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COMPETITION COMMITTEE**

**Working Party No. 2 on Competition and Regulation**

**Competition Enforcement and Regulatory Alternatives – Note by the Russian Federation**

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More documents related to this discussion can be found at  
<http://www.oecd.org/daf/competition/competition-enforcement-and-regulatory-alternatives.htm>

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## *Russian Federation<sup>1</sup>*

1. Economic regulation and competition policy are interdependent instruments of economic policy. Despite the fact that antimonopoly legislation and economic regulation differ from each other, they still overlap and in many ways complement each other.
2. In accordance with the established powers, the FAS Russia carries out activities on tariff regulation, including in the sphere of natural monopolies.
3. According to the FAS Russia, the state tariff policy should stimulate natural monopoly entities to reduce their own costs, and in order to increase their efficiency (optimization of operating and investment costs, financial and economic activity) tariffs for services provided by natural monopolies should be formed according to the "inflation minus" principle, which makes it possible to prevent the indexation of citizens' payments by more than the amount of inflation.
4. The use of long-term approaches and stable tariffs for infrastructure services are a key instrument of state regulation that has a positive effect on reducing macroeconomic uncertainty.
5. Having regard to the above, the Decree of the Government of the Russian Federation developed by the FAS Russia dated October 13, 2020 No. 2648-r<sup>2</sup> was approved, in which the key approach remains "tariff growth is less than inflation".
6. According to the FAS Russia, the implementation of given provisions will allow consumers on a long-term basis to predict the dynamics of tariffs for the transportation of oil and oil products through main pipelines, and will also serve to improve the investment climate in the oil industry as a whole.

### 1. Electric power industry

7. As part of the antimonopoly control, the FAS Russia initiated a number of major antimonopoly cases in the electric power industry, which are an example of the impact of competition enforcement on protecting the economic interests of consumers.

#### 1.1. Case of the FAS Russia against guaranteeing suppliers

8. In 2014, the FAS Russia recognized the guaranteeing suppliers of Dagestan Energy Retail Company, Nurenergo, Kabbalkenergo, Karachaevo-Cherkesskenenergo, Ingushenergo and Sevkavkazenergo violated Part 1 of the Article 10 of the Federal Law dated July 26, 2006 No. 135-FZ "On Protection of Competition"<sup>3</sup>.
9. In the period from January 2011 to December 2012, these companies showed signs of organized, regular and significant overestimations of the planned volumes of

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<sup>1</sup> The report was prepared by the FAS Russia

<sup>2</sup> <http://government.ru/docs/all/130356/> (Russian version only)

<sup>3</sup> Article 10 of the Law on Protection of Competition: "Actions (inaction) of a dominant economic entity are prohibited, the result of which is or may be the prevention, restriction, elimination of competition and (or) infringement of the interests of other persons (economic entities) in the field of entrepreneurial activity or an indefinite range of consumers".

consumption relative to the actual ones. As a result of such actions, there was an unjustified increase in prices for other consumers of electrical energy in the first pricing zone<sup>4</sup> of the wholesale electricity and capacity market, which is a sign of restriction of competition.

10. The FAS Russia issued remedies to companies to transfer more than 2 billion rubles of illegally obtained income to the federal budget. The legality of the decision and remedies of the FAS Russia was confirmed by all courts, including the Supreme Court of the Russian Federation.

11. Another case was initiated by the FAS Russia against the T-Plus group of persons and IES-Trading CJSC. These companies entered into an illegal agreement, which led to restriction of competition in the period from 2012 to 2013 by overstating the planned electricity consumption one day in advance of the wholesale electricity and capacity market. This, in turn, led to an increase in the price of electricity in the first pricing zone.

12. The given strategy was established by the FAS Russia in 2014 based on the results of two unscheduled inspections and on the basis of a comprehensive mathematical modeling and analysis of violators' behavior, as well as an assessment of the economic impact on consumers, carried out with the participation of the Association "Non-Commercial Partnership Market Council". The T-Plus group of persons was issued two remedies: to transfer to the federal budget income received as a result of violation of antimonopoly legislation, which amounted to more than 860 million rubles, and to comply with behavioral requirements.

13. The actions of the companies identified by the FAS Russia led to a significant increase in prices on the wholesale electricity market, which had a negative impact on all consumers in the first pricing zone.

14. The result of consideration of this case is that since 2014 there have been no such violations on the wholesale electricity market. By its ruling, the FAS Russia carried out preventive work to suppress such violations.

15. In the summer of 2017, the FAS Russia and T-Plus entered into a settlement. The company acknowledged the violation and in December 2017, the FAS Russia received confirmation from T-Plus regarding the transfer of more than 867 million rubles to the federal budget.

## 1.2. Case of the FAS Russia against OOO SGS PLUS

16. Another example is the case initiated by the FAS Russia in 2019 against SGS PLUS on violation of antimonopoly legislation in terms of price manipulation in the wholesale market by an entity that does not occupy a dominant position (hereinafter – Article 14.31.2 of the Code of Administrative Offences of the Russian Federation)<sup>5</sup>.

17. As part of the price monitoring on the wholesale electricity and capacity market, the FAS Russia noted an increase in the weighted average equilibrium price of electricity

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<sup>4</sup> The first pricing zone of the wholesale market for electrical energy geographically covers the European part of Russia and part of Western Siberia. The exceptions are the Arkhangelsk Region, the Komi Republic and the Kaliningrad Region, which belong to non-pricing zones due to the isolation of these energy zones, detachment from the Unified Power Systems and weak flows.

<sup>5</sup> Responsibility for this offence is provided for by the Paragraph 1 of the Article 14.31.2 of the Code of Administrative Offences of the Russian Federation ("Price manipulation in the wholesale and (or) retail electricity (capacity) markets").

purchase in the one day in advance market<sup>6</sup> (hereinafter – the day-ahead market index) in Sevastopol in January 2019 relative to December 2018 by 26.9%, in general for the Unified Power System<sup>7</sup> of the South by 1.8%.

18. According to the results of the analysis carried out jointly with the Association "Non-Commercial Partnership Market Council", it was found that this growth in the index appeared due to the demand for the Sevastopol thermal power plant offer against the background of the change in pricing from January 1, 2019 in terms of accounting for the applications of the wholesale electricity and capacity market participants operating in the Republic of Crimea and Sevastopol, when calculating the price.

19. In the course of the investigation, it was revealed that SGS PLUS, mainly in the evening peak hours in January 2019, filed deliberately overstated economically unjustified price bids, which ultimately led to an increase in the day-ahead market index in a number of regions of the Unified Power Systems of South, as well as, in general, in the first pricing zone (the growth of the hourly day-ahead market index in some hours reached 30%).

20. It should be noted that since January 1, 2019 the specifics of accounting for price bids when conducting a competitive selection of price bids for day-ahead market index in the Republic of Crimea and the city of Sevastopol, according to which prices were not taken into account when calculating equilibrium electricity prices during 2017 and 2018, specified in the price bids of suppliers, have ceased to be effective.

21. Thus, the prices indicated in the price bids began to be taken into account in the calculations of the day-ahead market index from January 1, 2019 whereof the economic entities were aware and additionally notified by the Association "Non-Commercial Partnership Market Council" in advance.

22. Thus, unfair actions of SGS PLUS, which occupies an insignificant market share, influenced the equilibrium price, which ultimately led to an increase in the day-ahead market price index.

23. Responsibility for price manipulation in the wholesale market by an entity that does not occupy a dominant position is established by the Article 14.31.2 of the Code of Administrative Offences of the Russian Federation.

24. An administrative investigation was carried out, as a result of which a ruling was made to impose a fine in the amount of 687.5 thousand rubles.

25. The case is of precedent importance, since a situation has arisen in which SGS PLUS, not being a dominant entity in the wholesale electricity and capacity market, influenced an increase in the purchase price of electricity on the day-ahead market.

26. In accordance with the Federal Law of August 2, 2019 No. 300-FZ "On Amendments to the Federal Law "On the Electrical Power Industry"<sup>8</sup>, it is possible to conclude agreements on the conditions for carrying out regulated activities between grid

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<sup>6</sup> One day in advance market – competitive selection of price bids from suppliers and buyers a day before the actual supply of electricity with the determination of prices and delivery volumes for each hour of the coming day.

<sup>7</sup> Unified Power System is a set of several energy systems, united by a common mode of operation with a common dispatch control as the highest level of control in relation to the dispatch control of the power systems included in it.

<sup>8</sup> Federal Law of August 2, 2019 No. 300-FZ<sup>8</sup> "On Amendments to the Federal Law "On the Electrical Power Industry": <http://publication.pravo.gov.ru/Document/View/0001201908020073> (Russian version only)

organizations and regulatory bodies, which will ensure the establishment of long-term tariffs for services on transmission of electrical energy, as well as long-term parameters of energy efficiency of the power grid complex.

27. The FAS Russia has prepared a draft Decree of the Government of the Russian Federation "On approval of the Procedure for concluding, changing, terminating agreements on the conditions for carrying out regulated activities, as well as on introducing amendments and invalidating certain acts of the Government of the Russian Federation", which is undergoing approval by federal executive authorities.

28. For the electric power industry, this is an absolutely new and promising mechanism for setting tariffs, which in the long term allows to ensure a balance of interests between the investor (territorial grid organization) and the constituent entity of the Russian Federation within the framework of the parameters of the Forecast of the socio-economic development of the Russian Federation, approved by the Government of the Russian Federation.

29. In 2019, the introduction of new mechanisms began to stimulate the development of competition in the retail electricity (capacity) markets and reduce the price for consumers.

30. On March 20, 2019 the Government of the Russian Federation adopted Decree No. 287<sup>9</sup>, which provides for a pilot project in 2019-2020, the purpose of which is to form aggregators of demand<sup>10</sup> management for retail consumers as a new type of energy market participants.

31. The purpose of introducing a demand management mechanism is to reduce payments for electricity by limiting consumption during peak load hours, for which both the aggregator and its consumers will receive payments. In addition, the introduction of this mechanism will reduce the required reserves in the energy system, exclude the construction of excess generation and reduce payments for capacity.

32. Since 2019, the System Operator of the Unified Power System has been providing a service for the formation of aggregators for managing demand for retail consumers as a new type of participants in the energy market.

33. In terms of participation in consumer demand management in the retail market in 2019, the volume of demand was limited to 50 MWth, while the volume of supply significantly exceeded demand.

34. In the first quarter of 2020, the planned volume of demand management services has significantly grown<sup>11</sup>. At the same time, the planned volume of decrease in consumption of the selected objects in the third quarter of 2020 increased compared to the second quarter of 2020<sup>12</sup>, which shows an obvious increase in the volume of services and the involvement of consumers in participation in the mechanism of demand management.

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<sup>9</sup> Decree of the Government of the Russian Federation of March, 20 2019 No. 287 <http://publication.pravo.gov.ru/Document/View/0001201903260027> (Russian version only)

<sup>10</sup> Demand management aggregators are specialized organizations coordinating the ability of a group of retail consumers to manage their electricity consumption, converting it into services for managing demand for electricity and transmitting to consumers part of the proceeds received from the sale of this service.

<sup>11</sup> 227 MWth (354% growth compared to Q4 2019)

<sup>12</sup> From 281 MWth to 336 MWth

35. Thus, the practice of introducing a demand management mechanism shows an obvious increase in the volume of services and the involvement of consumers in it.

36. This mechanism promotes the involvement of a wide range of consumers in the market management of demand for electricity and capacity, which allows competition between generating electric power companies and between consumers on market conditions.

37. Currently, the Decree of the Government of the Russian Federation dated February 2, 2021 No. 132 has come into force, providing for the integration of the demand management mechanism as a permanent instrument from 2021.

38. In addition, within the framework of improving antimonopoly control on the wholesale electricity and capacity market, the FAS Russia developed an order of the FAS Russia to determine the numerical characteristics of the factors, on the basis of which the dominant position of participants in the wholesale electricity and capacity market will be established, the market share of which is within the borders of free power transfer zone is less than 20%.

39. Federal Law dated March 26, 2003 No. 35-FZ "On Electric Power Industry" establishes that producers and consumers have a dominant position if their share in the WECM within the boundaries of the free power transfer zone exceeds 20%.

40. According to the Part 4 of the Article 25 of the Federal Law dated March 26, 2003 No. 35-FZ "On Electric Power Industry", the competition authority may recognize the dominant position of a business entity (group of persons) with a share of less than 20 percent based on the presence of a dominant position of such a business entity (group of persons) in the fuel markets and (or) establishing the fact that such a business entity (group of persons) exerts or is capable of exerting a decisive influence on the formation of the equilibrium price for electric energy in the corresponding zone or zones of free power transfer in a certain period of the wholesale market state, characterized by the inability to replace the supplied by such a business entity (group of persons) the volume of electrical energy by the volume of electricity supply from other business entities or by replacing the volume of electrical energy consumed by such an economic entity (group of persons) with the volume of consumption of electrical energy (power) by other consumers, as well as based on other conditions determined in accordance with the procedure established by the Government of the Russian Federation and related to the circulation of electrical energy and power in this free flow area.

41. Taking into account the above, the FAS Russia approved the order dated August 25, 2020 No. 777/20 "On determining the numerical characteristics of factors that determine the dominant position of a business entity (group of persons) with a share of the installed capacity of its generating equipment or with a share of electric energy generation using this equipment within the boundaries of the free power transfer zone of less than 20 %, and the procedure for their application"<sup>13</sup> (hereinafter – the Order).

42. It is necessary to note the relevance of the adoption of this Order by the FAS Russia, taking into account the already recorded case of recognition of an entity that did not occupy a dominant position, and at the same time, its actions (inaction) led to the restriction, elimination of competition or infringement of the interests of other business entities.

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<sup>13</sup> The Order of the FAS Russia dated August 25, 2020 No. 777/20: <http://publication.pravo.gov.ru/Document/View/0001202010160021> (Russian version only)

## 2. Heat supply industry

43. The FAS Russia has developed a practice of reviewing cases related to correcting the inefficiency of the market mechanism caused by the lack of proper regulation after the liberalization of the sector.

44. In 2019, there was a complete deregulation of prices (tariffs) for the types of goods in the field of heat supply, which are not subject to state regulation and should be determined by agreement of the parties to the contract, with the exception of the case provided for in the Paragraph 1 of the Part 2.2 of the Article 8 of the Federal Law dated July 27, 2010 No. 190-FZ "On Heat Supply"<sup>14</sup>, according to which, when selling heat energy (power) and (or) heat carrier required for the provision of utility services for heating and hot water supply to the population and categories of consumers equated to it, the regulation of prices (tariffs) in the field of heat supply remains, as well as the case provided by the Part 2 of the Article 44<sup>15</sup> of the Federal Law dated July 21, 2005 No. 115-FZ "On Concession Agreements"<sup>16</sup>

45. Since the beginning of the transition to deregulation of prices in the field of heat supply, the FAS Russia has considered 2 precedent cases on the signs of violation of the Paragraph 1 of the Part 1 of the Article 10 of the Federal Law dated July 26, 2006 No. 135-FZ "On Protection of Competition", which was expressed in the establishment of a monopolistically high price for heat energy in the form of a steam, for which indictments were made against the largest organizations. The justification and legitimacy of the decisions in these cases were confirmed by the courts of three instances.

46. The decisions on these cases by the FAS Russia are an example of proving the establishment of a monopoly high price for heat energy in the form of steam in the context of deregulation, which forms the practice of considering cases of this category for all regional offices of the FAS Russia.

### 2.1. Case of the FAS Russia against Federal Passenger Company (FPC) JSC

47. The FAS Russia considered the case on the basis of violation in the actions of FPC JSC of the Paragraph 1 of the Part 1 of the Article 10 of the Law on Protection of Competition, expressed in the establishment of a monopoly high price for the supply of heat energy in the form of steam for the consumer of Rikvest-Service LLC.

48. This is the first precedent case of the Central Office of the FAS Russia on the recognition of a violation of the existing legislation, expressed in the establishment of a monopoly high price in the specified market (it was established that the price was overstated by more than 3 times).

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<sup>14</sup> <http://www.kremlin.ru/acts/bank/31533> (Russian version only)

<sup>15</sup> Under a concession agreement, the object of which is heat supply facilities, centralized hot water supply, cold water supply and (or) wastewater disposal systems, individual objects of such systems, the establishment, modification, adjustment of regulated prices (tariffs) for goods produced and sold by the concessionaire, services rendered are carried out according to the rules in force at the time of the conclusion of such a concession agreement and provided for by federal laws, other regulatory legal acts of the Russian Federation, laws of the regions of the Russian Federation, other normative legal acts of the regions of the Russian Federation, legal acts of local self-government authorities

<sup>16</sup> <http://www.kremlin.ru/acts/bank/22649> (Russian version only)

49. The FAS Russia received an application from Rikvest-Service LLC on the presence of signs of violation of antimonopoly legislation in the actions of FPC JSC, expressed in a steep increase in prices for heat energy in the form of steam for Rikvest-LLC Service".

50. According to the analysis of the expenses of FPC JSC, which are taken into account when forming the price for heat energy (capacity) in the form of steam, the costs taken into account in the price for 2019 are several times higher than the costs taken into account in the tariff for a similar product in the previous period, and the price is not comparable (several times higher) to the price set by the regulatory authority for 2018, if the conditions of circulation of the product (heat carrier in the form of steam) remain unchanged.

51. As a result of the consideration of the case, the FAS issued a decision on the recognition of FPC JSC as violating the Paragraph 1 of the Part 1 of the Article 10 of the Law on Protection of Competition.

52. The positive effect of the consideration was the following: the deregulation mechanism allowed many contractors to form a proactive price for heat energy, beneficial to both parties to the heat supply agreement. It is unacceptable that unfair market participants use free pricing to establish or impose an unreasonably high price for steam on counterparties. This deprives the buyer of the ability to provide the required level of profitability in the production process.

53. Thus, the implemented function of the FAS Russia to consider the case against FPC JSC to establish a monopoly high price for heat supply to the end-consumer of Rikvest-Service LLC with thermal energy in the form of steam, led to a balance of interests of market participants, as well as to a decrease in the price for heat supply services for Rikvest-Service LLC.

## **2.2. Case of the FAS Russia against Russian Railways JSC**

54. The FAS Russia reviewed the case against Russian Railways JSC on the signs of violation of the Paragraph 1 of the Part 1 of the Article 10 of the Law on Protection of Competition, expressed in setting of a monopoly high price for heat energy (capacity) supplied with the use of a heat carrier in the form of steam for Rikvest –Service LLC.

55. The FAS Russia established that the boiler house belonging to the universal thermal insulation systems is the only source of heat energy in the form of steam for Rikvest-Service LLC within the boundaries of the connected heat supply network.

56. Thus, Russian Railways JSC was the only business entity operating in the market for heat supply to the end-consumer with heat energy in the form of steam within the boundaries of the heat supply networks connected to the specified boiler house.

57. At the same time, Russian Railways LLC did not intend to clear with Rikvest-Service LLC the value of the initial steam price or to revise it. Russian Railways LLC fictitiously overestimated the costs of heat production while the market conditions, steam production, and the composition of sellers and buyers remained unchanged.

58. The overestimation of costs in setting the price was proved by the analysis of the costs of Russian Railways LLC carried out by the competition authority, which were taken into account when forming the steam price for 2019.

59. After analyzing the costs of Russian Railways LLC, which are taken into account when forming steam prices, the FAS Russia came to the conclusion that the costs included in the price for 2019 are several times higher than the costs that were taken into account in previous periods. At the same time, the volumes of steam production, the composition of sellers and buyers did not change, the market situation did not change either.

60. In 2019, in accordance with the decision of the FAS Russia, Russian Railways LLC was found to have violated the Paragraph 1 of the Part 1 of the Article 10 of the Law on Protection of Competition.

61. The remedy was not issued due to the fact that during the meeting of the FAS Commission for the consideration of this case, Russian Railways LLC revised the price of heat energy in the form of steam downward and offered the indicated price to the Rikvest-Service LLC, which accepted this offer.