%	8.4%	11.6%	6.3%
Block I (up to 1320 kWh/year) (5)							4.3%
Block II (above 1320 kWh/year) (5)							8.9%
"B" tariff (separately measured)	5.7%	5.4%	5.2%	13.7%	12.1%	11.6%	10.0%

- (1) According to the Energy Tax Act 3. § (1) a)-b) Energy Tax (0,186 HUF/kWh) shall not be paid by residential customers.
- (2) From February 2003 excluding system usage (transmission, system operation and ancillary services) charges formerly included in wholesale prices.
- (3) Between the January 2000 - January 2004 period the average prices have been calculated with constant weights and with no eligible consumption in the non-residential sector as well.
- (4) Calculated with the weights used for the February 2005 price setting and with smaller public share in the non-residential sector.
- (5) There was no such distinction before February 2005.
- (6) Extent of VAT: until 12/31/2003 12%, from 1/1/2004 25%.

Table 11

Electricity Standard Consumer Prices (Household Consumers)

(EUR/MWh)*

Customer Type	Code	DA	DB	DC	DD	DE
Annual Consumption	kWh	600	1 200	3 500	7 500	20 000
including: night time (controlled)	kWh			1 300	2 500	15 000
1. January 2004		97,13	97,13	79,30	81,13	61,13
1. July 2004		102,88	102,88	84,00	85,94	64,75
1. January 2005		104,22	104,22	85,09	87,05	65,59

Electricity Standard Consumer Prices (Non-Household Consumers)

(EUR/MWh)*

Customer Type	Code	IA	IB	IC	ID	IE	IF	IG	IH	II
Annual Consumption	kWh	30 000	50 000	160 000	1 250 000	2 000 000	10 000 000	24 000 000	50 000 000	70 000 000
Contracted Output	kW	30	50	100	500	500	2 500	4 000	10 000	10 000
Annual Utilization Hours	hour	1 000	1 000	1 600	2 500	4 000	4 000	6 000	5 000	7 000
1. January 2004		99,49	99,49	97,53	78,32	65,31	47,78	46,83	48,32	46,94
1. July 2004		105,38	105,38	103,31	82,96	69,18	50,61	49,61	51,18	49,72
1. January 2005		106,75	106,75	104,65	84,04	70,08	51,27	50,25	51,85	50,36

Currency exchange rate (1 € / HUF): Jan 2004: 264.6 HUF; July 2004: 249.8 HUF; Jan 2005: 246.6 HUF

* Prices all taxes excluded (VAT and energy tax)

6.2 Natural gas

Public utility supply is received by household customers, and those eligible customers who so far did not wish to switch to the competitive market. These are supplied by public utility suppliers, for whom the public utility wholesaler procures and supplies natural gas. The task of public utility supplier companies covers exclusively the supply of public utility customers. According to the GET, public utility contracts have priority when contracting for spare transmission pipeline, distribution and storage capacity. This rule is detrimental to the evolution of competition. This is because it represents a level of security to public utility customers, which eligible customers do not wish to abandon. Furthermore, new customers also opt for the public utility. The dominance of public utility narrows the playground of players of the competitive market.

The protection of customers who are more exposed to disturbances in supply is ensured by the enforcement of statutory provisions pertaining to the order of curtailing.

According to the governmental decree issued for the execution of specific provisions of the GET, the order for curtailing customers is to be defined during September of each year. This order classifies the customers of gas into five curtail groups, and in the case of curtailing, the order of curtailing is to be implemented for these groups. According to this provision, household customers and certain community customers –belonging to the fifth group - may not be curtailed. Other community customers belong to the fourth group. The third group contains small industrial, commercial, and agricultural customers, as well as those major customers whose curtailing would cause technological damages. In the case of customers classified in the first and second group, a curtail would not cause technological damages. The first group contains such major customers.

Approximately 7,000 customers had been disconnected from the natural gas supply in 2004 due to reasons of non-payment.

Public utility supply is provided based on public utility contracts. The Gas Supply Public Utility Code, which is an Attachment to the governmental decree, governs the legal

relationship between public utility customers, public utility suppliers, and distributors, as well as the mandatory elements of the content of the public utility agreement. The price of public utility gas, the conditions of applying the prices, the tariffs to be paid, and the conditions of price regulation are set forth within a decree by the Minister of Economy and Transport based on the recommendation of the Office.

In Hungary, an administrative price control is in effect for end user prices in the case of public utility customers. Currently any customer may opt for remaining within the public utility sector, or may return there from the competitive market (switching-back is possible once a year, the process may take up to one year). This way, the public utility currently also operates as a price cap for the competitive market.

Administered prices are published in the form of a ministerial decree. Similarly to former practice, prices include system use costs, which have already been unbundled. This way, the public utility tariffs, paid by the end users, also have the role of covering system use tariffs related to the public utility supply. The cost of natural gas (as a product) is included in public utility prices on the level of import prices. The price regulation decree stipulates half-year periods for updating public utility prices with the changes in the import price.

See Table 12 for public utility natural gas prices, and Table 13 for public utility natural gas prices based on Directive 90/377/EC and pertaining to standard consumers that had been defined.

Table 12, Part 1

Administrative (Maximum) Natural gas Prices (excluding VAT and Energy Tax)

(excluding the effects of household price compensation from October 15, 2003 !)

This sheet should be interpreted together with the remarks !!!

Dimension: HUF/m ³ where no other indicated (gas charge, average)	Prices (3) (4) (16)						
	2002.	2003.	from October 15, 2003		2004.	2004.	2005.
	from December	from May 15	(9) (10)	(12)	from January 1 (8)(10) (11)	from July 1 (13)	from January 15 (13) (14)
Wholesale (average)							
(1)	24.36	28.34	30.92	34.85	40.02	40.37	45.66
(2)	38.16	38.33	40.47	40.66	39.92		
capacity charge (HUF/MJ/day)	11.46	13.35	19.42	19.42	21.57	21.96	21.42
gas charge					34.82	34.89	40.30
(1)	21.65	25.33	24.21	24.21	34.82		
(2)	35.33	35.33	35.84	35.84	34.82		
End user (average)					47.00	46.26	51.78
Residential / low consumption (average)					50.64	50.64	56.63
standing charge (HUF/year)					3144	3144	3504
gas charge					48.82	48.82	54.56
incl.: residential = group (a) (average)	(5) 36.36462	40.72	40.71	40.57	50.78		
standing charge (HUF/year)	2256	2520	2520	2520	3144		
gas charge	34.83	39.01	39.01	39.01	48.82		
group (b) (average)	(5) 35.44	40.74	49.68	49.63	49.63		
standing charge (HUF/year)	2256	2592	3144	3144	3144		
gas charge	34.83	40.06	48.83	48.82	48.81		
Medium customers (20 - 100 m ³ /h) (average)					56.47	56.47	61.17
standing charge [(HUF/m ³ /h)/year]					9400	9400	10440
gas charge					46.28	46.28	51.06
incl.: residential, district heating = group (a) (average)	(5) 35.14	39.35	39.35	39.70	54.55		
standing charge [(HUF/m ³ /h)/year]	4224	4728	4728	4728	9400		
gas charge	31.74	35.54	35.54	35.54	46.27		
group (b) (average)	(5) 35.92	41.32	55.61	56.85	56.84		
standing charge [(HUF/m ³ /h)/year]	4224	4848	9400	9400	9400		
gas charge	31.74	36.49	46.28	46.28	46.28		

Table 12, Part 2

Large customers												
I. Capacity contract 100 - 500 m ³ /h (average)												
capacity charge [(HUF/MJ/h)/year]						51.94	51.94	57.54				
gas charge						850	850	850				
incl.: group (a) (average)						(5) 29.09	32.55	32.55	33.71	45.22		
capacity charge [(HUF/MJ/h)/year]						488	488	620	620	850		
gas charge						25.82	29.29	28.41	28.41	37.96		
group (b) (average)												
standing charge [(HUF/MJ/h)/year]						(5) 35.20	39.79	54.29	52.68	52.47		
gas charge						488	488	850	850	850		
gas charge						25.82	30.41	37.96	37.96	37.96		
II. Capacity contract above 500 m ³ /h (average)												
capacity charge [(HUF/MJ/h)/year]										44.79	44.79	52.04
gas charge										850	850	850
gas charge										35.98	35.98	41.46
II.1. Favoured customers (average)												
capacity charge [(HUF/MJ/h)/year]										46.99		
gas charge										850		
gas charge										35.98		
incl: group (a) (average)						(5) 27.73	(5) 31.26	31.69	33.18	48.08		
capacity charge [(HUF/MJ/h)/year]						488	(7) 488	620	620	850		
gas charge						21.95	(7) 25.49	24.36	24.36	35.98		
group (b) (average)												
capacity charge [(HUF/MJ/h)/year]						(5) 28.27	(5) 31.81	47.01	46.02	46.02		
gas charge						488	(7) 488	850	850	850		
gas charge						21.95	(7) 25.49	35.98	35.98	35.98		
II. 2. Non-favoured customers (average)												
capacity charge [(HUF/MJ/h)/year]						40.27	40.27	43.15	42.61	42.61		
gas charge						550	550	850	850	850		
gas charge						35.51	35.51	35.98	35.98	35.98		
III. Customers with direct link (MOL) (average)												
capacity charge [(HUF/MJ/h)/year]										36.94	36.94	42.16
gas charge										620	620	620
gas charge										33.91	33.91	38.98
III.1. Favoured customers (average) (7)												
capacity charge [(HUF/MJ/h)/year]										37.98		
gas charge										620		
gas charge										33.91		
incl: group (a) (average)						26.00	29.15	27.22	25.86	37.98		
capacity charge [(HUF/MJ/h)/year]						488	488	620	620	620		
gas charge						21.74	24.89	21.80	21.79	33.91		
group (b) (average)												
capacity charge [(HUF/MJ/h)/year]						26.00	29.15	36.05	36.87	36.87		
gas charge						488	488	620	620	620		
gas charge						21.74	24.89	33.92	33.91	33.91		
III. 2. Non-favoured customers (average) (7)												
capacity charge [(HUF/MJ/h)/year]						34.27	34.27	35.09	36.08	36.08		
gas charge						550	550	620	620	620		
gas charge						32.42	32.42	33.02	33.02	33.02		

Remarks:

- (1) Calculated according to tariff category 1 (favoured).
- (2) Calculated according to tariff category 2 (non-favoured).
- (3) No data were available to design a consumption structure proper for groups (a) and (b).
- (4) The average price and average price change show the hypothetical case that every consumer - supplied in the country - is public utility consumer.
(This assumption is irrelevant since January 1, 2004.)
- (5) With identical tariffs the average prices vary within a tariff category because of different distribution of consumption and contracted capacity.
- (6) Assuming that the capacity and gas consuming proportions of the "favoured" and non-favoured" consumers are the same.
- (7) To keep the tariff system balance the distinction between (a) and (b) groups within a given customer category was not possible.
- (8) Tariffs and average prices do not include the effects of residential gas-price compensation specified in the ministerial decree 50/2003. (VIII. 14.).
- (9) From October 1, 2003 for the residential customers with a gas meter smaller than 20 m³/h the gas charge for block 1 is 36.66 HUF/m³, for block 2 is 37.45 HUF/m³, and for block 3 is 39.01 HUF/m³.
- (10) In administrative price categories, distinctions: "favoured" and "non-favoured", and "groups (a)" & "(b)" come to an end.
The prices do not include the Energy Tax (56 HUF/GJ for not excepted non residential customers) and the gas charge discount for heat generation for household and residential district heating. The VAT for natural gas has been increased from 12 to 15%.
- (11) From January 1, 2004 for the residential customers with a gas meter smaller than 20 m³/h the gas charge for block 1 is 38.95 HUF/m³, for block 2 is 41.66 HUF/m³, and for block 3 is 48.83 HUF/m³.
- (12) Calculated with fact weights of the price correction of May 15, 2003.
- (13) The percental indicators of average price changes does not show the significant changes in weights.
- (14) From January 15, 2005 for the residential customers with a gas meter smaller than 20 m³/h the gas charge for block 1 is 40.4 HUF/m³, for block 2 is 44.8 HUF/m³, and for block 3 is 54.56 HUF/m³.
- (15) In case of residential consumers the price changes calculations are based on non-compensated price.
- (16) The average prices, gas charges and the percentage values of their changes include the fact weights taken into consideration for different time periods and the effects of changes of thermal value being used as well.
- (17) The values shown above do not include the changes of fact weights and thermal value.

Table 13.

Natural Gas Standard Consumer Public Utility Prices (without subsidy)

(EUR/TJ)

Consumer type	Code	D1	D2	D3	D3b	D4
Annual consumption	GJ	8	17	84	126	1 047
1. January 2004		7 348	5 961	5 645	5 552	5 507
1. July 2004		7 781	6 313	5 978	5 880	5 832
15. January 2005		8 558	7 070	6 731	6 632	6 583

Natural Gas Standard Consumer Public Utility Prices (with subsidy)

(EUR/TJ)

Consumer type	Code	D1	D2	D3	D3b	D4
Annual consumption	GJ	8	17	84	126	1 047
1. January 2004		6 252	4 865	4 601	4 667	4 954
1. July 2004		6 621	5 152	4 873	4 943	5 246
15. January 2005		6 871	5 383	5 136	5 299	5 750

Natural Gas Standard Consumer Prices (Non-Household Consumers)

(EUR/TJ)

Consumer type	Code	I1	I2	I3-1	I3-2	I4-1	I4-2	I5-1
Annual consumption	GJ	419	4 186	41 860	41 860	418 600	418 600	4 186 000
1. January 2004		7 291	6 524	6 229	5 153	5 025	4 851	4 623
1. July 2004		7 722	6 909	6 597	5 458	5 321	5 137	4 896
15. January 2005		8 461	7 638	7 322	6 171	6 029	5 842	5 598

Currency exchange rate (1 € / HUF): Jan 2004: 264.6 HUF; July 2004: 249.8 HUF; Jan 2005: 246.6 HUF

* Prices all taxes excluded (VAT and energy tax)