

II

(Acts adopted under the EC Treaty/Euratom Treaty whose publication is not obligatory)

DECISIONS

COMMISSION

COMMISSION DECISION

of 26 February 2007

establishing that Article 30(1) of Directive 2004/17/EC of the European Parliament and of the Council coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors applies to the supply of electricity and gas in England, Scotland and Wales

(notified under document number C(2007) 559)

(Only the English text is authentic)

(Text with EEA relevance)

(2007/141/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Whereas:

Having regard to the Treaty establishing the European Community,

Having regard to Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors ⁽¹⁾, and in particular Article 30(4) and (6) thereof,

Having regard to the request submitted by the United Kingdom by e-mail of 24 October 2006 and confirmed by a signed fax of the same date, and to the additional information requested by Commission staff by e-mail of 17 November 2006 and submitted by the United Kingdom by e-mail of 27 November 2006,

Having regard to the conclusions of the independent national authority, the Office of the Gas and Electricity Markets (OFGEM), that the conditions for the applicability of Article 30(1) of Directive 2004/17/EC would be met,

(1) Article 30 of Directive 2004/17/EC provides that contracts intended to enable the performance of one of the activities to which the Directive applies shall not be subject to the Directive if, in the Member State in which it is carried out, the activity is directly exposed to competition on markets to which access is not restricted. Direct exposure to competition is assessed on the basis of objective criteria, taking account of the specific characteristics of the sector concerned. Access is deemed to be unrestricted if the Member State has implemented and applied the relevant Community legislation opening a given sector or a part of it.

(2) This legislation is listed in Annex XI of Directive 2004/17/EC, which, for the electricity sector, refers to Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity ⁽²⁾. Directive 96/92/EC has been superseded by Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC ⁽³⁾, which requires an even higher

⁽¹⁾ OJ L 134, 30.4.2004, p. 1. Directive as last amended by Council Directive 2006/97/EC (OJ L 363, 20.12.2006, p. 107).

⁽²⁾ OJ L 27, 30.1.1997, p. 20.

⁽³⁾ OJ L 176, 15.7.2003, p. 37. Directive as last amended by Commission Decision 2006/653/EC (OJ L 270, 29.9.2006, p. 72).

degree of market opening. In respect of the gas sector, Annex XI refers to Directive 98/30/EC of the European Parliament and of the Council of 22 June 1998 concerning common rules for the internal market in natural gas ⁽⁴⁾. Directive 98/30/EC has been superseded by Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC ⁽⁵⁾, which requires an even higher degree of market opening.

- (3) Under Article 62(2)(2) of Directive 2004/17/EC, Title III of that Directive setting out the rules on service design contests does not apply to contests organised for the pursuit, in the Member State concerned, of an activity to which the applicability of Article 30(1) of the Directive has been established by a Commission decision or has been deemed applicable under the second or third subparagraph of Article 30(4) or the fourth subparagraph of Article 30(5).
- (4) The request submitted by the United Kingdom concerns the supply, both wholesale and retail, of electricity and gas in England, Scotland and Wales. Although there may be some similarities, the respective characteristics, in particular the very limited degree of substitutability, nevertheless render it appropriate to consider that there are two different product markets, one for gas and one for electricity, rather than one product market for 'energy'.
- (5) Given the unified character of the markets for electricity of the three geographical areas concerned by the present request and the limited capacity ⁽⁶⁾ of the connections between the United Kingdom networks and those of other areas of the Community, England, Scotland and Wales should be considered to constitute the relevant market for electricity for the purposes of evaluating the conditions laid down in Article 30(1) of Directive 2004/17/EC. In respect of gas, it should also be concluded that the relevant geographic market is Great Britain, since, as noted by the British Office of Fair Trade, 'this is the limit of the gas trading regime: although gas is traded with continental Europe through the Bacton-Zeebrugge interconnector, quantities traded are relatively small.' The same applies to quantities traded between Great Britain and Northern Ireland (not covered by this Decision) and Ireland. These conclusions are consistent with one of the findings of the Communication from the Commission to the Council and the European Parliament:

⁽⁴⁾ OJ L 204, 21.7.1998, p. 1.

⁽⁵⁾ OJ L 176, 15.7.2003, p. 57.

⁽⁶⁾ Of the order of approximately 4 % of peak demand in the case of electricity.

Report on progress in creating the internal gas and electricity market ⁽⁷⁾, hereinafter referred to as the '2005 Report', that 'in economic terms ... electricity and gas markets in the EU remain national in economic scope'.

- (6) This assessment, and any other contained in this Decision, is made solely for the purposes of Directive 2004/17/EC and is without prejudice to the application of the rules on competition.
- (7) In respect of electricity, the United Kingdom has implemented and applied not only Directive 96/92/EC but also Directive 2003/54. Concerning gas, the United Kingdom has also implemented not only Directive 98/30/EC, but also Directive 2003/55/EC. Consequently, and in accordance with the first subparagraph of Article 30(3), access to the market should be deemed not to be restricted, both in respect of electricity and gas.
- (8) Direct exposure to competition should be evaluated on the basis of various indicators, none of which are, per se, decisive. In the 2005 Report, the Commission stated that 'many national markets display a high degree of concentration of the industry, impeding the development of effective competition' ⁽⁸⁾. Consequently, it considered that 'one indicator for the degree of competition on national markets is the total market share of the biggest three producers (electricity) and wholesale suppliers (gas)' ⁽⁹⁾. According to the latest available information, the aggregate market share of the three largest electricity generators of the total production is 39 % ⁽¹⁰⁾, while the aggregate market share of the three largest gas shippers in percentage of the wholesale market is 36 % ⁽¹¹⁾. Both these levels must be considered to be at a satisfactorily low level and should be taken as an indication of direct exposure to competition.
- (9) The degree of liquidity is also a good indicator of competition, as the conditions of competition in electricity and gas supply are greatly influenced by liquidity in wholesale markets. The United Kingdom wholesale market for electricity is characterised by being a bilateral trading market, with brokered deals. There is also more than one power exchange, although UKPX has the largest volume. Some of the principal actors on the wholesale market are the owners of generation capacity, with ownership of generation capacity being rather diverse with eight

⁽⁷⁾ COM(2005) 568 final of 15.11.2005.

⁽⁸⁾ See p. 2. See also the 'Report from the Commission: Annual Report On The Implementation Of The Gas And Electricity Internal Market', COM(2004) 863 final of 5.1.2005, p. 4.

⁽⁹⁾ See the 2005 Report, p. 7.

⁽¹⁰⁾ See Commission Staff Working Document, Technical Annex to the 2005 Report, SEC(2005)1448, p. 44, table 4.1. Hereafter referred to as Technical Annex.

⁽¹¹⁾ Technical Annex, p. 55, table 5.1.

companies sharing around 70 % of capacity. For the United Kingdom, liquidity multiple term trading amounts to around three times the amount consumed⁽¹²⁾. This degree of liquidity should be considered as being satisfactory, i.e. it is such as to constitute an indicator of a well-functioning and competitive wholesale market. For the gas sector, liquidity multiple term trading should also be considered to be at a satisfactory level, as it also amounts to two to three times total consumption⁽¹³⁾. At the retail levels as well, there are a sufficient number of actors, as there are six main suppliers active in the household market with additional companies active in the large user sector.⁽¹⁴⁾ The gas markets are also characterised by a sufficient number of active players and can be summarised as follows: 'The (United Kingdom) gas market has a high level of competition with around 10 companies active in the wholesale market. As with electricity, six companies account for the majority of the domestic supply market ... (of which) ... five are new entrants to the gas supply market. Larger users buy direct from the wholesale market, which also includes many major oil companies'⁽¹⁵⁾. These factors should therefore be taken as an indication of direct exposure to competition.

- (10) The workings of the balancing markets should also be considered as indicators, not only in respect of production but also for the wholesale and retail markets. In fact, 'any market participant who cannot easily match its generation portfolio to the characteristics of its customers may find itself exposed to the difference between the price at which the TSO (transmission system operator) will sell imbalance energy, and the price at which it will buy back excess production. These prices may either be directly imposed by the regulator on the TSO; or alternatively a market based mechanism will be used in which the price is determined by bids from other producers to regulate their production upwards or downwards ... a key difficulty for small market participants arises where there is the risk of a large spread between the buying price from the TSO and the selling price. This occurs in a number of Member States and is likely to be detrimental to the development of competition. A high spread may be indicative of an insufficient level of competition in the balancing market which may be dominated by only one or two main generators. Such difficulties are made worse where network users are unable to adjust their positions close to real time'⁽¹⁶⁾. Since the introduction of the British Electricity Trading and Transmission Arrangements (BETTA) there has been

a unified balancing market for England, Scotland and Wales. Furthermore, its main characteristics (market based pricing, half-hourly gate closures and a fairly low spread) are such that it should be taken as an indicator of direct exposure to competition. Similarly for gas, balancing prices are derived on the basis of a market mechanism operated by the TSO. Imbalances are settled on a daily basis and there is not usually a significant spread between the buy and sell price. This non discriminatory mechanism does not act as a barrier to suppliers.

- (11) Given the characteristics of the products concerned here (electricity and gas) and the scarcity or unavailability of suitable substitutable products or services, price competition and price formation assume greater importance when assessing the competitive state of the electricity and gas markets. The number of customers switching supplier is an indicator of genuine price competition and, thus, indirectly, 'a natural indicator of the effectiveness of competition. If few customers are switching, there is likely to be a problem with the functioning of the market, even if the benefits from the possibility of renegotiating with the historical supplier should not be ignored'⁽¹⁷⁾. Furthermore, 'the existence of regulated end-user prices is clearly a key determinant of customer behaviour ... Although the retaining of controls may be justified in a period of transition, these will increasingly cause distortions as the need for investment approaches'⁽¹⁸⁾.
- (12) In the UK, the degree of switching for the three categories of users of electricity — large and very large industrial users, small and medium-sized industrial and business, and very small business and household users — is above 70 % for the first two groups and close to 50 % for the last category⁽¹⁹⁾ and end-user price control was abolished in respect of electricity in 2002⁽²⁰⁾. Concerning gas, the degree of switching for the three categories of users — large and very large industrial users including power plants, small and medium-sized industrial and business, and very small business and households — is above 70 % for the first two groups and close to 50 % for the last category⁽²¹⁾. Price controls for all end users have been removed since 2002. The situation in the United Kingdom is therefore satisfactory as far as switching and end-user price control are concerned and should be taken as an indicator of direct exposure to competition.

⁽¹²⁾ See the Preliminary Report of the Sector Inquiry into Competition in Gas and Electricity Markets (in the following referred to as 'Preliminary Report'), Figure 42, p. 113.

⁽¹³⁾ Preliminary Report, point 64, p. 25.

⁽¹⁴⁾ Technical Annex, p. 177.

⁽¹⁵⁾ Technical Annex, p. 178.

⁽¹⁶⁾ Technical Annex, p. 67.

⁽¹⁷⁾ 2005 Report, p. 9.

⁽¹⁸⁾ Technical Annex, p. 17.

⁽¹⁹⁾ 2005 Report p. 10.

⁽²⁰⁾ Technical Annex p. 177.

⁽²¹⁾ 2005 Report p. 10.

- (13) In view of these indicators and given the overall picture of this sector in England, Scotland and Wales — in particular the extent to which networks have been unbundled from generation/supply and the effective regulation of network access — that emerges from the information submitted by the United Kingdom, the 2005 Report and the Technical Annex thereto as well as from the Preliminary Report, the condition of direct exposure to competition laid down in Article 30(1) of Directive 2004/17/EC should be considered to be met in respect of electricity and gas supply in England, Scotland and Wales. As noted in recital 7, the further condition of free access to the activity must be deemed to be met. Consequently, Directive 2004/17/EC should not apply when contracting entities award contracts intended to enable the supply of electricity and/or gas generation to be carried out in these geographical areas nor when they organise design contests for the pursuit of such an activity there. It is recalled that contracts awarded for the pursuit of other activities, such as the distribution of electricity and gas, continue to be subject to the provisions of Directive 2004/17/EC.
- (14) This Decision is based on the legal and factual situation as of November 2006 as it appears from the information submitted by the United Kingdom, the 2005 Report and the Technical Annex thereto. It may be revised, should significant changes in the legal or factual situation mean that the conditions for the applicability of Article 30(1) of Directive 2004/17/EC are no longer met.
- (15) The measures provided for in this Decision are in accordance with the opinion of the Advisory Committee for Public Contracts,

HAS ADOPTED THIS DECISION:

Article 1

Directive 2004/17/EC shall not apply to contracts awarded by contracting entities and intended to enable them to carry out electricity and/or gas supply in England, Scotland and Wales.

Article 2

This Decision is based on the legal and factual situation as of November 2006 as it appears from the information submitted by the United Kingdom, the 2005 Report and the Technical Annex thereto. It may be revised, should significant changes in the facts or the legal situation mean that the conditions for the applicability of Article 30(1) of Directive 2004/17/EC are no longer met.

Article 3

This Decision is addressed to the United Kingdom of Great Britain and Northern Ireland.

Done at Brussels, 26 February 2007.

For the Commission

Charlie McCREEVY

Member of the Commission