

## *Energy*

### **Practitioner Insights: ACER and Cross-Border Harmonization**

How do you realize the goal of a single EU-wide energy market work when the transmission networks within each member state and their interconnections are owned by dozens of operators that are regulated by 28 separate national regulatory authorities (NRAs)? And how do you accommodate new energy-generation patterns or cross-border power flows while dealing with the physical constraints that existing transmission infrastructure imposes?

Developing more flexible and reliant integrated networks at the cross-border level is a hot topic today. Europe added 6.1 gigawatts of wind capacity in the first half of 2017, according to WindEurope. Some 2.9 gigawatts were installed in Germany alone, where renewable electricity generating plants have been producing much more power than German consumers are using and doing so at prices that prove disruptive to interconnected markets.

What can be done so that a situation like Germany's overcapacity of wind generation can be turned into benefits for all member states rather than continuing the headaches of the German and neighboring TSOs?

One answer to this problem is ACER—the EU Agency for the Cooperation of Energy Regulators. Created under a dedicated EU regulation No. 713/2009 and officially launched in 2011 in Ljubljana, Slovenia, ACER has gained importance in European efforts to advance the development of the EU's internal gas and power markets. The agency is perhaps best known for its work in monitoring wholesale energy markets under the REMIT reporting scheme ((EU) No. 1227/2011) and issuing formal opinions on the proposals of the European networks of transmission system operators for electricity and gas (ENTSO-E and ENTSO-G) on EU-wide standards for the operation of the electricity and gas networks and network development plans.

In some of its recent decisions, ACER has begun to show how it can help resolve potential disputes among different member states on dealing with the interaction of increasingly interdependent national energy infrastructure systems.

The future role of ACER will likely be decided as the internal power market reform, which the European Commission launched in November 2016, takes shape. As part of the Clean Energy for All Europeans package of initiatives, commonly referred to as the Winter Package, the Commission proposed recasting the regulation

establishing ACER. Unsurprisingly, much of this new proposal is dedicated to adjusting the balance between ACER and national regulatory authorities (NRA) and coordinating initiatives affecting regional and EU-wide cooperation. Indeed, the Commission seeks to add a new layer for coordination and oversight for regional decision-making procedures, strengthening the agency's position.

**Structure and Governance** Managing the integration of highly meshed power systems hobbled by various problems from past policies and business decisions is a complicated task. ACER's composition proves how political balance remains an essential ingredient in advancing and integrating EU energy markets.

ACER is managed by a director appointed by an Administrative Board. The European Commission and the European Parliament each appoint two members to the Board, while the European Council, representing member state governments, appoints five. Key decisions and agency positions related to cooperation of transmission system operators (TSOs), including establishing EU-wide network codes, NRA compliance with EU law on power and gas markets, and access to and operational security of cross-border infrastructure, require a two-thirds majority approval of the Board of Regulators, representing NRAs of all member states. On a number of occasions, however, the agency has failed to obtain the necessary support from the Board of Regulators.

One way to advance the development of the single EU energy market from a regulatory point of view would be to turn ACER into a single, central regulatory authority with wider ranging powers and more autonomy from national authorities. The Commission took this approach in the clean energy proposal, and in its preliminary report the European Parliament's Committee on Industry, Research and Energy sided with the Commission. In some cases the parliamentary rapporteur suggested going even further.

Under the Winter Package, ACER could gather more momentum by lowering voting thresholds—two-thirds in place of unanimity or simple majority replacing the two-thirds qualified majority voting, for instance. ACER would gain control over a broader range of issues, as it currently has no power to issue binding decision. Noteworthy is the proposed power of issuing binding decisions addressed to ENTSO-E and ENTSO-G to ensure their compliance with the overall regulatory framework. The parliamentary draft report also aims at strengthening ACER's position when requesting information the agency considers necessary to fulfill its tasks. ACER's powers would increase with respect to regional initiatives whenever it identifies a tangible im-

pact of proposed measures on the internal energy market.

While we wait to see how far the Commission, Parliament, and member states are prepared to travel down that road as part of the Energy Union project, it is helpful to focus on how ACER has started to use its existing clout in the power market to determine where its greatest strengths may be.

**Where We Stand Today** The Third Energy Package of 2009, comprised of three regulations and two directives, is in many ways really an enabling framework for developing the single EU-wide gas and electricity markets, each currently composed of a series of regional markets with varying degrees of integration. The adoption of these measures, and their implementation by individual EU member states, has been followed by a range of subsidiary regulations, such as the network codes. These in turn sometimes require transmission system operators or other bodies to cooperate to formulate the follow-up, often highly technical rules or methodologies, that markets depend on at both the intraregional and inter-regional levels and affect not only power market players, but more generally the economies of the member states.

For a multitude of issues ACER is effectively a specialized advisory body to other authorities, in particular the Commission, rather than a decision-maker. In this scenario, it's required to give opinions related to the re-design of the regulatory framework. This includes establishing ENTSOs and monitoring their activities and rules on regional cooperation, and drafting network codes and network development plans.

The EU regulation on cross-border power exchanges (No. 714/2009) includes only one instance where ACER was expressly authorized to issue a legally binding decision. It concerns exemptions for new cross-border merchant lines where the national regulatory authorities are not able to reach an agreement within a specific deadline or jointly request ACER to resolve the matter instead.

The ACER regulation, however, includes a broader delegation of decision-making powers, when access to and operational security of cross-border infrastructure are concerned. This includes issues that fall within the competence of NRAs, but again, only when authorities are not able to reach an agreement by a specific deadline or jointly request ACER to resolve the matter. Disputes of this kind include procedures for capacity allocation, the time frame of such allocation or sharing congestion revenues or charges for the use of interconnectors. The Commission was authorized by member states to adopt detailed guidelines to be followed in such cases.

**CACM Regulation** The European Commission has made extensive use of this delegation by adopting the Capacity Allocation and Congestion Management Regulation in 2015. It sets an ambitious target for the 2017-2019 period for the introduction of regionally coordinated day-ahead and intraday capacity markets, preparation of a flow-based capacity calculation model, and use of market coupling as a standard capacity allocation arrangement.

ACER was already involved in what could prove to be a landmark case under the new regulation regarding the delimitation of capacity calculation regions. It required a unanimous proposal of all European NRAs.

The Austrian regulatory body E-Control opposed it and regulators could not reach agreement by the prescribed deadline.

Public consultations were launched in June 2016 and touched on significant issues like the merger of the Central and Western European and Central and Eastern European regions, as well as the introduction of new bidding zone borders among a number of transmission systems. The European Commission's Directorate-General for Energy was consulted on how to handle the matter; the Commission supported ACER in intervening directly, which could be interpreted as a vote of confidence in the agency's ability to resolve politically sensitive issues that are likely to arise particularly during the process of power market integration.

Last November, ACER adopted decision No. 06/2016, overruling E-Control's objections to introducing a new bidding zone border between Germany/Luxembourg and Austria, effectively splitting what was a single trading region into two capacity calculation regions. The division will require introducing a cross-border capacity allocation procedure and will alter conditions for cross-border power trading in those regions.

E-Control and two Austrian TSOs—Austrian Power Grid AG and Vorarlberger Übertragungsnetz GmbH—as well as Verbund AG, the country's leading electricity company, appealed against ACER's decision to the agency's Board of Appeal. Among those supporting the decision were regulatory authorities of three other member states and two more transmission system operators. In March, ACER's Board of Appeal found the appeal of Verbund AG inadmissible and dismissed all other appeals as unfounded.

The decision of ACER's Board of Appeal raises a few interesting points. First, the case sparked a lot of interest in the affected regions, with 45 requests for intervention from 19 applicants filed in addition to approximately 100 statements in support for the interventions.

Most of these requests were dismissed for lack of direct and individual interest in the results of the case. The Board of Appeal also did not recognize the statements in support of interventions as part of the proceedings. This greatly limits the ability of individuals, businesses, and professional organizations to affect the outcome of regulatory procedures that could significantly influence market conditions in the respective jurisdictions. While efficiency of proceedings, thus protected, is a notable priority, one could consider admitting positions filed by professional organizations and consumer representation at least as the voice of the *amicus curiae*, or friend of the court.

The Third Energy Package of 2009—and the Winter Package of 2016 to a greater extent—recognized the need for public consultations when the complex regulatory framework for energy is developed by authorities and specialized entities like the TSOs. Nevertheless, with ACER's wide-ranging powers to amend proposals presented by NRAs or TSOs, certain aspects of such cases may transpire only after the decision takes final shape. The further appeal procedure with the Court of Justice of the European Union is even more formalized. If this part of the procedure does not change, then only member states will be able to consider positions and insights of business and consumer organizations once they reach the Luxembourg court. Clear channels of communication with domestic stakeholders will prove invaluable for this purpose.

Second, the intervention of Verbund AG requires some attention. The company argued that its direct and individual concern in the result of the proceedings with the ACER Board of Appeal rests in Verbund's 100 percent shareholding in the affected transmission system operator, Austrian Power Grid AG. Based on the case law that supports this argument, Verbund AG said its position as the sole shareholder, by reason of factual circumstances, differentiated it from all other persons and thereby distinguished the company individually in the same way as the addressee—the Austrian TSO.

Calling upon the rules of TSO unbundling, ACER's Board of Appeal dismissed that argument. The Board found that based on the principle of transmission system operator independence from the remainder of the vertically integrated undertaking, such as Verbund AG, the company had no direct control over the structure and activities of the TSO, and thus the differentiating component discussed in the relevant case law was missing. It is an interesting effect of the unbundling regime, which independent investors in cross-border merchant lines will likely consider.

Two cases currently lodged with the Court of Justice of the European Union (the General Court) aim to overturn the decision of ACER's Board of Appeal. The way the court handles these precedent matters will show-case to what extent the decision-making powers of ACER are recognized. The European Commission may be expected to take interest in the outcome of these cases beyond the immediate effect on the capacity calculation regions. One can anticipate that the views of the court will become reflected in the final version of the regulatory framework currently discussed as part of the Winter Package initiative.

**ACER's Soft Powers** In many respects, 2015 was a landmark year for ACER. Apart from the introduction of the CACM Regulation and the agency's involvement in its implementation, ACER issued its first two opinions assessing the compliance of NRAs' decisions with the relevant provisions of EU legislation on energy markets. Although these opinions are nonbinding, they provide an excellent tool for dispute avoidance or amicable dispute resolution of issues that could arise with the advancing integration of national energy markets into regional structures.

In November 2014, Lithuania's National Commission for Energy Control and Prices (NCC) sought an opinion on the compliance of its approach to the methodology for the calculation of regulated transmission prices. The NCC adopted a decision moving from a distance (point-to-point) to an entry-exit tariff system. In its first opinion, published in July 2015, ACER found misalignment in some of the methodologies and invited the NCC to remove these to achieve compliance with EU law.

In this case, a national regulatory authority made its own decision subject to a compliance check by the dedicated EU authority. The authority and, as a consequence, the market participants were able to determine if gas pricing policies were in line with the relevant EU law before any dispute arose or business was affected. ACER's soft power proved a useful tool in securing uniform implementation of EU-wide rules without launching an infringement investigation or court proceedings.

The second case preceded the problem of delimiting capacity calculation regions that came to light following adoption of the CACM regulation. It closed a 10-

monthlong investigation into a number of national regulatory authority decisions in the Central-Eastern European region on compliance with guidelines on the management and allocation of available transfer capacity of interconnections under Regulation 714/2009. In contrast to the NCC, which sought confirmation about the compliance of its own proposed rules with EU law, the Polish national regulatory authority requested a compliance assessment of decisions taken by authorities in four other jurisdictions in the context of significant uncontrolled power flows (loop-flows) related to commercial power exchanges between Austria and Germany.

ACER found that interconnections at three borders in the region, as well as network elements within Germany, were subject to structural congestion—a legal term that involves not only congestion on interconnectors themselves, but also congested elements of neighboring power systems that are required for management of cross-border flows. ACER found that the corresponding NRAs' decisions were not in line with requirements of Regulation 714/2009 and invited the transmission system operators and Central-Eastern European regulatory authorities to take remedial action, including potential transitory regulatory measures to prepare market participants for any changes in how the power markets would be organized. This also was the main reason behind the subsequent introduction of the new bidding zone border between Germany/Luxembourg and Austria discussed earlier.

The assessment was formulated in a nonbinding opinion. The Austrian transmission system operators and the national regulatory authority appealed against it to the ACER Board of Appeal. Although these appeals were found inadmissible, Austria's E-Control lodged a further case with the General Court of the European Union. In June, the court dismissed the action (Case T-63/16). Most notably the court confirmed that under Article 8 of the ACER regulation, the agency was authorized to issue the opinion on compliance of cross-border capacity allocation rules between two regions.

In a more recent case, ACER again issued an opinion based on the request from the Lithuanian regulatory authority, this time clarifying the application of certain provisions of the European Commission's guideline on forward capacity allocation. The guideline set a six-month deadline for the NRAs to adopt coordinated decisions on long-term transmission rights. Coordinating those decisions meant setting up capacity calculation regions, which required ACER's intervention and took some time to be completed. The Lithuanian regulatory authority found itself obstructed by the lack of a corresponding regulation for a month following entry in force of the guideline, until ACER adopted its decision No. 6/2016 on capacity calculation regions.

In its application, the Lithuanian NRA sought legal certainty as to the application of EU law to determine if it was justified to extend the deadline for complying with the forward capacity allocation guideline. ACER adopted opinion No. 10/2017 providing the required clarification and confirming the extension of the deadline in April. By doing so, the agency ensured uniform application of the relevant regulation among NRAs across the EU.



**Conclusion** It appears that ACER has the capacity to be a useful venue for consultations on the uniform application of EU standards and designs for the power market when cross-border issues arise. These matters usually involve complex and interrelated technical and economic problems, and the insight of a specialized body like ACER would prove invaluable, especially when a quick fix is unavailable or would not serve market users' interests well.

The European Commission seems to be convinced of the vital role of ACER in the development of the internal electricity market. The Winter Package takes advantage of the procedure that ensures compliance of specific regulatory measures with a wider framework by proposing to expand the competences and decision-making powers of ACER. The European Parliament so far supports the Commission; the draft report suggests even certain enforcement measures further strengthening the position of the agency in its relations with the national regulatory authorities.

The ability to adopt binding decisions is naturally attractive to authorities and often guarantees the effectiveness of measures. The option to issue nonbinding opinions that don't penalize the national authorities involved should be underscored, however. With the growing interdependence of power systems and markets, especially after the implementation of the CACM regulation and Winter Package reform, referring future cases to a specialized body like ACER and allowing for more flexible approach to solutions may be more attractive

than making matters immediately subject to more formalized and stringent infringement or litigation procedures.

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