

The New Approach of the European Commission to Competition Cases in the Energy Sectors *Case COMP/39.402 – RWE Gas Foreclosure*

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I. Introduction

The new competition regime came into force with the modernisation of European competition law in May 2004. Regulation 1/2003¹ replaced Regulation 17/62² and fundamentally changed the enforcement system of EU competition law by extending the powers of the European Commission (hereinafter the Commission).³ The introduction of the new way of resolving cases, namely commitment decisions⁴ and the imposition of new and improved remedies through Articles 7 and 9, are two examples of the most important changes. Article 9 of Regulation 1/2003, for the first time, entails a public settlement procedure where the Commission instead of issuing a prohibition decision can conclude its investigations by rendering commitments binding upon undertakings who suggest them when such commitments address the Commission's concerns over competition.⁵

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¹ Council Regulation (EC) No 1/2003 of 6 December 2002 on the implementation of the rules on competition laid down in [Article 101 and 102 TFEU] (Regulation 1/2003).

² Regulation No 17 First Regulation implementing Article 85 and 86 of the Treaty OJ L 204/62.

³ Elena Wind, 'Remedies and Sanctions in Article 82 of the EC Treaty' (2005) 26(12) European Competition Law Review 659.

⁴ Before modernisation, the Commission had been using behavioural remedies offered as commitments by undertakings concerned to settle competition proceedings on an informal basis. A number of cases were resolved through informal commitments considered by the Commission as acceptable and only after the Regulation 1/2003 this practice was given an express legal basis. See further L.O. Blanco, *EC Competition Procedure* (Oxford University Press 2nd edition 2006).

⁵ Article 9 of Regulation 1/2003 (n1).

Another power given for the first time to the Commission by Regulation 1/2003 is to impose structural remedies on undertakings concerned under Articles 7 and 9 of the Regulation, when they are capable to effectively bring an infringement to an end, and proportionate to the violation committed.⁶

In this respect, this case comment will analyse one of the most significant examples of the commitment decisions⁷ given under Article 9 of Regulation 1/2003, i.e. the *RWE* decision of the Commission.⁸ One may infer from the *RWE* decision and other decisions alike that the Commission might tend to conclude investigations through commitment decisions, *first*, because of the administrative efficiencies such as cost and time reduction, as well as because they are less likely to be challenged through appeal mechanisms as commitments are offered by the parties subject to the investigations.⁹

1. Where the Commission intends to adopt a decision requiring that an infringement be brought to an end and the undertakings concerned offer commitments to meet the concerns expressed to them by the Commission in its preliminary assessment, the Commission may by decision make those commitments binding on the undertakings. Such a decision may be adopted for a specified period and shall conclude that there are no longer grounds for action by the Commission.

2. The Commission may, upon request or on its own initiative, reopen the proceedings:

where there has been a material change in any of the facts on which the decision was based;

where the undertakings concerned act contrary to their commitments; or

where the decision was based on incomplete, incorrect or misleading information provided by the parties.

⁶ Article 7(1) of Regulation 1/2003 (n1):

Where the Commission, acting on a complaint or on its own initiative, finds that there is an infringement of Article 81 or of Article 82 of the Treaty, it may by decision require the undertakings and associations of undertakings concerned to bring such infringement to an end. For this purpose, it may impose on them any behavioural or structural remedies which are proportionate to the infringement committed and necessary to bring the infringement effectively to an end. Structural remedies can only be imposed either where there is no equally effective behavioural remedy or where any equally effective behavioural remedy would be more burdensome for the undertaking concerned than the structural remedy. If the Commission has a legitimate interest in doing so, it may also find that an infringement has been committed in the past.

⁷ See other Commission decisions, Case COMP/39.388 and Case COMP/39.389 *E.ON* [2008], Case Comp/39.316 *GDF* [2009]; Case COMP/39.317 *E.ON Gas* [2010]; Case COMP/39.315 *ENI* [2010].

⁸ Commission Decision, Case Comp/39.402 *RWE Gas Foreclosure* [2009] 1885.

⁹ Temple J. Lang, ‘Commitment Decisions and Settlements with Antitrust Authorities and Private Parties under European Antitrust Law’ (Fordham Antitrust Conference, Brussels, September 2005).

Second, in comparison with infringement procedures, commitment procedures are less burdensome for the Commission as the infringement of competition law does not need to be proved. Preliminary assessment indicating possibility of the existence of these infringements would be enough to conclude investigations through public settlements.¹⁰ *Third*, the parties concerned may suggest more extensive commitments than those would be imposed by the Commission under Article 7 in order to cease investigations without any established infringement decision.¹¹ The Commission therefore could prefer to follow commitment procedure, in particular, where relevant markets under investigations are currently being liberalised and the commitments offered are sufficient to further such a liberalisation, on the one hand and are capable to eliminate the deficiencies of sector-specific regulations on the other.

II. Summary of the Decision

To facilitate the understanding of the analysis of the decision, it is useful to understand some basic concepts and mechanisms pertaining to energy sectors. The gas sector, as well as electricity sector, consists of four vertically integrated segments which are production/importation, transmission, distribution and supply. Transmission and distribution segments, i.e. the infrastructures for energy transmission¹² and distribution,¹³ are defined as natural monopolies given economic and technical difficulties to construct new ones as alternatives to the existing ones. Thus, market operators who do not own transmission and/or distribution networks have to use these existing ones in order to be able to participate in commercial activities in the energy markets. Transmission and distribution markets are regulated markets whereas production/importation and supply markets are open to competition.

¹⁰ *ibid.*

¹¹ Richard Whish and David Bailey, *Competition Law* (Oxford University Press 7th edition 2012).

¹² Gas transmission refers to transportation of natural gas through the network, which mainly contains high-pressure pipelines, and its delivery to customers. This does not include supply. Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC OJ L 211/94, art 2.

¹³ Gas distribution means transportation of natural gas through local or regional pipeline networks and its delivery to customers. This does not include supply. *ibid.*

In *RWE* decision, the Commission came to the conclusion that the problem mainly derived from the vertically bundled ownership of RWE AG (hereinafter RWE) including import, supply and network facilities such as transmission grid. The preliminary assessment of the Commission maintained that RWE may have excluded its potential competitors from the market by creating artificial obstacles to access its gas transport network, i.e. the so-called ‘third party access’, through the refusal to supply and margin squeeze.

1. Parties to the Investigation

The Commission’s investigation concerned RWE and its direct and indirect subsidiaries, in particular RWE Energy AG, RWE Westfalen Weser Ems AG, RWE Rhein Ruhr AG and RWE Transportnetz Gas GmbH.¹⁴ RWE is a fully integrated German-based energy and utility company, mainly active in production and supply of electricity and gas. With regard to the gas sector, the company is active in production, import, transmission and storage of gas as well as in the downstream gas distribution business.

2. Definition of Relevant Markets and Assessment of Dominant Position of RWE

2.1. Relevant Product and Geographic Market Definitions

When assessing the relevant product market, the Commission distinguished between the markets for *the supply (sale) of gas* and *the markets relating to gas infrastructure*, such as gas transport services. In the gas supply markets, the preliminary assessment divided markets into two groups: *wholesalers* and *end customers*. Within these groups, the Commission defined two different markets for *wholesales*: (i) ‘Regionalferngasgesellschaften’ (regional distributors) and (ii) ‘Stadtwerke’ (smaller distributors), and, two different markets for *the supply of gas to end customers*: (i) large industrial customers, and (ii) smaller customers such as household and small commercial customers.

¹⁴ Commission, ‘Antitrust: Commission initiates proceedings against RWE Group concerning suspected foreclosure of German gas supply markets’ MEMO/07/186.

Within the gas transport market, the preliminary assessment defined gas transmission market for services offered by transmission system operators¹⁵ (hereinafter TSO), on the one hand, and gas distribution¹⁶ market for services offered by distribution system operators¹⁷ (hereinafter DSO), on the other.

As to the relevant geographic market, the Commission found that gas transmission and distribution markets cannot be defined larger than grid-wide as in most cases the construction of competing parallel gas networks is not economically viable, therefore competitive constraints from TSOs outside RWE's network remain negligible. Moreover, given missing competitive constraints from suppliers outside RWE's gas network, the downstream gas supply markets were also defined as grid-wide.¹⁸

2.2. Assessment of Dominant Position of RWE

In the preliminary assessment, the Commission concluded that RWE may have had a dominant position both in the gas transmission market and in the downstream supply markets within its grid area. As regards gas transmission, it was found that no customers connected to RWE's grid had other possibility for their gas transmission needs other than the transmission infrastructure of RWE. High entry barriers for potentially competing TSOs such as the high construction costs and the high barriers to supply via other market areas guarantee that RWE TSO's position in the transmission business within its network area will not be challenged within the foreseeable future.

As regards the downstream supply markets, the preliminary assessment showed that the chances for third party suppliers to compete with RWE in the supply markets within RWE's grid were limited by the small volumes of

¹⁵ Transmission system operator refers to a natural or legal person who carries out the function of transmission and is responsible for operating, and ensuring the long-term ability of the system to meet reasonable demands for gas transport. Directive 2009/73/EC (n 9) art 2.

¹⁶ Gas distribution means transportation of natural gas through local or regional pipeline networks and its delivery to customers. This does not include supply. Directive 2009/73/EC (n 9) art 2.

¹⁷ Distribution system operator means a natural or legal person who carries out the function of distribution and is responsible for operating, and ensuring the long-term ability of the system to meet reasonable demands for the distribution of gas. Directive 2009/73/EC (n 9) art 2.

¹⁸ Commission Decisions, Case COMP/M.1383 *Exxon/Mobil* [1999]; Case COMP/M.3052 *ENI/Fortum Gas* [2003]; Case COMP/M.4180 *GDF/Suez GDF/Suez* [2006] 5419.

transport capacities available to them. The low share of gas transported for third suppliers on RWE's TSO pipelines translated into equally low market shares on supply markets served by these pipelines. Absence of a functional third party access system and the fact that almost the entire available capacity was booked on a long term basis for RWE, made the risk for RWE to lose customers in case of a price increase quite negligible.¹⁹

3. Practices that Raised Competition Concerns

The Commission suspected that RWE might have abused its dominant position in the gas transmission markets and in the downstream supply markets within its grid area through the refusal to supply and the behaviour aiming at decreasing the margin of its downstream competitors.

3.1. Refusal to Supply

According to the preliminary assessment, the first possible unilateral anticompetitive conduct of RWE was the refusal to supply. The gas transmission network was considered as an essential facility, since access to it was objectively necessary to carry out business in the gas supply markets within RWE's grid area.²⁰ RWE may have pursued a systematic approach according to which it tried to keep the transport capacities in favour of its own affiliate for a long period of time by understating the capacity that was technically available to third parties. In fact, it was observed by the Commission that more capacity was used by RWE than indicated as maximum technical capacity. The chances of competitors to get sufficient capacity from RWE's transmission networks were thus reduced. Furthermore, the Commission's investigations showed that the transmission requests of the competitors were regularly and systematically rejected, since the demand for the transmission was largely greater than the offered capacities.²¹ These facts could indicate that there was neither a functional third party access system nor an effective congestion management system, which could actually have avoided many of the refused and delayed capacity requests, harming third party transport customers and ultimately consumers. This claim of the Commission is quite significant, because despite the fact that both 'third party access' and 'congestion management'

¹⁹ RWE (n 6) para 19.

²⁰ Case C-7797 *Oscar Bronner* [1998] ECR I-7791.

²¹ RWE (n 6) para 26.

are sector-specific regulatory rules,²² the Commission was nevertheless referencing to these rules revealing their deficiencies.

In its conclusions, the Commission stated that RWE's intention might have been rather to protect itself from new competitors than to attract new transport customers. Third party shippers were, as a result of this intention, only granted a fraction of the transports at the RWE's transmission grid and could not compete in an effective manner in the downstream supply markets.²³

3.2. Margin Squeeze

The second concern of the Commission related to the possible abuse of the RWE's dominant position on the TSO-level by way of a margin squeeze. The preliminary assessment stated that RWE may have intentionally set its transmission tariffs at an artificially high level in order to squeeze its competitors' margins in the downstream gas supply markets.²⁴ According to the Commission, there was evidence that the network tariffs were creating asymmetric cost effects to the detriment of downstream competitors. This was because the detrimental network tariffs were only applied to third party users elevating the costs of tariffs which were already high. Moreover, rebates used by RWE increased the existing cost disadvantages for the competitors in the downstream supply markets, since they were only granted to RWE due to the long-term transmission contracts, although technically available for all market operators.²⁵ The preliminary assessment also raised concerns over balancing system²⁶ which posed an asymmetric negative impact on new entrants through high balancing costs, which was not paid by RWE due to an agreement signed between TSO (which was vertically integrated to RWE) and RWE, and high penalty fees, which prevented competitors from attempts to submit offer to downstream customers.²⁷

4. Commitments Proposed by RWE and Principle of Proportionality

²² Directive 2009/73/EC (n 9).

²³ RWE (n 6) paras 22-25.

²⁴ Oliver Koch and others, 'The RWE Gas Foreclosure Case: Another Energy Network Divestiture to Address Foreclosure Concerns' (2009) 2 Competition Policy Newsletter <http://ec.europa.eu/competition/publications/cpn/cpn_2009_2.html> accessed 07 December 2013.

²⁵ RWE (n 6) para 34.

²⁶ Balancing system is a gas transmission system within which differences between exact and forecasted gas consumption must be balanced. Directive 2009/73/EC (n 9) art 2.

²⁷ RWE (n 6) para 35.

RWE agreed to divest its transmission system business including the entire current German high-pressure gas transmission network with a total length of approximately 4000 km. According to the Commission's decision, the commitments suggested by RWE were not only suitable to remove the Commission's concerns over competition but also complied with the principle of proportionality.²⁸ The disposal of RWE's transmission business would guarantee that the control of RWE over transmission network would be taken as preventing the undertaking from engaging in similar unilateral anticompetitive practices relating to the access to its network in the future. These structural remedies were also necessary, since there was no equally effective behavioural remedy to the divestiture which could be easily monitored and administered without being more burdensome for RWE.²⁹

Furthermore, according to the Commission, in the absence of a structural remedy, the incentives to further engage in such behaviour would not be removed effectively, because anticompetitive unilateral behaviour of RWE, on a lasting and repeating basis, stemmed from the inherent conflict of interest within RWE as a vertically integrated gas company, i.e. from the very structure of the undertaking, which used to control both the transmission and the supply of the gas.³⁰

III. Conclusion

The outcome of the above case makes it clear that the Commission aims to eliminate the shortcomings of regulation in newly liberalised energy markets by accepting structural commitments offered by the parties under investigations. As it is seen from the decision, the structural remedies were used to eliminate weaknesses of the energy regulation as well as to create *ex ante* regulatory effects on the markets. This trend of the competition law application might launch a new form of the Commission's activity, ie the 'regulatory antitrust'.³¹ Regulatory antitrust therefore can be assumed as a

²⁸ According to the principle of proportionality, the measures adopted by the EU institutions must be suitable and not exceed what is appropriate and necessary for attaining the objective pursued. If there is a choice between several appropriate measures, the least onerous one must be imposed. Although the wording of Article 9 of Regulation 1/2003 does not mention the principle the Commission is obliged to comply with it when the decision is given on the basis of Article 9 of the Regulation; Case C-441/07P *European Commission v Alrosa Company Ltd* [2010] ECR II-5949.

²⁹ RWE (n 6) para 50.

³⁰ *ibid.*

³¹ See Giorgio Monti 'Managing the Intersection of Utilities Regulation and EC Competition Law' (2008) 4(2) *Competition Law Review* 123; Javier Tapia and Despoina

methodology to eliminate regulatory failure. It can be clearly seen that with regulatory antitrust the Commission aims at promoting further regulations. However, it should not be forgotten that competition law and sector-specific regulation have different objectives. Even though they can have a complementary relationship they cannot substitute each other. Furthermore, the approach of the Commission should not undermine *ex ante* sector-specific regulation by replacing its duty with regulatory antitrust which would impede legal certainty in the markets.