

TO THE MINISTERIAL COUNCIL OF THE ENERGY COMMUNITY  
represented by the Presidency and the Vice-Presidency of the Energy Community

In case ECS-8/15, the Secretariat of the Energy Community against Ukraine, the

ADVISORY COMMITTEE,

composed of

Rajko Pirnat, Alan Riley, Helmut Schmitt von Sydow, Verica Trstenjak, and  
Wolfgang Urbantschitsch

pursuant to Article 90 of the Treaty establishing the Energy Community ('the Treaty') and  
Article 32 of Procedural Act No 2008/1/MC-EnC of the Ministerial Council of the Energy  
Community of 27 June 2008 on the Rules of Procedure for Dispute Settlement under the  
Treaty as amended on 16 October 2015 ('Dispute Settlement Rules 2015'),

acting unanimously,

gives the following

OPINION

**I. Procedure**

By e-mail dated 28 May 2018 the Energy Community Presidency asked the Advisory Committee to give an Opinion on the Reasoned Request submitted by the Secretariat in case ECS-8/15 against Ukraine. The members of the Advisory Committee received the Reasoned Request and its annexes.

In its Reasoned Request the Secretariat seeks a Decision from the Ministerial Council declaring that Ukraine failed to fulfil its obligations arising from Energy Community law. The Secretariat argues that by maintaining in force its current regime for allocation of cross-border capacity for transit of electricity, Ukraine fails to fulfil its obligations under the Energy Community Treaty, and in particular Article 41 thereof, Articles 3(1), 12(f) and 32(1) of Directive 2009/72/EC, Articles 16(1) and 19 of Regulation (EC) 714/2009 as well as Section 2.1 of the Congestion Management Guidelines as incorporated and adapted by Decision 2011/02/MC-EnC of the Ministerial Council of the Energy Community of 6 October 2011.

Ukraine did not submit a reply to the Reasoned Request within the deadline ending on 28 June 2018.

On 26 September 2018 the Advisory Committee held a public hearing in order to assess the facts, the applicable law and the legal questions.

**II. Preliminary Remarks**

According to Article 32 (1) of the Procedural Act No 2008/01/MC-EnC of the Ministerial Council of the Energy Community on the Rules of Procedure for Dispute Settlement under the Energy

Community Treaty, the Advisory Committee gives its Opinion on the Reasoned Request, taking into account the reply by the party concerned. In the present case Ukraine did not respond to the Reasoned Request. Ukraine also had a further opportunity to present a response in the public hearing held on the 26th September 2018, however Ukraine did not attend the public hearing and make a presentation as to its position in relation to the issues in this case.

The Advisory Committee, exercising its duty to give an Opinion on the Reasoned Request does not duplicate the procedure and therefore does not collect evidence itself. The Advisory Committee gives its Opinion on the basis of undisputed facts. Where the facts were not sufficiently determined by the Secretariat, including the Reasoned Opinion, the Advisory Committee is not in a position to give its decisive legal opinion on these allegations; instead, such cases of incomplete determination of facts are pointed out in the Opinion of the Advisory Committee.

On the basis of these principles the Advisory Committee assessed the Reasoned Request and the relevant documents, discussed the legal topics which were brought up and came to the following conclusions.

### **III. Provisions allegedly violated by the Contracting Party concerned**

Article 41 of the Treaty reads:

- 1. Customs duties and quantitative restrictions on the import and export of Network Energy and all measures having equivalent effect, shall be prohibited between the Parties. This prohibition shall also apply to customs duties of a fiscal nature.*
- 2. Paragraph 1 shall not preclude quantitative restrictions or measures having equivalent effect, justified on grounds of public policy or public security; the protection of health and life of humans, animals or plants, or the protection of industrial and commercial property. Such restrictions or measures shall not, however, constitute a means of arbitrary discrimination or a disguised restriction on trade between the Parties.*

Article 3(1) of Directive 2009/72/EC as incorporated and adapted by Decision 2011/02/MC-EnC reads

*Contracting Parties shall ensure, on the basis of their institutional organisation and with due regard to the principle of subsidiarity, that, without prejudice to paragraph 2, electricity undertakings are operated in accordance with the principles of this Directive with a view to achieving a competitive, secure and environmentally sustainable market in electricity, and shall not discriminate between those undertakings as regards either rights or obligations.*

Article 12(f) of Directive 2009/72/EC as incorporated and adapted by Decision 2011/02/MC-EnC reads

*Each transmission system operator shall be responsible for [...] ensuring non-discrimination as between system users or classes of system users, particularly in favour of its related undertakings; [...]*

Article 32(1) of Directive 2009/72/EC as incorporated and adapted by Decision 2011/02/MC-EnC reads

*Contracting Parties shall ensure the implementation of a system of third party access to the transmission and distribution systems based on published tariffs, applicable to all eligible customers and applied objectively and without discrimination between system*

*users. Contracting Parties shall ensure that those tariffs, or the methodologies underlying their calculation, are approved prior to their entry into force in accordance with Article 37 and that those tariffs, and the methodologies - where only methodologies are approved - are published prior to their entry into force.*

Articles 16(1) of Regulation (EC) 714/2009 as incorporated and adapted by Decision 2011/02/MC-EnC reads:

*Network congestion problems shall be addressed with non-discriminatory market-based solutions which give efficient economic signals to the market participants and transmission system operators involved. Network congestion problems shall preferentially be solved with non-transaction based methods, i.e. methods that do not involve a selection between the contracts of individual market participants.*

Article 19 of Regulation (EC) 714/2009 as incorporated and adapted by Decision 2011/02/MC-EnC reads:

*The regulatory authorities, when carrying out their responsibilities, shall ensure compliance with this Regulation and the Guidelines adopted pursuant to Article 18. Where appropriate to fulfil the aims of this Regulation the regulatory authorities shall cooperate with each other, with the Energy Community Secretariat and the Energy Community Regulatory Board in compliance with Chapter IX of Directive 2009/72/EC.*

Section 2.1 of the Congestion Management Guidelines reads:

*Congestion-management methods shall be market-based in order to facilitate efficient cross-border trade. For that purpose, capacity shall be allocated only by means of explicit (capacity) or implicit (capacity and energy) auctions. Both methods may coexist on the same interconnection. For intra-day trade continuous trading may be used.*

#### **IV. Legal Assessment**

As the alleged points of non-compliance raised by the Secretariat are manifold, this opinion will – in the interest of improved readability – follow the structure of the Secretariat’s Reasoned Request. It has to be noted to begin with that all the allegations remained undisputed throughout the entire dispute settlement procedure.

The Secretariat stated a number of legal provisions allegedly violated by the Ukrainian wholesale electricity market system. As there are so many specific legal provisions concerned by certain aspects of this system, it is not necessary to resort to the most general provision of Article 7 of the Treaty prohibiting any discrimination. Article 7 of the Treaty is only a subsidiary remedy if there were no more specific Treaty provisions available. This subsidiarity – explicitly spelled out in Article 18 TFEU – also applies to Article 7 of the Treaty considering the principle of *lex specialis derogat legi generali* and its extremely wide scope of application.

##### ***(a) Allocation of Interconnection Capacity for Transit Based on Unilateral Administrative Action by the Energy Ministry and Discrimination Between Exports and Imports.***

There are two principal allegations. First, the allocation of interconnection capacity for transit based on unilateral administrative action by the Ministry of Energy and Coal Industry. Second, discrimination in the allocation of cross-border transit capacity so that the rules that apply to exports are different to those that apply to imports.

It follows from Articles 12(f) and 32(1) of Directive 2009/72/EC that allocation of transit capacity based on a unilateral administrative decision of the Ministry fails to comply with the third party access principles contained in those articles and the requirements therein to operate on the basis of published tariffs

In respect of the allocation of capacity for import and exports of electricity different rules have been applied. Allocation of cross-border capacity for export is performed by the Transmission System Operator (TSO) Ukrenergo under the market-based Auction Rules 2017. However, for imports of electricity allocation of capacity is subject to the Ministry of Energy approval and is only permitted to meet balance requirements when there is a shortfall in domestic supply. The impact of such an approval procedure and balancing limitation on imports is to exclude allocation of cross-border capacity for commercial imports. This clearly constitutes discrimination and was deemed unlawful by Opinion of the Advisory Committee and subsequently confirmed by the Ministerial Council in Case ECS 1/12.

Furthermore, the procedure for actually allocating interconnector capacity for the purpose of transit in Ukraine is itself discriminatory. The State-owned undertaking Ukrinterenergo is exclusively provided with transit capacity as this is the only entity permitted to execute contracts with foreign undertakings for the transit of electricity. Underpinning this exclusivity the TSO was instructed to accept only Ukrinterenergo's requests for interconnection capacity for transit.

The Court of Justice of the European Union in Case C-17/03 VEMW (para 50-56) took the view that reserving capacity to the benefit of certain system users deprives all other actual or potential system users of the possibility to access the network for that particular capacity.

These three elements - the ministerial allocation of interconnection capacity; the discrimination between import and export capacity allocation; and the exclusivity in respect of transit capacity of Ukrinterenergo – are incompatible with Energy Community law, namely Article 3(1) of Directive 2009/72/EC which requires Contracting Parties *not to discriminate between electricity undertakings* as regards either rights or obligations; Article 32(1) of Directive 2009/72/EC which requires them *to ensure access to the transmission system for all third parties in an objective manner and without discrimination*; Article 12(f) Directive 2009/72/EC according to which the transmission system operator is responsible for *ensuring non-discrimination* as between system users or classes of system users, particularly in favor of its related undertakings.

It should be noted that Article 3(14) of that Directive provides a possibility for derogation from its Article 32(1) *"insofar as [its] application would obstruct the performance, in law or in fact, of the obligations imposed on electricity undertakings in the general economic interest and insofar as the development of trade would not be affected to such an extent as would be contrary to the interests of the Energy Community."*

However, in order for Ukraine to benefit from the derogation it would need to comply with Article 3(2) of Directive 2009/72/EC. In particular, any such obligation *"shall be clearly defined, transparent, non-discriminatory, verifiable and shall guarantee equality of access for EU electricity companies to national consumers..."*. Furthermore, the Court of Justice emphasised in its VEMW judgment (para 63) that the effect of a discriminatory measure such as priority capacity allocation would significantly imperil and even block the access of new operators to the market, and protect the position of companies in the situation of Ukrinterenergo against competition.

In addition, throughout both this case and Case ECS-1/12 Ukraine did not invoke any exemption from the principle of non-discriminatory access to interconnectors for imports due to reasons of ensuring public service obligations. It is for the defending Contracting Party to

invoke and then justify the grounds for the application for a discriminatory priority access scheme and to demonstrate that all the conditions under the Directive are met.

***(b) Failure to Deal with Network Congestion Problems with Non-Discriminatory Market Based Solutions***

The second allegation again concerns the requirement for approval from the Ministry of Energy to the transit of electricity. The Ministry does not permit private parties access to interconnectors and prevents participation in auctions for cross-border capacity to undertakings without Ministerial approval.

This capacity allocation regime appears to be in breach of Article 16(1) of Regulation (EC) 714/2009 and Section 2.1 of the Congestion Management Guidelines. Article 16 in particular requires that network congestion problems are addressed with non-discriminatory, market based solutions which give efficient economic signals to market participants and transmission system operators. Section 2.1 of the Congestion Management Guidelines in Section 2.1 expands on the obligations contained in Article 16(1) of Regulation (EC) 714/2009 by specifying that congestion management methods shall be market-based and capacity shall be allocated only by means of explicit (capacity) or implicit (capacity and energy) auctions.

By decision of 23<sup>rd</sup> September 2014 in accordance with Article 94 of the Treaty, the Ministerial Council extended the application of Regulation (EC) 714/2009 in full to the Energy Community States and to situations where there were interconnections and cross border flows between ECT and EU States.

Given that Regulation (EC) 714/2009 and specifically Article 16 (1) and Section 2.1 of the Congestion Management Guidelines apply in full to the ECT Contracting Parties there is a breach of those provisions as to require a unilateral administrative decision by a Ministry as a basis for the allocation of interconnectors, and not via competitive procedures such as explicit or implicit auctions. This amounts to maintaining a non-market based method for capacity allocation that does not give efficient economic signals to the market participants and transmission system operators. The Advisory Committee has already given its opinion on this same point and with the same result in Case ECS 1/12.

***(c) Infringement by virtue of establishing measures equivalent to quantitative restrictions***

The third allegation is that the making the transit of electricity depending on prior approval by the Ministry of Energy makes the transit of electricity in Ukraine more difficult than purely domestic supply and prima facie constitutes a measure having equivalent effect to a quantitative restriction prohibited by Article 41 of the Treaty.

The Court of Justice has held in numerous cases, as for example in Case C-393/92 *Gemenle Almelo* that it would be incumbent on the defendant to justify its measures by referring to e.g. Article 41(2) of the Treaty or to mandatory requirements in the general interest. However, Ukraine has made no such demonstration.

Therefore Ukraine has breached Article 41 of the Treaty.

***(d) Compliance with the Congestion Management Guidelines***

The fourth allegation concerns the application of the Congestion Management Guidelines, that is required under Article 19 of Regulation (EC) 714/2009. Under the Guidelines the national regulatory authority has an obligation to ensure compliance with that Regulation, including its Congestion Management Guidelines.

Ukraine has not taken any effective remedial action to ensure full compliance and implementation of its Auction Rules by *Ukrenergo* with the *acquis communautaire*.

Thus Ukraine has failed to fulfil its obligation under Article 19 of the Regulation (EC) 714/2009.

#### **IV. Conclusions**

The Advisory Committee considers that Ukraine has failed to comply with its obligations under the Energy Community Treaty, and in particular Article 41 thereof, Articles 3(1), 12(f) and 32(1) of Directive 2009/72/EC, Articles 16(1) and 19 of Regulation (EC) 714/2009 as well as Section 2.1 of the Congestion Management Guidelines as incorporated and adapted by Decision 2011/02/MC-EnC of the Ministerial Council of the Energy Community of 6 October 2011.

Done in Vienna on 6 November 2018

On behalf of the Advisory Committee



Wolfgang Urbantschitsch, President