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#### **OPINION OF THE LEGAL SERVICE<sup>1</sup>**

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From: Legal Service

To: Energy Working Party

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Subject: **Proposal for a Directive of the European Parliament and of the Council amending Directive 2009/73/EC concerning common rules for the internal market in natural gas**

- Legal basis, allocation of competences, derogations

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#### **I. INTRODUCTION**

On 13 November 2017, the Commission presented a proposal for a Directive of the European Parliament and of the Council amending Directive 2009/73/EC concerning common rules for the internal market in natural gas.<sup>2</sup>

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<sup>1</sup> This document contains legal advice protected under Article 4(2) of Regulation (EC) No 1049/2001 of the European Parliament and of the Council of 30 May 2001 regarding public access to European Parliament, Council and Commission documents, and not released by the Council of the European Union to the public. The Council reserves all its rights in law as regards any unauthorised publication.

<sup>2</sup> COM(2017) 660 final, doc.14204/17.

At the meeting of the Working Party on Energy on 11 January 2018, the Presidency asked the Council Legal Service to put in writing its opinion on whether the application of the proposal to the exclusive economic zone of the Member States is compatible with the UN Convention on the Law of the Sea<sup>3</sup> and on the impact of its adoption on the allocation of competences between the Union and its Member States. This opinion answers the second question of that request. This assessment will also include an examination of the proposal, of the legal basis and of the derogations, which was requested by a number of delegations.

## **II. EXAMINATION OF THE PROPOSAL**

1. Pursuant to recitals 1 and 3, the aim of the proposal is to address the remaining obstacles to the completion of the internal market in natural gas resulting from the non-application of Union market rules to gas pipelines to and from third countries and to contribute to security of supply and sustainability.
2. In terms of content, the proposal extends the application of internal market rules on gas to pipelines to and from third countries, and provides for derogations for existing pipelines and exemptions for future pipelines.
3. According to the Explanatory Memorandum accompanying the proposal, “*the Gas Directive in its entirety (as well as the related legal acts like the Gas Regulation, network codes and guidelines, unless otherwise provided in those acts) will become applicable to pipelines to and from third countries, including existing and future pipelines.*”<sup>4</sup>

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<sup>3</sup> That opinion is in doc. 6738/18.

<sup>4</sup> Explanatory memorandum, COM(2017) 660 final, doc.14204/17, page 2, third paragraph.

4. To this end, the proposal alters the definition of "interconnector" in Article 2(17) of Directive 2009/73/EC<sup>5</sup> ("Gas Directive") to mean "*a transmission line which crosses or spans a border between Member States or between Member States and third countries up to the border of Union jurisdiction.*" This has the consequence that the rules of the Gas Directive on unbundling, transparency, third party access and regulated tariffs, currently applicable within the internal market, will be applicable to pipelines to and from third countries, up to the border of Union jurisdiction. In particular:
- a. the transmission system operator of the pipeline has to undergo ownership unbundling pursuant Article 9, which requires that a network ownership be separated from production and transport of gas, and be certified by the national energy regulator of the Member State(s) where it is active;
  - b. the pipeline has to offer non-discriminatory third party access to all interested parties (Article 32);
  - c. network tariffs for having access to a pipeline to and from third countries have to be set in a non-discriminatory, transparent and cost-reflective way<sup>6</sup> and approved by the competent national regulatory authority or authorities of the relevant Member States in cooperation with the relevant authorities of third countries (Article 41(1) and (6));
  - d. transparency requirements on the availability of network capacities, actual use and outages become applicable (Article 16(3)).

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<sup>5</sup> Directive 2009/73/EC of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC, OJ L 211, 14.8.2009, p. 94.

<sup>6</sup> Article 13 of Regulation (EC) No 715/2009 of 13 July 2009 on conditions for access to the natural gas transmission networks and repealing Regulation (EC) No 1775/2005, OJ L 211, 14.8.2009, p. 36.

5. The Gas Directive can only apply to the part of a pipeline that lies within the territory of the Member States and not to the part of the pipeline under the jurisdiction of a third country. Beyond the limits of the Union jurisdiction, as referred to in the proposed new Article 2(17), the rules on energy which are set out in Union law will be applicable only if the third countries are willing to adopt those Union rules, unilaterally or by agreement, such as in the case of the Energy Community Treaty<sup>7</sup> or the EEA Agreement.<sup>8</sup> The result is that the legislation of two or more jurisdictions may potentially be applicable to the same pipeline. To address this issue, the proposal envisages the possibility for Member States to derogate from the rules of the Gas Directive in respect of existing pipelines, as well as the possibility for exemptions for new pipelines.<sup>9</sup> The proposal does not expressly deal with cases where it could be necessary to determine a mutually agreed legal framework with third countries, but the Commission Staff Working Document indicates that "*[r]esolving contradicting requirements and ensuring legal certainty could be achieved by concluding an intergovernmental agreement establishing a specific regulatory framework for the operation of such pipeline.*"<sup>10</sup>

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<sup>7</sup> See the Decision of the Ministerial Council of the Energy Community D/2011/02/MC-EnC: Decision on the implementation of Directive 2009/72/EC, Directive 2009/73/EC, Regulation (EC) No 714/2009 and Regulation (EC) No 715/2009 and amending Articles 11 and 59 of the Energy Community Treaty (9th MC/06/10/2011-Annex 11/05.10.2011).

<sup>8</sup> See Decision of the EEA Joint Committee No 93/2017 of 5 May 2017 amending Annex IV (Energy) to the EEA Agreement.

<sup>9</sup> Accordingly, the Explanatory memorandum indicates that "*Pipelines to and from third countries would thus be subject to at least two different regulatory frameworks. Where this results in legally complex situations, the appropriate instrument for ensuring a coherent regulatory framework for the entire pipeline will often be an international agreement with the third country or third countries concerned. In the absence of such an agreement, an exemption for new infrastructure or derogation for infrastructure already in operation, the pipeline may only be operated in line with the requirements of Directive 2009/73/EC within the borders of EU jurisdiction.*" COM(2017) 660 final, doc.14204/17, page 2, last paragraph.

<sup>10</sup> SWD(2017) 368 final, doc. 14204/17 ADD1, p. 6, fourth paragraph, second sentence.

### III. LEGAL ANALYSIS

#### Legal basis

6. According to the settled case-law of the ECJ, the choice of legal basis for a Union act must rest on objective criteria which are amenable to judicial review, including in particular the aim and content of the measure.<sup>11</sup>
7. From the examination of its aim and content, it appears that the proposal is designed to establish a legal framework for the operation of pipelines to and from third countries within the Union jurisdiction, by rendering applicable to them the rules on unbundling, third party access, regulated tariffs and transparency with the objective of contributing to the security of supply of the Union. When part of a pipeline is not within the Union jurisdiction and conflicting legislation of two or more jurisdictions applies to the same pipeline, the conclusion of an intergovernmental agreement for the operation of a pipeline becomes necessary to resolve contradicting requirements and ensure legal certainty.
8. The proposed legal basis is Article 194(2) TFEU. Article 194(2) states that "*[i]n the context of the establishment and functioning of the internal market [...], Union policy on energy shall aim, in the spirit of solidarity between Member States, to:*
  - a) *ensure the functioning of the energy market;*
  - b) *ensure security of energy supply in the Union;*"

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<sup>11</sup> See, inter alia, Judgment of 11 June 1991, *Commission v Council (Titanium dioxide)*, Case C-300/89, EU:C:1991:244, paragraph 10; Judgment of 12 November 1996, *United Kingdom v Council*, Case C-84/94, EU:C:1996:431, paragraph 25; Judgment of 25 February 1999, *Parliament v Council*, Joined Cases C-164/97 and C-165/97, EU:C:1999:99, paragraph 12; Judgment of 4 April 2000, *Commission v Council*, Case C-269/97, EU:C:2000:183, paragraph 43; Judgment of 19 September 2002, *Huber*, Case C-336/00, EU:C:2002:509, paragraph 30; Judgment of 29 April 2004, *Commission v Council*, Case C-338/01, EU:C:2004:253, paragraph 54; Judgment of 14 April 2005, *Belgium v Commission*, Case C-110/03, EU:C:2005:223, paragraph 78; and Judgment of 12 May 2005, *Regione autonoma Friuli-Venezia Giulia*, Case C-347/03, EU:C:2005:285, paragraph 72.

9. Under the second subparagraph of Article 194(2), "*measures shall not affect a Member State's right to determine [...] its choice between different energy sources and the general structure of its energy supply*". From the examination of its aim and content, it does not appear that the proposal, directly or indirectly, prohibits or has the effect of excluding the construction or the operation of a pipeline with one or more third countries. For existing pipelines, the proposal offers Member States a great degree of flexibility by allowing them to maintain the existing arrangements. For future pipelines, their operation may be subject to internationally agreed rules. Such future agreements, which would become an integral part of the Union legal order, if concluded by the Union <sup>12</sup>, would be subject to the principle of conferral enshrined in Article 5(2) TEU and would have to respect the limitations on Union competence in energy contained in the second subparagraph of Article 194(2) TFEU.
10. By creating a legal framework for the operation of third country interconnectors that deliver gas to the internal market, the proposal falls within the scope of the establishment and functioning of the internal market in gas. As to whether it contributes to the security of supply in the Union, as indicated in the first recital of the proposal, the concept of security of supply involves an element of discretion in the definition of the policies through which such security is ensured. The Council Legal Service therefore considers that the proposal can be adopted on the basis of Article 194(2) TFEU, if in the assessment of the legislator the security of supply of the Union is enhanced by a regulated framework for third country interconnectors.
11. Should the legislator be satisfied that the proposal contributes to the objectives of its legal basis, then, in addition, the principle of proportionality requires that the Directive should not exceed what is appropriate and necessary to achieve the intended purpose and that the disadvantages should not be disproportionate to the aim pursued.<sup>13</sup>

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<sup>12</sup> Article 216(2) TFEU.

<sup>13</sup> Article 5(4) TEU provides that "*Under the principle of proportionality, the content and form of Union action shall not exceed what is necessary to achieve the objectives of the Treaties.*"

12. According to the settled case-law of the Court of Justice, the principle of proportionality, which is a general principle of Union law, requires that "*acts of the EU institutions be appropriate for attaining the legitimate objectives pursued by the legislation at issue and do not exceed the limits of what is necessary in order to achieve those objectives; when there is a choice between several appropriate measures, recourse must be had to the least onerous, and the disadvantages caused must not be disproportionate to the aims pursued.*"<sup>14</sup>
13. In this respect, faced with a choice between several appropriate alternative measures, the legislator must be able to assess all the relevant factors and circumstances. This is an exercise to be carried out on the basis of the information provided by the Commission in the explanatory memorandum, impact assessment and the report on the stakeholder consultation, as well as on the basis of information in the possession of delegations regarding the impact of the proposal in their national systems.
14. An impact assessment has not been presented and therefore alternative measures have not been examined.
15. The Commission argued that "*[t]he present initiative does not require a detailed impact assessment. First and foremost, it aims at achieving a legal situation which reflects the common practice of applying core principles of the regulatory framework set out in the Gas Directive in relation to third countries, notably via intergovernmental agreements.*"<sup>15</sup>
16. In the light of this, it is for the Council as co-legislator to weigh up the different policy options available to it, and to determine whether the proposal, which adopts the current Member State practice of concluding intergovernmental agreements with third countries to establish the regulatory framework applicable to pipelines, is appropriate and does not go beyond what is necessary to achieve the objectives pursued.

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<sup>14</sup> See, for example, Case C-547/14, *Philip Morris*, EU:C:2016:325, paragraph 165.

<sup>15</sup> Commission Staff Working Document, SWD(2017) 368 final, doc. 14204/17 ADD1, p.5, second paragraph.

## Allocation of competences between Member States and the Union following the adoption of the proposal

17. Union competence in the area of energy is described in Article 4(2)(i) TFEU as an area of shared competence between the Union and the Member States.
18. Currently, Directive 2009/73/EC only covers transmission lines which cross or span "*a border between Member States for the sole purpose of connecting the national transmission systems of those Member States*". Therefore, Member States have jurisdiction to regulate the operation of third country interconnectors to which Directive 2009/73/EC is currently not applicable and retain the competence to conclude international agreements to regulate the operation of such pipelines following Article 2(2) TFEU.<sup>16</sup>
19. The application of the common requirements of Directive 2009/73/EC to interconnectors with third countries has consequences for the allocation of competences between the Union and its Member States in the area covered by Union internal rules. In fact, as regards the Union's external competence in the area of energy, Article 3(2) TFEU states that "*[t]he Union shall also have exclusive competence for the conclusion of an international agreement [...] in so far as its conclusion may affect common rules or alter their scope.*"

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<sup>16</sup> Article 2(2) TFEU states that "*When the Treaties confer on the Union a competence shared with the Member States in a specific area, the Union and the Member States may legislate and adopt legally binding acts in that area. The Member States shall exercise their competence to the extent that the Union has not exercised its competence. The Member States shall exercise their competence again to the extent that the Union has decided to cease exercising its competence.*" (emphasis added).



20. As the Union is vested only with conferred powers, the Court's case law requires that any competence, especially where it is exclusive, must have its basis in conclusions drawn from a comprehensive and detailed analysis of the relationship between the international agreement envisaged and the Union law in force.<sup>17</sup> That analysis must take into account the areas covered, respectively, by the rules of Union law and by the provisions of the agreement envisaged, their foreseeable future development and the nature and content of those rules and those provisions.<sup>18</sup>
21. As the Court of Justice has stated, there is a risk that common Union rules may be affected, or that the scope of those rules may be altered, such as to justify an exclusive competence of the Union, where international commitments fall within the scope of the common Union rules. This may be the case where the areas covered by international commitments and those covered by Union rules coincide fully, or where international commitments are concerned with an area which is already covered to a large extent by such rules.<sup>19</sup>
22. Since the proposal can only apply to the part of a pipeline that lies within the Union jurisdiction and not to the part of the pipeline under the jurisdiction of a third country, an international agreement would become necessary to determine the legal framework for the operation of such a pipeline whenever the third country legislation differs from Union energy law on unbundling, third party access, regulated network tariffs and transparency requirements. After the adoption of the proposal, such an agreement would fall within an area that is largely covered by Union common rules and would be liable to affect those common rules or alter their scope within the meaning of Article 3(2) TFEU.

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<sup>17</sup> Judgment of 4 September 2014, *Commission vs Council [CoE Convention on the protection of the rights of broadcasting organisations]*, C-114/12, EU:C:2014:2151, paragraph 74; to this effect also opinion 1/03 of the Court of 7 February 2006 [*New Lugano Convention*], EU:C:2006:81, paragraph 124.

<sup>18</sup> Opinion 1/13 of the Court of 14 October 2014 [*Convention on the civil aspects of international child abduction*], EU:C:2014:2303, paragraph 74; Judgment of the Court of 26 November 2014, *Green Network*, C-66/13, EU:C:2014:2399, paragraph 33.

<sup>19</sup> Opinion 1/13 of the Court of 14 October 2014 [*Convention on the civil aspects of international child abduction*], EU:C:2014:2303, paragraph 71-73.

23. It follows that the conclusion of such an agreement would fall under the exclusive external competence of the Union insofar as it is liable to affect the common rules of the Gas Directive or alter their scope within the meaning of Article 3(2) TFEU. Pursuant to Article 3(2), third limb, TFEU, only the Union would be able to conclude international agreements in the area covered by Directive 2009/73/EC, and Member States would no longer have the right to undertake obligations with third countries which affect these common rules even when there is no possible contradiction between those commitments and the Union common rules.<sup>20</sup>
24. This reasoning would certainly apply to future third country interconnectors and already existing third country interconnectors which are not covered by a derogation. The situation would be the same where an existing third country interconnector is covered by a derogation as provided for in the new draft Article 49(9). The Court of Justice has confirmed the existence of exclusive external Union competence also in cases where an international agreement concerns an area which is internally covered by a Directive which allows Member States to derogate from common requirements.<sup>21</sup> The risk that common Union rules may be adversely affected or altered in scope cannot in fact be excluded on the ground that Member States have some discretion as to whether or not to provide for exceptions or derogations to certain rules within the harmonised legal framework.

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<sup>20</sup> Opinion 3/15 of the Court of 14 February 2017, 2014 [*Marrakesh Treaty*], EU:C:2017:114, paragraph 108 and case law cited there.

<sup>21</sup> See Judgment of 26 November 2014, *Green Network SpA v Autorità per l'energia elettrica e il gas*, case C-66/13, EU:C:2014:2399, paragraph 54, where the Court ruled that exclusive external Union competence is not prevented by the fact that internally a Directive "*allows Member States considerable latitude*" to adopt measures. In its Opinion 3/15, *Marrakesh Treaty*, the Court specified this case-law for the case where an international agreement concerned an area which was internally covered by a Directive which allowed Member States to derogate from common requirements. It nevertheless confirmed exclusive external Union competence based on a number of arguments set out in paragraphs 118 to 129 of the opinion.

25. It follows that, after the adoption of the proposed Directive, Member States would be under the obligation to take all appropriate steps to eliminate the incompatibilities of the existing intergovernmental agreements with the Gas Directive in accordance with Articles 4(3) second subparagraph TEU<sup>22</sup> and 351(2) TFEU.<sup>23</sup> In so far as such intergovernmental agreements regulate areas covered to a large extent by the Gas Directive and are liable to alter its scope, they would fall within the sphere of Union exclusive competence. Member States would be under the obligation to terminate them whenever possible, and the competence to renegotiate them would lie with the Union pursuant to Article 3(2) TFEU.

### **Derogations**

26. The new Article 49(9) envisages that the Member State where the first interconnection point of a pipeline with the Union network is located may grant a derogation from the rules on unbundling, designation and certification of transmission system operators, regulated tariffs and third party access for pipelines to and from third countries completed before the entry into force of the proposed amendments to the Gas Directive.
27. The principles of uniform application of Union law and of equality of treatment require that derogations from common requirements be objectively justified and limited in time.<sup>24</sup> The derogation regime envisaged in the proposal does not meet those requirements. In fact:

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<sup>22</sup> The second subparagraph of Article 4(3) TEU provides that "*The Member States shall take any appropriate measure, general or particular, to ensure fulfilment of the obligations arising out of the Treaties or resulting from the acts of the institutions of the Union*".

<sup>23</sup> The second paragraph of Article 351 TFEU provides that "*to the extent that such agreements are not compatible with the Treaties, the Member State or States concerned shall take all appropriate steps to eliminate the incompatibilities established.*" See also Judgment of 5 November 2002, *Commission v Kingdom of Sweden*, Case C-468/98, EU:C:2002:626, paragraph 37, Judgment of 15 September 2011, *European Commission v Slovak Republic*, C-264/09, EU:C:2011:580, paragraph 44 and Judgment of 4 July 2000, *Commission v Portugal*, Case C-62/98, EU:C:2000:358, paragraphs 34 and 49.

<sup>24</sup> Judgment of 21 September 1983, *Deutsche Milchkontor GmbH and Others v Federal Republic of Germany*, Joined Cases 205 to 215/82, EU:C:1983:233, paragraph 17; Judgment of 12 May 2011, Case C-176/09, *Grand Duchy of Luxembourg v. European Parliament and European Commission*, EU:C:2011:290, paragraph 31. These principles have been inscribed in Article 27 TFEU to guide the Union action in the internal market.

- a) It allows derogation from the core rules of the Gas Directive on unbundling, network tariffs and third party access;
- b) It does not provide any objective criteria for the granting of a derogation.  
Derogations are left to the discretion of Member States on the sole condition that they are not "*detrimental to competition on or the effective functioning of the internal market in natural gas in the Union, or the security of supply in the Union*";
- c) It indicates that the derogation must be limited in time, but no timeframe is included;
- d) The preamble does not provide a justification for such a regime besides the need "*[t]o take account of the previous lack of specific Union rules applicable to gas pipelines to and from third countries*", which is the sort of reasoning that usually justifies transitional measures but not a permanent opt-out;
- e) There is no mechanism of monitoring of the derogations granted.

28. While the existence of intergovernmental agreements may offer an objective justification under certain circumstances,<sup>25</sup> such as the absence of a clause of denunciation or the respect of investment protection agreements, those grounds are not mentioned in the proposal. It follows that the proposal leaves it to the discretion of Member States whether and for how long to exempt all existing pipelines to and from third countries from the common requirements of the Gas Directive.<sup>26</sup> In other words, it allows Member States to maintain the legal regime in place for existing pipelines to and from third countries for an unspecified limited time.

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<sup>25</sup> According to the Report from the Commission on the Application of Decision 994/2012/EU establishing an information exchange mechanism on intergovernmental agreements between Member States and third countries in the field of energy (COM(2016) 54 final), doc.6227/16, it is difficult for Member State to renegotiate intergovernmental agreements for which the consent of the third country is required.

<sup>26</sup> In its slide presentation to the Working Party on Energy of 20 February 2018, the Commission indicated that "*Derogation is unilateral choice of Member States - does not require an agreement with third country or Commission involvement*".

#### **IV. CONCLUSIONS**

29. The proposal is designed to establish a legal framework for the operation of pipelines to and from third countries within the Union jurisdiction, by rendering applicable to them the rules on unbundling, third party access, regulated tariffs and transparency with the objective of contributing to the security of supply of the Union. When part of a pipeline is not within the Union jurisdiction and conflicting legislation of two or more jurisdictions applies to the same pipeline, the conclusion of an intergovernmental agreement for the operation of a pipeline becomes necessary to resolve contradicting requirements.
30. Article 194 TFEU is the appropriate legal basis if the legislator is satisfied that the proposed Directive contributes to the security of supply of the Union and considers that the means employed do not exceed what it is necessary to attain that objective.
31. With the adoption of the proposed Directive, the Union would acquire exclusive external competence to conclude agreements with third countries on the operation of pipelines insofar as they are liable to affect common rules or alter their scope within the meaning of Article 3(2) TFEU.
32. Member States would be prevented from entering international commitments liable to affect Union common rules on unbundling, third party access, regulated tariffs and transparency. They would be under the obligation to take all the appropriate steps to terminate such existing agreements on the operation of pipelines with third countries once derogations expire.
33. The principles of uniform application of Union law and of equality of treatment require derogations to be objectively justified and limited in time. The derogation regime envisaged in the proposal does not meet those requirements.