

**CASE COMMENT: JUDGMENT OF THE COURT  
OF 15.9.2016 PGE GÓRNICtwo I ENERGETYKA  
KONWENCJONALNA SA V PREZES URZĘDU  
REGULACJI ENERGETYKI**

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**Abstract:** The case deals with the problem of the division of powers as well as state aid law in relation to the issue of compensation schemes for the termination of long-term contracts in the electricity sector. Moreover, the case faces the problem of interpretation of the scope of the adjustment of state aid.

Long-term contracts in the electricity sector have been present in many EU member states. Such contracts have enabled energy companies to invest in infrastructure in order to boost the capacity and guaranteed sale of the electricity produced. However, these contracts were against fair competition and as a result the electricity market was closed for other competitors. This explains why the EU introduced rules that introduced competition on the electricity market and gave compensation to companies for the termination of such contracts.

One of the problems in interpretation of state aid rules occurred in a case concerning the Polish electricity market on which such contracts existed before Poland's accession to the EU. The case concerned the leading

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Polish electricity producer PGE *Górnictwo i Energetyka Konwencjonalna S.A.* (PGE) whose business was performed by two bodies *Zespół Elektrowni Dolna Odra S.A.*, and *Elektrownia Bełchatów S.A.* (ELB). These two bodies were separate entities and were not in the same group of entities at the time when the stranded costs proceeding was started. The Polish Supreme Court dealt with the issue of whether the correction of the annual amount of compensation of stranded costs could be made taking into account the financial outcome of the given company and including in such an outcome the financial results of another company which is covered by national legislation on the termination of long-term contracts. ELB was a company that was treated as an entity in which financial results are taken into account when the annual correction was made for the electricity producer belonging to the same group of entities. These companies were listed in the Polish Act on the termination of long-term contracts. If such a correction were made taking into account that ELB was part of a different group of entities PGE would benefit with a higher amount of state aid. However, if such a correction took into account real membership in a group of entities such state aid for PGE should be lower. The Polish Supreme Court had doubts how to interpret the Polish Act on the termination of long-term contracts with EU state aid and asked the CJEU two questions.

The first question asked by the Supreme Court concerned whether EU provisions on state aid – Article 107 TFEU read together with Article 4(3) TEU and Article 4(2) Decision 2009/287 could be interpreted as prohibiting national authorities and national courts to review the state aid scheme which was already assessed by the European Commission in light of the Stranded Costs Methodology and found to be compatible with the internal market before it was implemented.

First of all it could be said that it is astonishing why the Polish Supreme Court asked such a question because there is a great deal of EU case law which describes the role of national bodies and courts and the European Commission in applying state aid. Perhaps it is because most of the cases concerned long-term contracts in western EU countries which are not analogous to their respective electricity markets like Poland. It should be added that Polish lawmakers introduced an act on the rules governing the covering of costs incurred by electricity generators in connection with the early termination of Power Purchase Agreements which dealt with the problem of the termination of long-term contacts. In the system created by the Polish Act, the President of the Energy Regulatory Office (President of URE) was entitled to establish the amount of compensation which was payable in advance for a given year which covered the stranded costs.

Such compensation should not exceed the amount described by the Act. At the end of the adjustment period, the President of URE made the final adjustment. So the question of the Polish Supreme Court was taken in order to confirm if the President of URE has the authority to supervise all state aid schemes concerning the electricity market not only in light of Polish acts but also EU rules of state aid.

It should be added that the question asked by the national court was extremely important for the Polish regulator of the energy sector. If the CJEU would agree that national bodies have the authority to assess whether the scheme which was already approved by the European Commission is in line with EU law, it would enable the supervision of all state aid schemes at the national level at the time when they are implemented.

In trying to answer this issue it has to be determined that long-term purchase contracts were a form of state aid which was given to different electricity companies in order to guarantee the supply of energy. Such contracts were incompatible with EU legislation on state aid and this explains why Decision 2009/287 was issued. This decision enables Polish state to terminate such contracts and give compensation to those companies which exercised contracts by, for example, undertaking investments in electric infrastructure. Such compensation is a form of state aid which is compatible with the internal market when it is in line with the Stranded Costs Methodology. So it can be said that the termination of long-term purchase contracts would in general be extremely unfavorable for those companies because they would make a loss on investments needed to exercise such contracts. In order to stabilize the Polish electricity market the European Commission agreed to conditionally accept state aid given to those companies which signed long-term contracts in order to compensate their losses. Such compensation is granted after the approval of the State aid scheme by the European Commission. It is worth highlighting that such approval is made before the aid scheme is implemented.

It could be argued that such scheme is a framework which has to be implemented by the company which is a beneficiary of state aid. So the company has to prove that its scheme is compatible with the internal market and after commission approval of such state aid can be granted. The Polish Supreme Court stated that such a situation can be insufficient in order to ensure compliance with EU state aid law. It added that it is worth considering whether the national courts or administrative bodies should have the competence to check if the state aid scheme was implemented in accordance with the conditions approved by the European Commission. Such a finding could be justified because it would strengthen the enforcement

of EU state aid law. However, on the other hand it would mean that the European Commission and the national courts or administrative bodies share competences in enforcing state aid law. Such a statement is partly true because as the CJEU stated the European Commission and national authorities play their roles in enforcing state aid law but as the Tribunal stated those roles are complementary and separate from each other<sup>1</sup>. TSEU judgements describe the roles of the national courts and national authorities in such cases.

The CJEU highlighted that the role of the national courts is to safeguard the rights of individuals against those activities of the state that would infringe Article 108(3) TFEU. Thus, the courts are obliged to act in two situations.

The first situation covers cases in which the role of the national courts is to safeguard the rights of individuals until the final decision of the European Commission is made. In this respect the national Courts should react when such rights are abused by state activities that are incompatible with prohibition laid down in Article 108(3) TFEU<sup>2</sup>. Therefore, the national courts should react in order to safeguard individual rights when state aid was not notified to the European Commission and thus Article 107(3) TFEU was infringed. This also means that individuals have to use actions in the national courts in order to obtain protection against unlawful state aid<sup>3</sup>.

The second situation in which the national courts are obliged to act is the matter of the interpretation of Article 107(1) TFEU. This means that the court can interpret, in a given case, if a measure adopted by the state constitutes an advantage that favours undertakings and whether it is selective.<sup>4</sup>

The role of the European Commission is slightly different. First of all the Commission is not obliged to file a decision in which it orders the repayment of state aid because it was not notified in accordance with EU

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<sup>1</sup> PGE Górnictwo i Energetyka Konwencjonalna SA v. Prezes Urzędu Regulacji Energetyki, Case C-574/14, Judgment of the Court of 15.9.2016, ECLI:EU:C:2016:686, para. 30.

<sup>2</sup> Piaggio, Case C-295/97, Judgment of the Court of 17.6.1999, ECLI:EU:C:1999:313, para. 31.

<sup>3</sup> H. C. H. Hofmann, C. Micheau, *State Aid Law of the European Union*, Oxford University Press 2016, p. 451.

<sup>4</sup> Transalpine Ölleitung in Österreich GmbH and Others, Case C-368/04, Judgment of the Court of 5.10.2006, ECLI:EU:C:2006:644, paras 39 and 40.

rules on state aid<sup>5</sup>. This can be made after a member state has then chance to give its opinion about the granted state aid. Therefore, the first step in such a such a case is issuing an interim decision that requires member states to suspend pending state aid. While this is undertaken, the European Commission can request the member state to provide all documentation and data concerning the granted state aid in order to examine if this aid was granted in accordance with EU law<sup>6</sup>.

In the commented case, the European Commission stated that the compensation scheme was state aid according to Article 107(1) TFEU and it approved the fact that this scheme was compatible with the internal market. Such a decision of the European Commission is final in meaning in that no other authority is entitled to approve such a scheme before it is implemented. As the Tribunal stated, if the national court was entitled to do so it would meant that it could replace the Commission decision<sup>7</sup>. Hypothetically, even if such powers were granted to the national courts it would be hard to determine which state aid scheme is in accordance with EU law. It would also mean that the national courts could undermine a European Commission decision that was issued earlier. Moreover, it would even mean there is even a change in relations between the European Commission and the national courts in cases of state aid. The latter institutions would be obliged to check if the Commission decision was in accordance with EU law. Undoubtedly such a finding is unacceptable.

The European Commission is thus the only body that can file a decision in which it approves certain state aid stating that such aid is compatible with the internal market. It is argued that the Commission has wide discretionary powers in exempting aid according to Article 107(3) TFEU<sup>8</sup>. Enabling the national courts to decide whether a given state aid scheme is covered by this exemption would also lead to a different interpretation of law in many member states. This would lead to uncertainty of law because companies could face problems in which a similar state aid scheme was approved in one member state while rejected in another member state. Certainly, as in many other cases, the European Commission

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<sup>5</sup> Belgium v Commission, Case C-142/87, Judgment of the Court of 21.3.1990, ECLI:EU:C:1990:125, paras 15 to 20; FNCE, ECLI:EU:C:1991:440, Case C-354/90, Judgment of the Court of 21.11.1991, para. 13.

<sup>6</sup> France v Commission, Case C-301/87, Judgment of the Court of 14.2.1990, ECLI:EU:C:1990:67, paras 19 and 21.

<sup>7</sup> C-574/14, para. 35.

<sup>8</sup> L. Hancher, T. Ottervanger, P. J. Slot, *EU State Aids*, Sweet & Maxwell, 2012, p. 753

plays a crucial role in safeguarding the unilateral interpretation of law across all member states. If a Commission decision could be changed by the national authorities there would be different competition conditions in every member state.

This explains why the EU legislator created a system in which the competences of different bodies are complementary. The CJEU explained this mentioning that fact that the decision taken by the Commission could change over time but this does not mean that a new decision should be adopted. If such a fact changes, the national authorities should inform the European Commission of it and wait for its decision. Such a division of roles is also an expression of the rule of loyal cooperation between the European Commission, the national courts and national authorities. According to this rule, the above mentioned bodies have their roles assigned by the TFEU. Moreover the CJEU explains that the national courts are obliged to take all necessary measures in order to fulfill all obligations resulting from EU law. This means that the national courts cannot take any decision that would be in conflict with a European Commission decision<sup>9</sup>. The author feels it necessary to highlight the fact that this finding of the courts was correct and is extremely important not only for cases concerning competition law but for all cases in which there is any doubt related to the supremacy of EU law.

In the light of the above mentioned issues it can be argued that the Polish Supreme Court had justified doubts about the interpretation of EU law. The procedure of granting state aid as a compensation of stranded costs seems to be extremely unrealistic. It is worth highlighting the fact that EU law assumes that such a state aid scheme is verified only once before its implementation. Of course there is a legal mechanism for stating that EU rules were abused but these rules cover situations when the benefits resulting from state aid were already transferred to the company. Therefore, it can be said that there should be three phases in which state aid is verified. The first should cover the proposal of the state aid scheme, the second phase is its implementation and the third when the benefits are transferred to the company. It is clear that there are no legal instruments to deal with the phase when the state aid scheme is implemented. On the one hand, the European Commission has no resources to monitor such a phase; however, on the other hand, abuses of EU law and other errors could

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<sup>9</sup> Deutsche Lufthansa, Case C-284/12, Judgment of the Court of 21.11.2013, EU:C:2013:755, para. 41.

be eliminated at such a phase. It could be argued that even if national authorities have no powers to once again approve a state aid scheme they should be empowered to check if the state aid scheme is implemented in line with EU provisions and rules on state aid. The author could imagine that within such a system if there are serious doubts found by a national authority it should pass them on to the European Commission which would once again check the compatibility of the implementation of the state aid scheme with EU rules.

The second question which was asked by the national court concerned the interpretation of the methodology of stranded costs compensation laid down in Article 4(1) and (2) of Decision 2009/287. The national court asked when membership of a given group of undertakings should be taken into account. The court asked whether it should be taken into account at a time when the European Commission assessed the compatibility of the stranded cost compensation scheme or at a time when the adjustment is made. The court simply recognized those two situations as “static” and “dynamic” interpretation<sup>10</sup>.

Finding the answer to the question whether static or dynamic interpretation should be adopted is not an easy task. Decision 2009/287 does not say anything about this but it should to be highlighted that the general assumption of this decision is the approval of the compensation scheme based on the stranded costs methodology. In order to find the answer to this question the idea of stranded costs has to be recalled. First of all the electricity market regulated by the state, energy prices are set by the regulator in such a way as to reflect the costs of service. This is understood as the regulator setting prices where total revenue equals total costs. So the electricity company will face no losses selling electricity in the process set by the national regulator<sup>11</sup>. But in many cases the supplying of energy required undertaking new investments which were not reflected by the price set by national regulator. The European Commission faced the problem of stranded costs before the liberalization of the electricity market was undertaken. Before liberalization took place member states could compensate stranded costs for so called “non-returned” investment

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<sup>10</sup> Case C-574/14, Judgment of the Court of 15.9.2016, para. 44.

<sup>11</sup> R. A. McNerney, *Changing Structure of the Electric Power Industry: An Update*, DIANE Publishing 1998, p. 77.

costs which resulted from the construction of generating plants<sup>12</sup>. Such costs were connected to long-term investments and by the liberalization of the market and would not be covered.

So the problem of stranded costs was raised when it was no longer possible to pass them onto the consumer. This explains why the European Commission agreed to accept compensation schemes to those companies which faced the problems of stranded costs. Of course such compensation consisted of state aid which had to be approved by the European Commission. So the member did not have the autonomy to grant such compensation even if long-term contracts were made on their initiative or even request. The signing of such contracts was for electricity companies the only solution to deal with the restructuring of the Polish electricity sector in which old technology dominated. In order to run investments in power plants or power lines, Polish companies signed long-term contracts with the state owned power operator. They agreed to build new or upgrade older power plants in order to increase electrical capacity and they were obliged to deliver a specified amount of electricity whose price was based on the rule that the costs were covered by the final user. When Poland joined the EU, such contracts were against EU law and had to be terminated. But such a situation meant that those companies which already made investments in infrastructure would face the problem of stranded costs because they simply lost a long-term client who agreed to pay for the electricity for many years. If EU law would not introduce compensation of stranded costs many Polish power companies would suffer because of the termination of long-term contracts and this would even lead to their bankruptcy. But the EU legislator decided that in such situations the existence of competition is more important and conditionally allowed state aid which covers the losses of such companies.

It should be added that the liberalization of the energy market through EU law was introduced in all member states but the conditions of competition on those markets were very different. An example is Poland where for many years the state was the sole owner of the electricity infrastructure and invested in it for many years. The introduction of a market economy in Poland did not mean that the market was suddenly opened up for competition; the state still had many monopolies and even

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<sup>12</sup> L. Hancher, A. de Houteclocque, M. Sadowska, *Capacity Mechanisms in the EU Energy Market: Law, Policy, and Economics*, Oxford University Press 2015, p. 159.



when privatization was undertaken those state monopolies often changed into private monopolies. The end of monopolies came when Poland joined the EU and was obliged to implement EU rules on competition on electricity markets. This means that there can be slight or even huge differences in market conditions in the electricity sector in different member states. Enabling “dynamic” interpretation of compensation enables us to take into account those conditions which changed after the scheme was approved by the European Commission. It should also be added that such an adjustment of compensation can be both an advantage and disadvantage to companies.

Returning to the question asked by the court, it should be highlighted that allowing for “dynamic” interpretations of annual compensation of stranded costs and its final adjustment is in line with the stranded cost methodology which is the main idea behind Decision 2009/287. So why should the “dynamic” conception be used? It can be justified by changes on the market. It is obvious that competition conditions are not “static”. Market conditions reflect the whole process and costs of companies could change radically. The court stated that the stranded costs methodology is based on the solution that compensation is paid based on future developments of competition, and changes of competition should be reflected in the amount of compensation paid<sup>13</sup>. So acceptance of only one way for calculating compensation could be harmful for companies. It even denies the idea of granting such compensation because it is granted only to those companies which would lose out because of their previous commitments from the state.

What is worth highlighting is the fact that the Advocate General said that in Decision 2009/287 the European Commission states that the annual adjustment of compensation reflected actual market conditions when the compensation was granted. This means that the changes in competition on the electricity market has to be analyzed. Moreover, the composition of the group of companies in a given year can mean that conditions of competition are worse<sup>14</sup>. The Advocate General also stated that a useful hint for finding the answer the question can be found in the idea behind Decision 2009/287. This decision was issued in order to grant compensation over a span of years. It would even be hard to believe that the idea of the European Commission was to stick only to those calculations of compensation made at the time of their approval.

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<sup>13</sup> C-574/14, Judgment of the Court of 15.9.2016, para. 49.

<sup>14</sup> C-574/14, Advocate General Opinion of 14.4.2016, para. 62.

The European Commission itself being an antimonopoly authority is aware of the above-mentioned changes of competition which are often connected with the cycles of the economy. He added that this type of interpretation is in line with the logic of granting state aid where the Commission is responsible for approving it and enables the amount of state aid to be suited to actual market conditions<sup>15</sup>.

The answer to the second question of the national court is crucial for EU state aid law as well as for EU competition law. In the author's opinion the CJEU reflected the main goal of competition law which is to ensure workable competition on the internal market. It doing so it would be hard to stick only to static provisions, which do not take into account market conditions that change over time. So such an interpretation highlights that the European Commission should always react when there is a fear of weakening competition.

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<sup>15</sup> Advocate General Opinion Case C-574/14 PGE, paragraph 74.