Energy regulation

The impact of Brexit on the energy sector will only become clear over time. Now that the UK has left the EU and entered into a transition period until 31 December 2020 (or later, if extended), attention turns to the negotiations on the future UK-EU relationship. Much of the nature and extent of the impact on energy will depend on the model of co-operation adopted as an alternative to EU membership.

Beyond the physical integration of energy markets, Brexit raises significant questions for the UK. How will the UK approach security of gas supply as an EU “third country”? How will the UK’s approach to climate change and international negotiations evolve? And, more specifically, how will the UK price carbon emissions once, as seems likely, it leaves the EU-ETS? While it is yet unclear what the precise form of the future UK-EU cooperation in relation to energy would be, it remains possible that a situation similar to no deal comes into effect, if a new trading relationship is not in place at the end of the transition period. This note will, therefore, examine the immediate impact of no deal on the future relationship in relation to energy post-transition on key areas of the energy sector, as well as look at the implications of the EU’s and UK’s stated negotiating positions to assess the likely shape of the future agreement for the energy sector.

Given the relative depth of EU legislative harmonisation involved in the Internal Energy Market, the greatest risk of discontinuity in a no-deal comes in relation to electricity trading, explored below.

Tariffs and customs procedures

As with other industries that involve the trade in goods, parts of the energy sector could be impacted by tariffs. So, for example, wind and solar projects could be impacted by tariffs of up to 2.7% applicable to wind-powered generator sets and lithium-ion (for use in batteries) imported into the UK from the EU. The impact of new customs formalities at the EU-UK border could also have cost implications for energy projections in relation to both construction and maintenance.

Although much less likely in practice, tariffs could also become relevant to energy trading with certain energy products. While the UK and the EU have both agreed as WTO

The section is part of our Brexit Legal Guide.

Deal/transition period

- Now that it has been approved by the UK and EU Parliaments, the Withdrawal Agreement sets out arrangements for the UK’s withdrawal from the EU with effect from 11 pm on 31 January 2020 – when the UK ceased to be an EU Member State.
- The UK is now in a transition period following its exit from the EU until the end of 2020. UK legislation calls this the “implementation period”.
- During transition, EU law continues to apply in and to the UK and the UK continues to trade with the EU as part of the Single Market.
- The non-binding Political Declaration on the future relationship between the UK and the EU accompanies the Withdrawal Agreement – there will now be an intense period of negotiations to seek to finalise the details of the future relationship.
members that the electricity and oil that they trade must be zero rated, natural gas could be increased to its “bound rate” of 0.7% if the UK or EU chose to (from its currently applicable zero rate).

**Internal Energy Market (“IEM”)**

In February 2020, the EU issued negotiating directives on the future relationship negotiations between the EU and the UK that define the scope and terms of the partnership as envisaged by the EU, which contain provisions for future cooperation in areas including energy.

On 12 March 2020, a first draft of the proposed free trade agreement was also released. The draft text of the “Agreement on the New Partnership between the European Union and the United Kingdom” ("Draft Agreement") is likely subject to change, however, it does convey a reasonably comprehensive sense of the future relationship between the EU and the UK from the EU’s perspective. The Draft Agreement addresses matters relating to energy under provisions set out in Title XIII: Energy and Raw Materials of the Draft Agreement, the scope of which seems to be based on the concepts contained in the current arrangements for the internal market while addressing the fact that the UK is no longer a member of the IEM as we know it. Among the issues dealt with under the provisions are export arrangements, such as monopolies and pricing, renewable and energy efficiency 2030 targets, the integration of renewable energy into the wider electricity market, future cooperation on technical matters, and research and development.

The key principles of the IEM in relation to electricity and gas are covered, such as non-discriminatory access to networks, third party access to energy transport infrastructure, and a commitment to competitive electricity and gas markets. The unbundling of network operators and the principles of ownership unbundling, the role of an independent regulatory authority and efficient use of electricity and gas interconnectors are also covered. The Draft Agreement also sets out an outline of cooperation on supply security issues as well as infrastructure planning and offshore energy.

The UK, in turn, also published its negotiating position and has sent its version of the draft free trade agreement to the EU (which was published on 19 May 2020). On the basis of its negotiating position, the UK seeks a “Comprehensive Free Trade Agreement on Goods” (“CFTA”) as the cornerstone of its post-Brexit relationship with the EU. The envisaged CFTA comprises detailed rules on aspects such as the removal of technical barriers to trade, customs and trade facilities, capital movement, subsidies and competition policies, and rules of origin and trade remedies. The envisaged future relationship with the EU from the UK’s perspective sees a CFTA by a series of additional agreements, one of which would be on energy and would cover the facilitation of efficient cross-border electricity and gas trade, the facilitation of technical cooperation between electricity and gas network operators and organisations in the planning and use of energy infrastructure connecting their systems, support of the integration of renewable power, and investment in decarbonisation projects in the North Sea.

The UK appears more centred on energy trade with the EU across interconnectors, cooperation with transmission system operators and the European Network of Transmission System Operators (“ENTSOs”), and decarbonisation objectives, without setting out or referencing a regulatory framework within which to achieve this.

Whilst the energy provisions of the Draft Agreement are more detailed and, overall, tend to remain closer to the established principles of the IEM compared to the approach taken by the UK, the Draft Agreement provisions do, nonetheless, fall short of the IEM regime.

In April 2018, the EU issued a notice to stakeholders on the UK’s withdrawal from the IEM which sets out, from the EU’s perspective, the implications of the UK leaving the EU (and as a consequence, the IEM) and being treated as a third country in relation to energy with no new replacement arrangements in place:

- UK Transmission System Operators (“TSOs”) would not be party to the Inter-Transmission System Operator Compensation Mechanism and would be required to pay transmission system usage fees;
- UK TSOs would require certification to continue activities within the EU;
- UK TSOs would cease to participate in the single allocation platform for forward interconnection capacity, the European balancing platforms and the single day-ahead and intraday coupling;
- UK based wholesale power and gas market participants (and any other third country market participants who are registered in the UK) would need to register with a national energy regulatory authority in an EU Member State in which it is active in order to continue to trade;

- Directly applicable EU legislation, such as the Regulation on Wholesale Energy Market Integrity and Transparency (EU 1227/2011) and the Regulation on conditions for access to the network for cross-border exchanges in electricity (EC 714/2009), continues to apply in the UK until the end of the transition period.

**At the end of transition – will there be elements of no deal?**

- At the end of the transition period, if the new trading relationship is not in place, there could be a situation similar to no deal. It is more likely that this will be modified by the introduction of agreed elements of the future relationship or some other temporary set of rules, even though the UK Government has ruled out extending the transition period. Both sides have set out their respective negotiating positions. The UK and the EU have also released their versions of the draft UK-EU FTA – for further updates, please subscribe to our Brexit blog.

- However, there will be no clarity as to what will happen until towards the end of 2020 and the adage “plan for the worst, hope for the best” continues to apply and no-deal guidance therefore remains relevant. See the accompanying section: Leaving the EU - The process and preparations.

- The body of EU law in force at the end of 2020 will be imported into UK law (with necessary amendments) under the European Union (Withdrawal) Act 2018 and the UK legislation made to implement EU law will be retained, with suitable amendments – this will be called “retained EU law.”
entities controlled by the UK or UK nationals may be refused authorisation (or an existing authorisation may be challenged) for the prospection, exploration and production of hydrocarbons in EU Member States on grounds of national security; and

trade and fundamental data relating to the UK wholesale energy market will no longer be collected by ACER during a review period shortly after exit day, but will be collected by Ofgem instead. Following the review period, Ofgem will announce the start date of the new reporting scheme, allowing at least a three months’ period for market participants to adjust to the new requirements.

**Single Electricity Market on the island of Ireland (“SEM”)**

The Withdrawal Agreement’s Protocol on Ireland/Northern Ireland provides the basis for the continued operation of the Single Electricity Market and trade of wholesale electricity across the island of Ireland beyond the transition, whether or not there is any wider agreement between the UK and the EU on the future relationship.

However, a consequence of the UK being de-coupled from the iEM in a no-deal post-transition is that, in practice, Ireland is also de-coupled from the immediate benefits of being within the iEM as Ireland is currently dependent on the UK for any degree of electricity interconnection (pending the construction of interconnection between Ireland and France).

We consider it likely that the EU will be mindful of the interests of Ireland (as an EU Member State) when considering its response in a post-transition no-deal scenario to avoid stranding Ireland from its supplies of electricity and gas. Article 194(1) TFEU provides that EU energy policy shall ensure supply security in the EU in a spirit of solidarity.

**Electricity interconnectors**

In order for cross-border electricity trade to continue between the UK and the EU in any post-transition no-deal, new access rules for all interconnectors need to be approved in the UK and with the relevant EU Member State authorities. To that end, all interconnectors between the UK and continental Europe (France, Belgium and the Netherlands) have published their modified access rules for a no-deal and Ofgem has approved the proposed modifications in each case. Broadly, this means moving from the implicit day-ahead allocation under the iEM to explicit day-ahead allocation under the revised (no-deal) access rules of the relevant interconnector, analogously to how things operated prior to market coupling in 2014. For further details, please see below:

- IFA1 (France – UK) – IFA Access Rules and charging methodology,
- IFA2 (France – UK) – IFA2 Access Rules and charging methodology,
- NEMO (Belgium – UK) – Nemo Link Access Rules,
- BritNed (Netherlands – UK) – BritNed Access Rules,
- ElecLink (France – UK) – ElecLink Access Rules and modified charging methodology.

**Gas interconnectors**

Gas markets are already well integrated physically between the UK and the EU, through three interconnectors (IUK, BBL and Moffat) with only small wholesale price differences and little congestion. As a result, subject to any drastic changes in UK energy policy, the gas sector is unlikely to suffer following the end of transition.

However, it is likely that the UK will be excluded from the “solidarity principles”, whereby EU Member States agree to supply gas to their neighbours in the event of a gas supply crisis. Conversely, as Ireland is largely dependent on UK gas imports, it is possible that the EU tries to intervene in the form of a solidarity mechanism for Ireland.

**REMIT**

The UK is amending the EU’s REMIT regulations (prohibiting insider trading and energy market manipulation, and providing for market monitoring by regulators) for a no-deal under the Electricity and Gas (Market Integrity and Transparency) (Amendment) (EU Exit) Regulations 2019.

The changes are to “domesticate” the regime, with market participants facing the same transparency obligations and market integrity prohibitions as before. It is simply that the UK legislation can now only deal with the UK aspects of enforcement and regulation (and not the EU side). Market participants trading in wholesale energy products where delivery is within Great Britain are required to register with Ofgem. However, Ofgem has stated that, until further notice, this requirement will not apply to market participants already registered with an EU regulatory authority (or the Northern Ireland utility regulator). From the EU side, however, no such waiver has been proposed and so in order to trade on the EU wholesale energy market, registration with an EU Member State national authority will be required.

**Means:**

- Energy related UK domestic law, as well as licences and industry codes, will remain in place subject to changes required to ensure their operability. Ofgem has released guidance outlining the relevant modifications.
- UK market participants will need to register under REMIT with an EU regulatory authority to trade within EU wholesale energy markets.
- Operators of UK installations who are participants in the EU Emissions Trading Scheme (EU-ETS) will no longer be able to take part. See further information here.
- UK TSOs would require certification to continue activities within the EU.
**Upstream oil and gas**

EU Member States are sovereign as to their natural resources and any authorisations to prospect, explore and produce hydrocarbons. EU legislation for the upstream sector is limited and has largely been in line with the existing UK regulatory approach.

**Nuclear**

In November 2019, the Department for Business, Energy and Industrial Strategy (“**BEIS**”) published a quarterly update to Parliament on the UK’s exit from the Euratom Treaty. The report notes that the Government has now put in place all the necessary measures to ensure continuity of the UK’s nuclear industry, including in a no-deal, and continues to develop and strengthen a new domestic safeguards regime.

To ensure continuity of the UK’s civil nuclear trade following withdrawal from Euratom, among other things, the following regulations were made in 2019:

- **Nuclear Safeguards (EU Exit) Regulations 2019,**
- **Nuclear Safeguards (Fissionable Material and Relevant International Agreements) (EU Exit) Regulations 2019,**
- **Shipments of Radioactive Substances (EU Exit) Regulations 2019,**
- **Transfrontier Shipment of Radioactive Waste and Spent Fuel (EU Exit) Regulation 2019.**

To ensure continuity in the area of research and training, the **Euratom Research and Training Programme (Revocation) (EU Exit) Regulations 2019** were also made in 2019.

Civil nuclear energy is also addressed in the Draft Agreement released by the EU, broadly tracing the concepts of Euratom and providing a framework for cooperation between the EU and the UK in the peaceful uses of nuclear energy on the basis of mutual benefit and reciprocity.

**What kind of future relationship on energy might there be?**

The UK Government has made clear that it wants a new trading relationship with the EU which allows it the same sort of policy freedoms as are enjoyed by other major economies with free trade agreements with the EU, such as Canada and Japan. The UK wants the most ambitious future relationship agreement compatible with that aim.

This, together with the EU’s position, accepted by the UK, that any future agreement must respect the integrity of the Single Market and the indivisibility of the four freedoms, means that the UK will not remain part of the IEM after transition. However, it is in the interests of both sides (including to protect Ireland as referenced above) to ensure, as far as possible, security of supply and as efficient trade as possible over interconnectors.

Given the time pressures, energy may be a good candidate to be included as part of a work programme in the agreement on a new trading relationship to work on further details of the cooperation. Most existing free trade agreements contain such provisions including the EU’s agreement with Canada.

**Additional Resources**

- Trading electricity from 1 January 2021 guidance published by the Government;
- Together with The Boston Consulting Group and Global Counsel, we produced a report which looks in more detail at the implications for the UK and the EU27 of the post-Brexit energy market;
- Together with Global Counsel, we have written a paper which provides an overview of the legal and political background on the UK’s decision to leave Euratom available here.
Euratom: Nuclear co-operation agreements

Withdrawing the UK from the Euratom Treaty required separate notice to be given under the Euratom Treaty. This becomes relevant to supply chains both between the UK and Euratom members, as well as to all the other countries with whom the UK’s trade in the nuclear sector is currently reliant on Euratom membership (e.g., US, Australia and Japan).

The Nuclear Safeguards Act 2018 addresses the UK’s departure from Euratom and enables the Government to establish a domestic nuclear safeguards regime regulated by the Office of Nuclear Regulation (“ONR”). A UK nuclear safeguards regime is an essential pre-cursor to the future trade of nuclear materials and cooperation with other states on nuclear matters (previously done through the nuclear safeguarding regime of Euratom).

The UK also signed two new bilateral safeguards agreements with the International Atomic Energy Agency (“IAEA”) on 7 June 2018 to replace the existing trilateral arrangements between the IAEA, Euratom, and the UK, which affirmed the UK’s commitment to international safeguards and nuclear non-proliferation and provided the basis for civil nuclear trading arrangements. The agreements ensure that the IAEA retains the right to inspect all civil nuclear facilities and continues to receive safeguards reporting.

To ensure continuity of arrangements for the UK’s nuclear industry in all scenarios, including a no-deal, the Government signed a nuclear cooperation agreement (“NCA”) with the USA as well as with Australia and Canada. In February 2018, the UK and Japan signed an Exchange of Notes confirming the terms of the UK’s 1998 NCA with Japan, following the UK’s exit from Euratom.

BEIS, in conjunction with the ONR, has also published Technical guidance for nuclear operators on reporting requirements in relation to NCAs.

“If the UK and the EU do not reach some form of agreement on their future relationship by the end of the transition period, the UK’s participation in the Internal Energy Market ceases. This means the UK market will de-couple from the EU and revert to the situation which existed prior to market coupling in 2014.”

SILKE GOLDBERG

“But this does not mean there has to be physical disruption to interconnectors, it simply means, amongst other things, moving to new access rules and losing the single platforms to allocate Transmission System Operators long-term electricity transmission capacities and for balancing electricity at short notice.”

PAUL BUTCHER