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Subject : **PREPARATION OF THE TTE (ENERGY) COUNCIL ON
3 DECEMBER 2007**

- a) Proposal for a Directive of the European Parliament and of the Council amending Directive 2003/54/EC concerning common rules for the internal market in electricity
 - b) Proposal for a Directive of the European Parliament and of the Council amending Directive 2003/55/EC concerning common rules for the internal market in natural gas
 - c) Proposal for a Regulation of the European Parliament and of the Council establishing an Agency for the Cooperation of Energy Regulators
 - d) Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EC) No 1228/03 on conditions for access to the network for cross-border exchanges in electricity
 - e) Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EC) No 1775/05 on conditions for access to the natural gas transmission networks
- Progress report
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I. Introduction

1. In response to the call of the Spring European Council, the Commission adopted on 19 September a 3rd Internal energy market package, comprising the five abovementioned proposals, with articles 47(2), 55 and 95 as legal bases for the two Directives and article 95 for the three Regulations. The European Parliament, the Committee of the Regions and the European Economic and Social Committee are consulted on these proposals; according to the EP current work plan, its opinions will not be available before late Spring.
2. The Working Party on Energy, since the presentation of the package, has focused mainly on the general principles of the two Directives and of the Regulation establishing the Agency. In the framework of preliminary positions Member States have been willing to discuss the general principles in a very constructive way. The impact assessment submitted by the Commission was also discussed by the WP on Energy ¹ and led to divergent views among Member States.
3. On the basis of the progress achieved during these meetings as well as consultations the Presidency, under its responsibility, draws the assessment set out in section II on ²:
 - a. the principles and provisions that meet with broad support, without prejudice to further work at drafting level;
 - b. issues, areas and options that according to a number of Member States still require discussion and orientations at the “principles” level to progress further.
4. These principles and issues are grouped according to the following topics:
 - A. Unbundling
 - B. Investment planning, New Infrastructure, Cross-border regulatory regime
 - C. Regional cooperation and solidarity
 - D. Market functioning
 - E. Regulatory powers
 - F. Regulatory Agency

¹ As required by the Interinstitutional Common Approach to Impact Assessment.

² Qualifications such as "a significant number of Member States", "most Member States", etc. reflect the Presidency's own assessment of positions expressed, noting that not all Member States intervened on all topics and that not all issues were discussed to the same extent; these qualifications should not be seen as reflecting formal votes in any sense.

5. Delegations discussed this assessment on the occasion of a High Level (Director-General level) meeting (Estoril, 5-6 November), bearing in mind the priorities identified by the Spring European Council, with a view to refining the assessment, it being understood that "nothing is agreed until everything is agreed". The High Level agreed on the need to take a quick and adequate decision on the third Internal Energy Market package. All the alternatives outlined in section II.A should be examined provided this does not delay the legislative process.
6. Having revised its report in light of the High Level's input as well as additional comments, the Presidency is of the view that it constitutes a fair and balanced assessment of the state of play that could be endorsed by the Council.

II. Principles and pending issues ¹

A Unbundling

Delegations agree that effective separation of supply/generation activities from transmission network activities has to be achieved

1. A significant number of Member States agree that this could best be achieved through **Ownership Unbundling** of the Transmission System Operator (TSO) . They believe that this is the best means to resolve the problems which arise when the TSO is a legal entity within an integrated company, namely the inbuilt incentive to treat its affiliated companies better than competing third parties and to limit new investment when this will benefit its competitors.
 - a. Minority interests of supply/generation undertakings in the TSO, provided they do not allow for control or appointment of board members, could have a different and more extended derogation period than the one currently foreseen in Art. 8(4), or be allowed under certain conditions, as long as independence in decision-making is guaranteed. Therefore further discussion is needed on:
 - whether and how Article 8 (1) should better distinguish between “Interest holding” and “Control”, notably to allow for a separate derogation on Article 8 (4);
 - to what extent financial minority shareholdings could be compatible with the objectives of the Directives.

¹ Unless otherwise indicated article numbers refer to the proposal for a Directive on Electricity.

2. Several Member States question the proportionality of the proposed provisions for ownership unbundling or ISO, that they see as infringing property rights. They consider the proposed ISO alternative, which imposes the ownership unbundling of the body responsible for infrastructure management, as a particular form of ownership unbundling. This proposed ISO cannot therefore be presented as a genuine alternative to full ownership unbundling. They express strong doubts about its functioning and the consequences of its implementation on the network, notably taking into account previous experience in some Member States. They call for the acceptance of another alternative ensuring a more effective unbundling without interfering with property rights and in line with the European Council conclusions. The Presidency invited them to come up with a concrete alternative that the Commission is ready to explore in detail.

In any case, effective unbundling should meet at least the following requirements:

- b. The implementation of effective unbundling should respect the principle of non-discrimination between the unbundling alternatives;
 - c. The obligations imposed to the overall transmission activities and investments under the different unbundling alternatives should be similar to avoid distortions between Member States in the internal market;
 - d. Be “based on independently run and adequately regulated network operation systems which guarantee equal and open access to transport infrastructures”;
 - e. Guarantee “independence of decisions on investment in infrastructure”.
3. Most of the delegations that can agree with ownership unbundling could also accept an ISO option as an alternative in order to achieve the effective separation of supply/ generation activities from transmission network activities. This ISO option should comprise the following elements:
 - f. The ISO should be responsible for granting and managing third party access, including the collection of access charges, congestion rents and payments under the inter transmission system operator compensation mechanism;
 - g. The ISO should be responsible for ensuring the long term ability of the system to meet reasonable demand through investment planning (which should include the authorisation procedure of authorized investments);
 - h. The ISO should be responsible for the operation of the system, namely dispatch management and balancing / reserve capacity markets operation;

i. The ISO should be independent when taking decisions on investment in infrastructure.

4. Items potentially relevant to all alternatives.

j. *“The implementation of effective unbundling should respect the principle of non-discrimination between the public and private sectors. To this effect, the same person should not be able to exercise any influence, solely or jointly, over the composition, voting or decision of the bodies of both transmission system operators and supply undertakings. Provided that the Member State in question can demonstrate that this requirement is respected, two distinct public bodies could control on the one hand generation and supply activities and on the other transmission activities”* (recital 12). Therefore:

- Article 8 [unbundling] should include clear provisions, building on recital 12, regarding the implementation of unbundling requirements notably for undertakings belonging to or controlled by the public sector.

k. Several countries with small and isolated markets that only recently have implemented liberalization provisions may request a derogation to the unbundling implementation. Such so-called "emergent market" clause exists in the current Gas Directive. In this respect, clarifications should be provided on the continuation of existing derogations.

l. Further discussion and definition at principles level is required notably on:

- The respective role of the national regulator, the Commission or possibly the proposed Agency for the final decision in the Certification procedure (Article 8b) and whether the national regulator decision should be reviewed only for certain undertakings;
- Derogation criteria (for gas, should the existence of a dominant external supplier, at national or regional level, be a criterion as well ? Should the criteria in littera k be cumulative or not ?) and time period;
- Whether countries with small isolated energy systems should be allowed to derogate from ownership unbundling;
- Whether the model(s) to achieve effective separation should be differentiated between gas and electricity.

m. Regarding **third country** investment in TSO or ISO, most Member States agree that:

- i) Limitations to TSO ownership by companies from third countries should not aim to discriminate against companies from third countries. These provisions should only exist to guarantee that third countries companies respect the same rules that apply to EU undertakings.
- ii) Further discussion and definition at principles level is required on:
 - The nature of the agreement enabling control by third country undertakings and criteria (such as non-discrimination, protection of investors, impact on the functioning of the European market) that these agreements should fulfil;

- Whether it would not be more advisable to have horizontal guidelines for foreign investors rather than energy-specific provisions;
 - To which extent limitations to TSO ownership by companies from third countries should apply to existing investments;
 - As a related issue, whether electricity import from third countries should be addressed.
- n. Regarding **unbundling for natural gas**, a significant number of Member States agree:
- i) There are different levels of market development in the natural gas sector across Member States, as recognized through several derogations under Directive 2003/55/CE, therefore existing derogations should be respected and
 - Further discussion and definition at principles level is required on whether derogation period for implementing new unbundling provisions should be extended for natural gas relative to electricity;
 - ii) The identification of storage facilities, to which unbundling provisions for Storage System Operators (SSOs) would apply, should be based on national, published criteria (Art.9a and 19 Gas).

B Investment planning, New Infrastructure, Cross-border regulatory regime

1. Regarding investment planning,

- a. Member States agree that one of the main purposes of this package should be to encourage investment in energy infrastructure and that better coordination of investment at EU level is necessary.
- b. Member States support a bottom-up approach, to be reflected in the Directives and Regulations, starting from the individual TSOs investment plan, to regional plans where regional fora are in place, and culminating with the non-binding EU-wide 10-year plan to be developed by ENTSOs with its scope focusing on cross-border infrastructure and investment having an impact on cross-border issues.
 - Further discussion may be needed as to the inclusion of large storage facilities in this scope and the level of autonomy of TSOs regarding investment decisions.
- c. Ensuring consistency between these three levels requires regulatory checks to be carried out, taking due account of the complementarities between the various levels:
 - by national regulators as regards individual TSOs and ISOs plan and their consistency with the non-binding EU 10-year plan and
 - by the proposed Agency as regards the non-binding EU 10-year plan and its contribution to non-discrimination, effective competition, efficient functioning of the market and security of supply.
- d. Taking into consideration the separation of activities to be achieved by the proposal, regulatory checks to ensure consistency between the various levels of investment planning should preferably be *ex ante* as part of the planning process.

2. Maintaining the possibility to grant exemption to **new infrastructure** (Art. 22 Gas) is generally accepted; it does not appear necessary to foresee concrete time-limits for these exemptions in the Directives. Further discussion is needed on:
 - Whether, in the case of exemptions for cross-border infrastructure it is not appropriate to ensure adequate consultation of the regulators concerned before the proposed Agency decides, or even to consider a two-step procedure with first, the national regulators trying to reach agreement and, second, if they fail within a certain time period or decide to call upon the proposed Agency, the proposed Agency steps in.
3. Regarding **cross-border regulatory regime** (art. 22d), this provision meets with broad support as long as it remains clear that the proposed Agency only intervenes as a last resort and subject to clarifying the content of "regulatory regime".

C. Regional cooperation and Solidarity

There is broad support to:

1. the general concept of Regional Cooperation and its importance, but further discussion is needed on: the definition of the geographical scope of the cooperation (Art. 5a), possible structural solutions at regional level, how to address congestion.
2. improving regional and bilateral Solidarity (for gas) between Member States relying to the extent possible on existing instruments and fora and market mechanisms, and as long as solidarity enhancements are largely voluntary. (Art. 5a Gas).

D. Market functioning

There seems to be broad support for the following provisions, subject to further detailed discussion:

1. regarding extended record keeping:
 - Supply undertakings need to keep at the disposal of regulators the relevant data relating to all transactions in gas/electricity supply contracts and gas/electricity derivatives;
 - With respect to derivatives, Commission needs to adopt guidelines before requirement enters into effect.
2. regarding consumers' rights:
 - consumers rights to be supplemented to guarantee that customers are informed on their energy consumption and costs more frequently, give them the right to change supplier at any time and require energy companies that bills are settled within a month after a consumer switches supplier.

Further discussion could be useful on market monitoring regarding the possible role of the future European Energy Observatory and similar bodies on national level.

E. Regulatory Powers

It is proposed to enhance regulatory powers:

- by strengthening the independence of regulators (Art. 22a)
- by defining common general objectives (Art. 22b)
- by extending the list of common duties and powers (Art. 22c)
- by foreseeing decision-making by comitology
- by overseeing the compliance of regulators with guidelines (Art. 22e).

1. Regarding **the independence, designation, objectives and supervision of the national regulatory authority**, there is a large degree of support to:

- a. The enhancement of regulator's independence and powers is necessary to ensure the effective functioning of the internal market.
- b. Member States will have to appoint one single independent regulatory authority for representation and contact purposes at EU level; this is not incompatible with the current existence of multiple regulators in a few Member States at federate/regional level.
Therefore:
 - Article 22a should be redrafted accordingly.
- c. Independence criteria as defined in article 22a (2) and (3) seems appropriate subject to further refinement of the drafting e.g. to reflect the legal autonomy of regulators and clarifying the distinction between legal acts and instructions.
- d. Regulator independence needs to be balanced with the requirement for motivated decisions and the creation of adequate mechanisms to appeal (as in article 22c (12) and (13)).
- e. The general objectives of the regulators should be set by the Directives and be in line with the scope of the Directives, which means for instance that responsibilities dealing, *inter alia*, with security of supply, energy efficiency or research however important in their own right should not be attributes of regulatory authorities. Therefore:
 - Article 22b should be amended accordingly (see Annex I).

f. When carrying out their tasks regulators have to act, where relevant, in close cooperation with other authorities, such as competition ones, and without prejudice to their competence. Therefore:

- The chapeau of Art. 22b and 22c should be amended accordingly (see Annex I and II)

2. Taking into account litterae d and f above and subject to drafting revisions, most Member States agree with the specific **duties of the regulatory authority** outlined at Annex II subject to addressing the articulation between regulator and other authorities competencies for instance regarding 22c(1) (k) and (l)[public service and social tariffs], (g)[network security], (o) [security of supply], c(3) (f) [safeguard measures], on the application of the provisions of the Directive. Duties, powers and responsibilities are set out in a manner detailed enough for not justifying to supplement this article by guidelines.

g. Further discussion and definition at principles level may however be required on:

- Whether the duties, powers and responsibilities outlined at Annex II should be equally applicable to the unbundling alternatives;
- Whether the Commission. and proposed Agency will affect the independence of the national regulators because of 22c (1)c and (3)d ;
- Whether tariffs should provide incentives to research activities by operators (22c(5))
- Whether provisions on tariffs should also include tariff calculation methodologies.

3. Regarding the adoption of **guidelines by comitology**, there is broad agreement that adopting such guidelines should remain optional for the Commission given that, to a large extent, the corresponding articles can already be implemented without these guidelines.

- Further discussion is however needed to decide whether this option should remain available to the Commission for all the articles for which it is proposed (for instance regarding public service obligations , cooperation on cross-border issues or compliance of regulators).

4. Regarding the **compliance of regulators with guidelines**, the thrust of this provision is generally supported although further discussions may be needed on:

- How to make it less cumbersome
- Assessing whether it does not undermine the regulators' independence
- Whether any regulatory authority could challenge each and every decision taken by another regulator.

F. Proposal for an Agency for the Cooperation of Energy Regulators

A significant number of Member States agree:

- a. The establishment of an independent mechanism, as a European platform for improving the coordination, of independent national regulators and of TSOs, is important for the effective functioning of the internal market and to deliver on the mandate from the European Council.
- b. In so doing the mechanism should take due account of the outcomes of regional cooperation between TSOs and between regulators.
- c. Besides a broad advisory role towards ENTSOs and the Commission, the mechanism should carry out well defined tasks where it can provide added-value, for instance promoting good practice amongst regulators or reviewing the EU 10-year investment plan, should focus on well circumscribed individual cases, mainly those related to cross-border issues and supervise TSOs' activities at EU level.
- d. Adequate means should be provided to ensure transparency, accountability and democratic control regarding the mechanism's proceedings.
- e. The mechanism should be independent both from Member States and from the Commission., representing the views from independent national regulators.
- f. The organisation of the mechanism should ensure an effective and balanced representation of Member States.
- g. Further discussion is needed on:
 - The format and legal nature of the mechanism (e.g. Agency)
 - Whether its tasks should be developed in a step-wise manner.

General objectives of the regulatory authority (Art. 22b)

In carrying out the regulatory tasks specified in this Directive, the regulatory authority shall take all reasonable measures to contribute to the following objectives within the framework of their duties and powers as laid down in Article 22c, in close consultation with other relevant national authorities and without prejudice to their competencies:

- (a) the promotion, in close cooperation with the proposed Agency, regulatory authorities of other Member States and the Commission, of a competitive, secure and environmentally sustainable internal electricity market within the Community, and effective market opening for all consumers and suppliers in the Community;*
- (b) the development of competitive and properly functioning regional markets within the Community in view of the achievement of the objective mentioned in point (a);*
- (c) the suppression of restrictions to electricity trade between Member States, including the development, of appropriate cross border transmission capacities to meet demand and enhance the integration of national markets which may facilitate electricity flow across the Community;*
- (d) promoting the development of secure, reliable and efficient systems as well as system adequacy, including through facilitating the access of new generation capacity to the grid, in particular encouraging new market entrants;*
- (e) ensuring that network operators and users are granted appropriate incentives, in both the short and the long term, to increase efficiencies in network performance and foster market integration;*
- (f) ensuring the efficient functioning of their national market, and promoting effective competition and consumer protection in cooperation with other relevant authorities.*

Duties and powers of the regulatory authority (Art. 22c)**Duties - 22c (1)**

The regulatory authorities shall have the following duties, to be carried out, as appropriate, in close consultation with other relevant national authorities and without prejudice to their own specific competencies

- (a) ensuring compliance of TSO/DSO/TSOW...with their obligations under this Directive and relevant Community legislation...;*
- (b) cooperating on cross-border issues with the regulatory authority or authorities of those Member States;*
- (c) complying with, and implementing, decisions of the proposed Agency and of the Commission;*
- (d) reporting on a yearly basis on its activity and the fulfilment of its duties to the relevant authorities of the Member States, the proposed Agency and the Commission....;*
- (e) ensuring that there are no cross subsidies between transmission, distribution and supply activities;*
- (f) reviewing investment plans of the transmission system operators and independent system operators...;*
- (g) monitoring compliance with network security and reliability rules and monitoring standards and requirements for quality of service and supply and;*
- (h) monitoring the level of transparency, ensuring compliance of electricity undertakings with transparency obligations;*
- (i) monitoring the level of market opening and competition at wholesale and retail levels..;*
- (j) monitoring the time taken by transmission and distribution undertakings to make connections and repairs;*
- (k) contributing to high standards of universal and public service for electricity, the protection of vulnerable customers, and that consumer protection measures set out in Annex A are effective;*

- (l) publishing recommendations, at least on a yearly basis, on compliance of supply tariffs with Article 3;*
 - (m) ensuring access to customer consumption data, the application of a harmonised format for consumption data and the access to data under paragraph (h) of Annex A;*
 - (n) monitoring the implementation of rules relating to the roles and responsibilities of transmission system operators, distribution system operators, suppliers and customers and other market parties pursuant to Regulation (EC) 1228/2003;*
 - (o) monitoring investment in generation capacities in relation to security of supply;*
 - (p) to monitor the implementation of safeguards measures as referred to in Article 24.*
-