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European Commission ends long-running investigation by accepting Gazprom commitments

On 24 May 2018 the European Commission made binding a set of commitments offered by Russian gas company Gazprom to ensure the free flow of natural gas at competitive prices in Central and Eastern European (CEE) gas markets. The decision formally closes the Commission's probe into Gazprom's suspected abuse of dominance in these markets (in contravention of Article 102 of the Treaty of the Functioning of the European Union (TFEU)). The Commission opened formal proceedings in September 2012, following a series of dawn raids in September 2011, and issued a Statement of Objections in April 2015. The Commission's market test on commitments offered by Gazprom, opened in March last year, prompted a range of responses from companies, governments, regulators and industry experts and led the Commission to seek an improved proposal from Gazprom.

The Commission's concerns

The Commission's preliminary view was that Gazprom was pursuing an overall strategy to partition CEE gas markets with the aim of maintaining an unfair pricing policy in several CEE Member States. The Statement of Objections alleged that Gazprom had implemented this strategy by:

- hindering cross-border gas sales, in particular, by imposing territorial restrictions in its supply agreements with wholesalers to prevent the export of gas in eight EU Member States.[1] This included export ban clauses and "destination clauses" (which stipulate that gas purchased from Gazprom may only be sold or used within the country in which it was delivered);
- implementing an unfair pricing policy in five of those Member States (Bulgaria, Estonia, Latvia, Lithuania and Poland) by using a specific price formula (linking the price of gas to the price of oil products) that largely seems to have favoured Gazprom over its customers; and

[1] Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland and Slovakia.

- leveraging its market dominance in Bulgaria and Poland by making gas supplies conditional upon receiving gas transport infrastructure-related commitments from wholesalers. In particular, the Commission alleged that:
  - Gazprom made sales to the Bulgarian gas wholesaler conditional on the latter's participation in Gazprom's South Stream pipeline project in Bulgaria; and
  - supplies in Poland were conditional on maintaining Gazprom's control over investment decisions in the Yamal pipeline project (which otherwise would have allowed gas from alternative suppliers to enter the Polish market).

The binding commitments

The Commission may decide to accept binding commitments offered by the undertakings concerned in light of a possible infringement of Article 101 or 102 TFEU (under Article 9 of Regulation 1/2003) rather than adopt an infringement decision (under Article 7 of Regulation 1/2003). Under the commitments that the Commission has made binding, Gazprom must:

- ensure that there are no more contractual barriers to the free flow of gas in the CEE region, including by: (i) removing all contractual barriers to the free flow of gas, regardless of whether cross-border sales are rendered financially less attractive or even impossible; and (ii) not re-introducing such clauses in the future;
- take active steps to integrate gas markets in the CEE region and facilitate gas flows to and from isolated markets. Gazprom is obliged to allow customers that purchased gas originally for delivery to Hungary, Poland or Slovakia to elect to have all or part of it delivered to Bulgaria and/or the Baltic states, and *vice versa*, at four months' notice;
- commit to a structured process to ensure competitive gas prices. Gazprom is required to ensure that, for contracts with a minimum duration of three years:
  - its customers have a contractual right to demand a price reduction where the price diverges from competitive Western European price benchmarks, including at liquid hubs; and
  - any new gas prices must be set in line with levels in competitive Western European gas markets. Arbitration procedures will result if Gazprom fails to agree on a new price within 120 days; and
- remove demands obtained by leveraging its dominance in gas supply. In particular, Gazprom is prohibited from seeking damages from its Bulgarian partners following termination of the South Stream project.[2]

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[2] However, according to the decision, it is not possible to impose similar restrictions with regards to the Yamal pipeline, as gas relations between Russia and Poland are determined by intergovernmental agreements and cannot therefore be altered by antitrust procedure.

Significance of the decision

The commitments will remain legally binding for eight years.[3] However, Gazprom can request a review in certain circumstances, including where circumstances have changed such that Gazprom is no longer a dominant market player in any or all of the CEE Member States.

Non-compliance with the commitments may result in a fine of up to ten per cent of worldwide turnover. This can be imposed without the Commission having to prove an infringement of EU antitrust rules.

Commissioner Margrethe Vestager **announced** the decision by noting that it would remove obstacles created by Gazprom to the free flow of gas in CEE and provide a "*tailor-made rulebook for Gazprom's future conduct*" without the need for a financial penalty. The Commissioner explained that the Commission had not pursued an infringement decision so as to prompt Gazprom to take positive steps to integrate isolated gas markets, stating that "*a fine would not have achieved all of our competition objectives in this case*" despite the fact that "*some would have liked [this] no matter the solution on the table*".

Other developments

State aid

European Commission orders Germany to recover illegal aid from certain large electricity users exempted from network charges in Germany

The European Commission has **ruled** that network charge exemptions in force in Germany between 2012 and 2013 for large electricity users contravened State aid rules. Germany must now calculate and recover the illegal aid from each beneficiary. This is the first time that the Commission has decided on a case involving a full exemption from electricity network charges.

In Germany all electricity users connected to the grid are required to pay fees to the network operator to cover service and network maintenance costs. Large users generally have more predictable usage, and therefore generate fewer network costs. Reflecting this, in 2011 Germany introduced an exemption from network charges for electricity users with an annual consumption of more than 10 gigawatt hours and stable consumption. The exemption saved large users circa €300 million in network charges in 2012.

In 2012 a levy, known as the section 19 surcharge, was imposed on consumers in order to finance the large users' network charges exemption. The surcharge was abolished in 2014.

Consumer associations, energy companies and German citizens complained to the Commission about the section 19 surcharge, and in March 2013 the Commission opened a State aid investigation in respect of it.

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[3] Gazprom's commitment not to claim damages resulting from the cancellation of the Bulgarian South Stream project will remain binding for 15 years.

On 28 May 2018 the Commission announced that:

- Proceeds from the section 19 surcharge constitute State resources, as consumers must pay them by law and the German State has control of the proceeds.
- Consequently, the exemption for large electricity users between 2012 and 2013 was funded by State resources and was therefore State aid.
- There was no objective justification for the large user exemption. Large users created network costs and used network services despite having predictable consumption. However, as large stable users generated fewer network costs than other electricity users, market conditions justified a partial exemption from network charges during the relevant time period.

The Commission has set out in its decision the methodology for calculating the amount of illegal aid that must be recovered from beneficiaries. Germany must now calculate and then recover that aid.

General competition

SAMR announces campaign against unfair competition

On 17 May 2018 China's newly-formed State Administration for Market Regulation (SAMR) **announced** a nationwide campaign against unfair competition from May to October 2018. The campaign focuses on four areas, namely: (i) misleading market conduct and infringement of intellectual property rights (e.g. unauthorised or misleading use of another undertaking's label, name, packaging or trademark); (ii) commercial bribery in the pharmaceutical and education sectors; (iii) deceptive internet advertising so as to mislead consumers regarding, for example, the nature, functionality, or quality of a product; (iv) strengthening co-governance amongst undertakings and industry associations and establishing a fair and orderly competitive landscape. Other sectors that were named include online trading and rural markets (with the SAMR being particularly concerned with misleading market conduct and infringement of intellectual property rights in the sales of daily necessities and alcohol in rural markets, as opposed to urbanised areas).

As discussed in our **briefing** on the establishment of the SAMR, the technology sector may also be on the SAMR's radar, given the State Intellectual Property Office is now part of the SAMR and a SAMR official has reportedly stated that the agency would soon issue regulations on internet-technology-based antitrust conduct.

Regulatory

Ofgem publishes policy consultation on default tariff cap proposals

The Office for Gas and Electricity Markets (Ofgem) has published a **policy consultation** on the design and implementation of the proposed temporary default tariff cap. The temporary cap will initially apply to domestic energy customers on standard variable and default tariffs (SVTs) from late 2018 until 2020.

The proposal for a temporary price cap followed work by Ofgem and the Competition and Markets Authority's (CMA) findings in the 2016 Energy Market Investigation, which concluded that the energy market is not working well for domestic energy customers who are on SVTs. The government has since proposed legislation to alleviate this problem, by introducing a temporary tariff cap. The Domestic Gas and Electricity (Tariff Cap) Bill (the Bill), which will implement the cap, is currently passing through Parliament. Pursuant to this new legislation, Ofgem will be responsible for designing and implementing the cap.

Ofgem's policy consultation outlines its proposals for the design and implementation of the temporary cap, including potential exemptions and the circumstances in which the cap may be lifted. The headlines are summarised below:

- The consultation describes how Ofgem could set the initial level of the cap and calls for input on the proposed methodology.
- The level of the cap is planned to be reviewed and updated every six months (if necessary), by reference to objective measures such as price indices and industry data.
- No SVTs are proposed to be exempted from the cap, but there may be derogations for tariffs supporting renewable energy (as these incur materially higher costs than standard forms of energy production).
- The Bill provides that the cap may end in 2020, but can be extended annually for up to three years. Extensions are subject to Ofgem finding that the market framework is in place for there to be effective competition for disengaged customers after the price cap is removed. In forming its view, Ofgem will monitor technological changes and other initiatives which might facilitate increased customer engagement and/or market innovation.

The deadline for responding to the consultation is 12:30pm on Monday 25 June 2018. Subject to its review of the responses to the policy consultation and the Bill's passage through Parliament, Ofgem plans to publish a final statutory consultation in August 2018.

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