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NOTE

from : General Secretariat of the Council
to : Delegations

Subject : TTE (Energy) Council on 6 June 2008
- Internal Energy Market

Delegations will find attached the content of the room document that was circulated on Friday last and on which basis the President of the Council, Minister A.Vizjak, could conclude that, although not all Member States could agree with all the elements of the package, the Council reached a broad agreement on the essential elements of this internal market package

ROOM DOCUMENT

**TTE COUNCIL
6. JUNE 2008**

1. Since the last February TTE Council, the Presidency has intensified the work on the five proposals submitted by the Commission in September 2008, in order to meet the deadline set by the last spring European Council.
2. While noting the one or other reservation delegations or the Commission might still have on specific issues or pending requests for derogations, the Presidency is of the view that the elements that are outlined in section 3 and reflected in legal texts¹, without prejudice to further adjustments of the drafting, could form the basis for a general approach on the whole package, pending the opinions of the European Parliament. At the current stage of the legislative process the Commission has to maintain a general reservation.

3. Elements towards a general approach

a/ Effective separation (Electricity D., Gas D.):

All delegations agree that effective separation of supply and production activities from network operations should be achieved in accordance with the orientations defined by the 2007 spring European Council. However, while the majority of delegations and the Commission see full ownership unbundling as the first best option, an option allowing for an Independent Transmission Operator (ITO) has been developed with the provisions outlined below; **in order to take account of cases where arrangements are in place for a transmission system that belongs to a VIU, which guarantee more effective independence of the TSO, additional provisions are introduced in Article 8 (el. D).**

These provisions aim at balancing concerns on the scope, time-frame and enforceability of this option with keeping it workable and preserving the financial interest of the vertically integrated undertaking (VIU):

¹ The latest versions of the five instruments appear in doc.9963/08 + COR1 (Electricity Directive), 9964/08 + COR1(Gas Directive), 9966/08 (Electricity Regulation), 9967/08 (Gas Regulation), .9965/08 (Agency Regulation).

- The ITO option should be available to both sectors for Member States where the transmission system belongs to a VIU on entry into force of the Directive.
- Effective and proportionate provisions on the ITO are set out in Chapter IIIa (gas) and IVa (electricity) to ensure the effective independence of the operator, its management and supervisory body, adequate access to financial resources, that it does not share certain means and resources and corporate identity with the parent company, and to avoid conflicts of interest.

Rules preventing management from having certain position or responsibility, interest or business relationship, directly or indirectly, with the VIU are targeted at management with actual decision-making power. **This should apply to the majority of that management for 3 years ex-ante, and to all for 4 years ex-post. With respect to the rest of the management, there should be a minimum period of 6 months ex-ante during which no management or other relevant activity is exercised in the VIU.** To that effect "management" in art. 10d(3) and (7) Gas D (12d(3) and (7) Elec. D) refers to the executive management level as well as the staff directly reporting to this level; moreover the regulator will vet the appointment of the executive management.

- Concerning the Supervisory body: provisions (art. 10e(3) Gas D, 12e(3) Elec. D) allow for up to half of its members plus one to be exempted from the independence rules. **The nomination of the rest of the members of the Supervisory body is subject to approval by the national regulator. The national regulator may object in the case of premature termination of a term of office, if this termination is unjustified.**

Regarding the influence of the Supervisory body on the independence of the TSO in terms of investment decisions and their financing it is recalled that, in any event, the regulator can force a) amending the investment plan, and b) implementing the amended plan.

Moreover art. 10e(1) Gas and 12e(1) Electricity clarify that the remit of the Supervisory body excludes decisions linked to the day to day activities of the ITO, to the management of the network and to the preparation of the network development plan.

- Network development and investment decisions (Art. 10g gas D., 12g electricity D.): these provisions foresee that the regulator has to examine whether the ITO network development plan is consistent with the Community-wide plan (which should reflect commitments such as achieving the 10% interconnection capacity target stated by the 2007 Spring European Council) and, in case of doubt, has to consult the Agency, thus ensuring that the views of other regulators are taken into account. On that basis the regulator could require the ITO to amend its plan. Besides, the development of investments and interconnection infrastructure are among the criteria to be taken into account for the specific review of the ITO option (art. 10i Electricity D., 12i Gas D.).
- Provisions on non-discriminatory behaviour by the ITO on its own (art. 10c(5) Gas D., 12c(5) Electricity D.) or on the influence exerted by the VIU (art.10c(9) Gas D., 12c(9) Electricity D.) are introduced.
- Access to the capital market by the ITO (art. 10b(1)) is balanced by the Supervisory body decision-making power for decisions such as approval of the annual financial plan and level of indebtedness of the TSO. (Art. 10e(1) Gas D.,12e(1) Electricity D.). It is recalled that Member States may choose (art. 10g(7) Gas D, 12g(7) Elec D) among the modalities to ensure that investment is made in case a TSO does not execute an investment (for instance Member States may choose an option of a tender open to investors rather than oblige the TSO to accept a capital increase).
Additional safeguards aiming at ensuring compliance with the provisions through effective penalties (Art. 22c(3a) Electricity D./24c(3a) Gas D.), obligatory designation of an ISO in the case of a persistent breach of its obligations by the ITO (art. 22c(3a)h electricity, 24c(3a)h). Regarding penalties, depending on whether the breach of their obligations pursuant to the Directives originates with the ITO or its parent company the penalties are defined with respect to the turnover of the ITO or of the parent company, respectively and imposed on the non-compliant company.
- In order to avoid that compliance be limited to formal compliance it is clarified that any decisions or prior approvals taken by regulators/Agency are without prejudice to any duly justified future use by the regulators of their powers or to penalties by other authorities or the Commission (Art. 22c(1a) Electricity D., 24c(1a) Gas D.).

- Review: **as part of the general review** the Commission will conduct a specific review of the ITO-related provisions **and using effective and efficient unbundling as a benchmark**, to be conducted at an early stage (2 years after implementation) on the basis of objective criteria (**competition, development of network and infrastructure - in line with the 2007 Spring European Council orientations -, security of supply**), leading, where appropriate, **no later than 3 years after implementation** to proposals to ensure fully effective independence of the TSO.
- **Level playing field: three different models of unbundling will exist in the internal energy market with the present proposal. Measures that the Member States have the possibility to take pursuant to this directive in order to ensure a level playing field have to be compatible with the Treaty and the EU legislation. These measures have to be proportionate, non-discriminatory and transparent. In addition, Article 12a (El. D.)/10a(gas D.) which is redundant given the Article 8(7) (El. D./7(7) Gas. D.) that has been included in the Presidency's text, will be deleted.**

b. Minority shareholding:

The Presidency text does not exclude minority shareholding of producer/supplier in TSO under the condition that this does not entail **any control or any influence** of one on the other and cannot lead to a conflict of interest (Art. 8(2) electricity D., 7(2) gas D.). While producers/suppliers should be allowed to have minority shares in the TSO, the TSO should not be allowed to have shares in the producer/supplier company.

The case of net final customers that also perform, in a marginal way, the functions of generation/supply of electricity is handled under Art.26(3) electricity D.

c. Public ownership:

The Presidency text contains the possibility to achieve ownership unbundling with two separate public bodies through a provision recognising that two distinct public bodies can be considered as two persons for the purpose of implementing ownership unbundling (Art. 7(5a) gas D., 8(5a) electricity D.).

- d. **Third country clause** (Art. 8a and 30(1) electricity D., 7a and 33(1) gas D.):
Irrespective of the option retained to achieve effective separation, **the text needs to ensure that the issue of third country control of networks is addressed** in a non-protectionist way **which guarantees that these companies** respect the same rules that apply to EU undertakings **and addresses Member State concerns about third country control. It also needs to address concerns** about potential implications on Community competence and the handling of existing investment. To that effect, the text **needs to clarify the criteria against which investment from third country would be assessed in particular the EU security of supply.**
- e. **Certification/designation of TSOs** (Art. 8b, 8c and 10 electricity D., 7b, 7ba and 9 gas D., Art. 2aa and 2ab electricity and gas R.s):
The streamlined procedure set out in the above articles applies to all options, gives a preponderant role to the national regulator during its different phases and allow for extensive consultations at all stages. The Commission **may give an opinion on the regulator's draft decision and the national regulator shall take the utmost account of the Commission's opinion.**
- f. **Derogations:**
Derogations for small/isolated systems have been confirmed, with nominative derogations for CY/LU/MT for both sectors (gas D. Art. 28(1),(2) and (6) and Electricity D. Art. 26(3)) as well as derogation for EE/FI/LV regarding gas until any of these Member States is directly connected to the system of other Member State than EE/FI/LV/LT. Moreover, consistency between these derogations and provisions on combined operators (Art. 15 gas D., Art. 17 electricity D.) has been ensured.
- g. **Adoption of network codes** (electricity and gas R.s):
The Presidency text has introduced a new, more streamlined procedure for the establishment and adoption of network codes, set out in Art. 2ba (both R.s). This procedure clearly allows for the possibility to make these codes binding after extensive consultations of all stakeholders, especially on the industry side, as well as adequate involvement of the Agency. These codes are without prejudice to the Member States' right to establish national codes for non-cross border issues.

h. regulatory authorities (art. 22a to 22c, electricity D., 24a to 24c gas D.

– Independence

Strict provisions (art. 22a(2 and 3), resp. 24a(2 and 3)) ensure the independence of regulators in terms of means and decision-making powers; this does not mean however that regulators are free from judicial control or can ignore broader objectives e.g. on environmental sustainability or on public service obligations, as stated in art. 22b electricity, 24b gas.

– multiple regulators:

The Presidency text ensures that the principle of a single regulator at national level combined with unique representation (e.g. at the Agency) is compatible with the current existence in some Member States of regulators at regional/federal level or for small and isolated parts of the territory (Art. 22a(1a),(1b), respectively 24a(1a),(1b)).

– regulatory powers/duties:

Art. 22c electricity D. /24c gas D define a comprehensive series of duties for national regulators and grants them the necessary powers. This text ensures that, when carrying out these duties, regulators have the possibility to act, where relevant, in close cooperation with other authorities, such as competition ones, while preserving their independence and without duplicating the tasks (e.g. monitoring) usually carried out by other authorities. With a view to reflecting the specificities of the ISO and ITO options, additional powers are granted to regulators with respect to ISOs (art. 22c(2) electricity, 24c(2) gas) and ITO (22c(3a) electricity, 24c(3a) gas).

i. handling of cross-border cases [regulatory regime¹ / exemptions for new infrastructure / new interconnectors]:

For the topics of the regulatory regime (Gas/Electricity D.s Art. 24e/22e, Agency R. Art. 7a), and the exemptions for new infrastructure (Gas D. Art. 22) and for new interconnectors (Electricity R. Art. 7), the Presidency compromise provides for a two-step approach, involving the Agency only as last resort after attempts to solve the issue between the national authorities concerned or when they so decide and with consultation at the national level all along the process. Moreover, for the exemptions for new infrastructure/interconnectors, it allows for Member States to take the final formal decision. In the Presidency's view, these provisions achieve the right balance between a reasonably fast procedure and adequate involvement of the national level.

¹ Referred to in the Agency Regulation as "terms and conditions for access and operational security for cross border infrastructure"

j. Guidelines

– Comitology procedure for the adoption of guidelines:

The adoption of guidelines through comitology procedure has been made optional and is now limited to fewer articles than in the Commission proposals; in the remaining instances the scope of these guidelines has been clarified and narrowed.

– Compliance with guidelines adopted by comitology:

The text (art. 22e electricity D., 24e gas D.) has narrowed down the scope of this Article to cross-border trade insofar as a regulator can lead the Commission to examine another regulator's compliance.

k. Regional cooperation/Regional solidarity:

The Presidency compromise [electricity and gas D.s (Art. 5a, resp. 5b) and R.s (Art. 2h both)] provides for a more flexible definition of the geographical scope of this regional cooperation and that due account of the outcome of this cooperation is taken, notably in relation with the tasks conferred upon the Agency (Agency R. Art. 6(6)).

In order to avoid that these provisions hinder the work of existing regional cooperation fora, it is provided that monitoring compliance with measures to ensure that discriminatory and anticompetitive conducts are excluded should be carried out by the compliance officers of the vertically integrated TSOs participating in this (regional) undertaking. In any case, general competition rules apply to any undertaking set up to implement this cooperation.

Regarding the related provisions on regional solidarity (art. 5a, Gas D.) they build, to a large extent, upon existing mechanisms (e.g. Directive on security of gas supply) and remain fairly flexible as to the manner in which to contribute to this solidarity, e.g. relying on market-based mechanisms or not.

l. Market functioning including retail markets:

The Presidency text (art. 22f electricity D., 24f gas D.) includes provisions regarding extended record keeping (supply undertakings need to keep at the disposal of regulators the relevant data relating to transactions in supply contracts and gas/electricity derivatives) and regarding consumers' rights (guaranteeing that customers are properly informed on their energy consumption and costs frequently enough to regulate their electricity/gas consumption, give them the right to change supplier at any time and require energy companies that bills are sent within three months after a consumer switches supplier) (Annex in both D.s). Moreover, the provisions (new Art. 23 electricity D., new 25 gas D) on retail markets have been streamlined, and the explicit reference to cross-border markets deleted.

m. Gas specific issues:

While extending some of the provisions of the current Directive to storage and LNG facility or operator the text gives ample discretion to Member States. The latest texts leave it to Member States to define criteria for granting access to storage facilities (Art. 19 gas D.), which is taken into account in the requirements for legal and functional unbundling (Art. 9a gas D.), and set only fairly general conditions for the provision of third party access services concerning storage and LNG facilities (Art. 4a R). Besides, the text provides some flexibility, notably through a two-year transition period, regarding the basis for the calculation of network tariffs (Art. 3(1) gas R.)

n. The Agency:

- **principle:** The Presidency compromise provides for a regulatory Agency, independent from the Member States and the Commission, with well circumscribed tasks.
- **tasks:** the Agency focuses on issues involving more than one Member State as far as binding decision-making is concerned; its involvement in technical matters (establishment of codes) has been strengthened, but is still of an advisory nature; it generally allows for the national levels to play their parts (e.g. two-step approach for defining regulatory regimes and proposing ISOs). In all these tasks, market participants and authorities at national level are duly consulted and due account is taken of the outcomes of regional cooperation between TSOs and between regulators.
- **Internal balance of powers:** The Presidency text provides for
 - a strong Regulatory Board, comprised of representatives of the national regulators, with decision-making rules giving them equal weight and a Director of the Agency acting in accordance with the Regulatory Board;
 - a lean and efficient Administrative Board consisting of six members, five of them being appointed by the Council and one by the Commission, with partial rotation ensuring adequate participation of Member States over time.
- **Transparency:** with a view to improving democratic control, transparency provisions have been significantly strengthened, e.g. on the interests of Boards members.
- **Review clause:** the Presidency text contains a review mechanism, with strong input from the Regulatory Board (Art. 30 Agency R.).