Europeanising Energy Policy

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The EU Council's call at the EU Summit, the first ever summit on energy policy, on 4 February to europeanise EU energy policy signals a new and more robust approach to energy policy at the EU level(1).

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FOTO: Anže PetkovšekDespite the recession putting breaks on the world economy in the recent years, the IEA still expects world energy demand to grow by 45 % between 2006 and 2030, with demand in China and India doubling over this period[2]. With fossil fuels expected to represent 70% of the EU's energy mix by 2030 based on the "business as usual" scenario, and dependency on imports to reach 94% and 83% for oil and gas by then, ensuring safe, secure, sustainable and affordable energy is regarded as key to the EU's continued prosperity . With total investment needed in the electricity and gas sector between now and 2020 estimated at over € 1 trillion, the Council announced a number of priorities for the new European energy policy, the key ones of which are discussed below.

Building a Truly Pan-European Energy Market

The Council has declared the completion of internal market for gas and electricity by 2014 as its foremost priority. This is the first time that such a deadline has been set. According to the Commission's recent study, achieving a fully functioning and competitive European electricity and gas market could add an extra 0.6% - 0.8% to the EU's GDP by 2020, create employment and curtail inflation.

The Third Energy Package ("TEP"), which will enter into force on 3 March this year, was adopted as a further step in the process of creating an internal market for gas and electricity. Although an essential pillar of Commission's initial draft of the TEP, the requirement of ownership unbundling of energy generation and supply from transmission network ownership and operation was replaced by "effective unbundling" in the final version of TEP after extensive lobbying from vertically integrated energy companies. Sceptics in the sector believe that this last minute compromise, which leaves it up to the Member States ("MS") to choose between three "effective unbundling" options (of which ownership is one), means that TEP will not deliver on its objective and that further legislation will be necessary.

PHOTO: Alenka ŽumbarEmphasising the new powers granted to EU institutions in respect of energy policy under the Lisbon Treaty (see Article 194 of the Consolidated version of the Treaty on the Functioning of the European Union), the Council has made clear that, if need be, further legislative measure will be drawn up to achieve the 2014 objective.

In fact, the ability to adopt further detailed rules to create a single energy market has been granted for the first time to the Commission in TEP. Specifically, the Commission has been accorded the power to adopt binding network codes concerning inter alia transparency, third party access and energy efficiency of electricity and gas networks across the EU. These network codes, many in the sector believe, will significantly and effectively remove the real barriers to competition in the energy sector. From a practical point of view for all of us involved in the energy sector, this means that going forward we can expect detailed rules and regulations affecting technical and the day-to-day running of energy companies to be promulgated at the EU rather than the national level. Following what is happening at the EU level and partaking in discussions at the EU level will therefore be crucially important for energy companies.

The European Networks for Transmission System Operators for Gas and Electricity (known as "ENTSOS") have already started drafting framework guidelines concerning inter alia electricity balancing, capacity allocation management for gas, and capacity allocation and congestion management for electricity. Based on these framework guidelines the drafting of binding network codes is expected to start later this year.

In its conclusions on 4 February, the Council called on the Agency for Cooperation of Energy Regulators ("ACER") to, together with transmission system operators, step up the work on market coupling, framework guidelines and network codes. On 3 March, the very day on which it officially starts working, ACER will published the Draft Framework Guidelines on Capacity Allocation Mechanisms for the European Gas Transmission Network for the purposes of public consultation.

Member States have until 3 March to give effect in their national laws to the provisions of TEP. The Commission has made clear in the Summit background papers that it expects that MS to meet the deadline. It is clear that Slovenia will not comply with the deadline. The draft Slovenian Energy law is expected to be submitted to the government for review on 8 March and if all goes well the law is expected to be adopted by the Slovenian Parliament in November this year. At this point it is not clear whether any other MS will find itself in a similar position. It should be noted that the Commission can commence infringement proceedings against a MS which fails to transpose EU law on time pursuant to article 258 of the Treaty on the Functioning of the European Union.

Concerning infringement proceedings, it should also be noted that 40 infringement proceedings are pending against 20 MS for failing to implement and apply the second energy package of 2003. The Commission issued 35 reasoned opinions against 20 MS, including Slovenia, in June last year. MS had until the end of August last year to respond to the reasoned opinions. In the absence of a satisfactory response from the MS concerned, the Commission is under the Treaty free to refer the matter to the European Court of Justice. It is quite likely that the Commission will commence legal proceedings before the ECJ in respect of the breaches of the second package on 3 March 2011. It is likely to use this to signal a more robust approach to energy policy going forward at the EU level in line with the Council's priorities.

Infrastructure Priorities by 2020

The Council declared that no MS should remain isolated from the European gas and electricity networks after 2015 or see its energy security jeopardized by lack of the appropriate connections. Investments of over € 1 trillion are need by 2020 to modernise and expand Europe's energy infrastructure, provide for increasing and changing demand, interconnect networks across borders and integrate electricity from renewable sources. In the shorter term, the Commission estimates that for the completion of priority projects the EU needs at least € 19bn for gas pipelines and € 6bn for electricity transmission before 2013.

The TEP package brings important changes in respect of the evaluation of new infrastructure projects going forward by requiring national regulators to evaluate new investments not solely on the basis of benefits to the MS granting the authorisation but by reference to the broader EU-wide benefits. However, recognising that a far more ambitious policy framework must be put in place to ensure that the infrastructure priorities are achieved by 2020, the Council proposed on 4 February that the following actions be taken.

First, the Council has called for the streamlining of the authorisation procedures and has asked the Commission to prepare a proposal in this regard in the coming months. While respecting national competences and procedures, the Commission is expected to propose a one-stop shop for authorising projects of "European interest" whereby a single national authority would coordinate the entire permitting process. It is understood that the Commission is also considering setting time limits for the issue of decisions by the competent authority in respect of each stage of the permitting process. Presumably careful considerations will be given to circumscribe the ability of companies to "country shop" between MS to try to take advantage of the fact that some MS have more lax environmental and planning laws than others.

Second, since the bulk of the investment in infrastructure investments will be made by private companies and thus financed through tariffs, the Council emphasised the importance of ensuring that tariffs are set in a transparent and non-discriminatory manner at levels consistent with financing needs and the appropriate cost allocation for cross-border investments, enhancing competition and competitiveness as well as taking account of their impact on consumers.

Third, recognising that some infrastructure projects, which may be justified from a security of supply/solidarity perspective, will require some public finance to leverage private funding the Council has invited the Commission to adopt a new method for defining European priority projects and the financial support needed to realise them by June of this year. Projects declared of "European interest" will be eligible for financial support from the EU in the form of grants, equity participations, guarantees, public-private partnership loans or EU project bonds. Why the existing guidelines for trans-European energy networks as set out in Decision No 1364/2006/EC need replacing is not clear from the background papers.

At present, the infrastructure priorities for the region of South East Europe are (i) the Central Eastern and South Eastern Europe Electricity Connection, (ii) the North and South Eastern Europe Gas Interconnector (from the Baltic to the Adriatic) and (iii) the Southern Corridor. It is expected that these projects will be amongst the European interest projects proposed by the Commission in June.

Finally, given the long lead-in time for changes to be achieved in the energy sector, the Council has called for the adoption of a low carbon 2050 strategy. This strategy is to provide a complete roadmap of measures to be adopted between 2020 and 2050 to ensure that the EU objective of reducing greenhouse gas emissions by 80-95% compared to the levels in 1990, as required by the IPCC, is achieved by 2050.

Achieving the Energy Efficiency Target

Both the Commission and the Council have expressed concern that the 20% energy efficiency target is presently not on track to be realised by 2020. The Commission has made clear in the background documents presented at the EU Summit that it regards the quality of MS' National Energy Efficiency Action Plans as disappointing.

In view of this the Council has proclaimed energy efficiency as a key priority action going forward. Referring to the new powers granted to EU institutions under the Lisbon Treaty in respect of energy policy, the Council called for a new approach to be taken to the issue of energy efficiency from a pan-European perspective. The Commission is expected to publish its Energy Efficiency Plan in March setting out further policies and measures to be adopted across the full energy supply chain to achieve the target. Concrete regulatory proposals are expected to follow during the course of the year addressing the issues of access to finance, the availability of innovative financing products, incentives to induce energy-efficiency investments as well as the role of EU funding, including existing structural funds.

In addition, the Council has called for MS to prescribe by 1 January 2012 energy efficiency standards based on the EU headline target in respect of public procurement contracts for public buildings and services. What, therefore, is clear is that this year will bring lots of new regulation at the EU level regarding energy efficiency.

Europeanising EU's External Energy Policy

In a further step in europeanising energy policy, the Council has called for greater coordination and coherence in the EU's external energy policy and relations. In the background document prepared for the purposes of the Summit, the Commission called for the EU to formalise the principle whereby in bilateral energy relations with key partners and in global discussions MS must act for the benefit of the EU as a whole. The fact that in the same paragraph reference is again made to the new power granted to EU institutions in respect of energy policy under the Lisbon Treaty undoubtedly reveals the Commission's ambitions concerning the strengthening of EU's external energy policy. These statements will undoubtedly ring alarm bells in most capitals across the EU.

Although these statements have not expressly been endorsed by the Council in its conclusions, the Council has invited the Commission to submit a communication on security of supply and international cooperation aimed at further improving the consistency and coherence of the EU's external action in the field of energy by June 2011. According to the Commission, this document will propose mechanisms to align existing international agreements (notably in the gas sector) with the internal market rules and to strengthen cooperation between Member States for the conclusion of new ones. What effect this may have on the South Stream project and other Gazprom related projects in the EU is unclear. There is no doubt, however, that the faster these projects are concretised, the more difficult it will be for the EU to try to unwind, should it decide to do so.

As a further step in coordinating EU external energy policy, the Council has invited MS to start informing the Commission of all their new and existing bilateral energy agreements with third countries from 1 January 2012 onwards. Pursuant to the current proposal it is envisaged that the Commission will, having due regard to the need to protect commercially sensitive information, provide this information to other MS. This is likely to be another matter which will be strongly resisted by MS.

The Council has also endorsed the Commission's proposal to extend and deepen the Energy Community Treaty by integrating neighbouring countries, in particular transit and Mediterranean countries (Ukraine joined in February) and extending new acquis communitaire to the existing signatories to the Treaty. Without specifically referring to Gazprom and Russia but clearly with them in mind, the Council called for the Commission to develop measures it sees necessary to ensure a level playing field for power producers within the EU with those outside the European Economic Area. It would seem from this, that the third country certification procedure for transmission system operators owned by non-EU nationals set out in the TEP (dubbed the "Gazprom clause") are regarded by the Commission and the Council as not sufficient to address what the EU sees as imbalance in the level playing field. Given Russia's and Gazprom's objection to the so called "Gazprom clause", it is likely that any further measures adopted by the Commission in this regard will be strongly objected to by them.

When taken together with Council call to diversify routes and sources of supply of oil and gas to the EU and its emphasis on the Southern Corridor, this may well mean that any agreement with Russia will be impossible. It is unclear, therefore, how the Council considers that these policies and actions can be pursued in conjunction with its other declared priority of developing an energy partnership with Russia.

The proposed europeanisation of EU external energy policy is the most important change to EU's energy policy going forward and which will probably raise the most controversy. There is no doubt that the Commission expects to play a much greater role in devising EU foreign policy in the field of energy. The infringement proceedings it brought against Poland in July last year in respect of the Gazprom territorial clause is likely to be a taste of what is to come.

Conclusion

The EU Summit on 4 February seems to mark a watershed in EU energy policy. The Commission and the Council have said that the time for a truly European energy policy has come. There is little doubt that both consider the new powers granted to EU institutions concerning energy policy by the Lisbon Treaty as key to this new approach to EU energy policy. Whether or not the MS intended for broad powers to be granted to EU institutions under this article, it is clear that the Commission and Council believe that they have such powers.

If it is shown that TEP does not lead to the creation of the single energy market by 2014, both the Council and the Commission have made clear that a new package of measures will be adopted. This may well mean that energy companies and MS who fought hard and successfully resisted ownership unbundling during the TEP negotiation and who plan to adopt the independent transmission operator (ITO) or independent system operator (ISO) options of effective unbundling under TEP have simply delayed its adoption rather than precluded it. In this case they must start preparing for ownership unbundling as it may happen much sooner than anyone would have anticipated at the time TEP was being negotiated.

It is clear that the europeanisation of EU's energy policy will bring significant changes to the way the EU energy sector operates and is to be regulated much sooner than many in the industry had anticipated and, perhaps, would wish. An understanding of EU energy law and involvement in its drafting will, therefore, undoubtedly become even more important than it has been to date.

[1] *European Council, Conclusions on Energy European Council, 4.2.2011 (**MORE**).*
[2] *IEA, World Energy Outlook 2010.*

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