

# KEY TCA ISSUES FOR THE ENERGY SECTOR

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Legal Briefings

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The EU-UK Trade and Cooperation Agreement ("**TCA**") establishes objectives for the energy market by providing for the facilitation of trade and investment between the EU and the UK (the "**parties**") in the areas of energy and raw materials, and supporting security of supply and environmental sustainability, notably in contributing to the fight against climate change in those areas.

Following the end of the transition period, the UK is now treated as a third country in relation to the EU generally, and this includes in relation to the Internal Energy Market ("**IEM**"). While the TCA avoids the imposition of tariffs (electricity and gas are classified as goods, as is equipment necessary to generate electricity, and as such no customs or tariffs will be imposed), it brings about a number of changes that will invariably have an impact on the UK and EU energy markets.

Generally, the energy provisions of the TCA, set out in Title VIII, are broad in nature and provide for a range of cooperation obligations and the prospect of detailed arrangements being made between the parties at specified times in the future.

This briefing provides a short overview of the main energy provisions in the TCA and discusses their likely impact on the UK energy sector.

## REGULATORY AND TSO COOPERATION

With the aim of ensuring that the objectives of the TCA are met, the UK regulatory authority, ie Ofgem, and the Agency for the Cooperation of Energy Regulators (ACER) must develop contacts and enter into administrative arrangements covering, among others, electricity and gas markets, access to networks, offshore energy, the efficient use of electricity and gas interconnectors, and gas quality and decarbonisation.

In relation to transmission system operators (“**TSOs**”), the parties commit to the establishing of technical procedures for transmission, and frameworks for cooperation between the European Network of Transmission System Operators for Electricity and Gas, respectively ENTSO-E and ENTSO-G, and the Great Britain (“**GB**”) TSOs. The TCA clearly states that these frameworks for cooperation will not involve, or confer a status comparable to, membership in ENTSO-E or ENTSO-G by GB TSOs.

The TCA also commits the EU and the UK to ensuring that “transmission system operators develop working arrangements that are efficient and inclusive in order to support the planning and operational tasks associated with meeting the objectives of this Title [VIII], including, when recommended by the Specialised Committee on Energy, the preparation of technical procedures to implement effectively” the provisions of the TCA on electricity and gas interconnectors, trading arrangements, grid developments and supply security.

At this early stage, the exact scope of these cooperation arrangements is unclear, as is the detail of their implementation.

## THIRD PARTY ACCESS AND UNBUNDLING

Third party access (“**TPA**”) and unbundling were essential elements in the liberalisation of the European energy sector, and continue to be core tenets in both British and EU energy legislation. The TCA retains these two concepts and commits the parties to safeguarding the principals of TPA and unbundling, albeit at a high level. The TCA does however include a form of exemption regime under which the UK or the EU can decide not to apply the TPA or unbundling provisions of the TCA if relevant conditions are met.

On unbundling, under the TCA the parties have a broad obligation to implement arrangements to remove conflicts arising as a result of the same person exercising control over a TSO and a producer or supplier. This obligation, based on the limited detail given in the TCA, appears unlikely to add further restrictions in addition to those already existing under the provisions of the EU Electricity Directive and the Electricity Act 1989. The TCA provisions also do not reference the unbundling models of the current EU regime that was introduced by the third energy package in 2009, which leaves open the possibility of alternative unbundling models in the UK in the future.

## INTERCONNECTORS

The TCA commits the UK and EU to cooperating to facilitate the timely development and interoperability of energy infrastructure connecting their territories (ie interconnectors). In as far as they relate to electricity interconnectors, the provisions of the TCA cover familiar ground in that they principally follow overarching principles set out in existing EU legislation governing electricity infrastructure, eg TPA, unbundling and congestion management.

The impact of these provisions on individual projects will depend on how the provisions are implemented in UK and EU law. For example, it is not clear how a decision by the UK or the EU not to apply the new 'exemption' regime of the TCA that allows the UK or the EU to decide not to apply TPA and unbundling requirements would impact the application of existing requirements of UK and EU law unless the relevant regulations are modified in order to implement the TCA.

## **CONGESTION MANAGEMENT AND TRANSMISSION COSTS**

Consistent with Article 16 of each of the EU Electricity Regulation and the UK Electricity Regulation (the EU Electricity Regulation is retained in UK law in an amended version following the expiry of the transition period), the parties are to ensure that capacity allocation and congestion management on electricity interconnectors is market based, transparent and non-discriminatory, and that the maximum level of capacity of electricity interconnectors is made available to the market.

Article ENER.13(1)(f) of the TCA requires the coordination of capacity allocation and congestion management between EU and GB TSOs, involving the development of arrangements for all relevant timeframes (forward, day-ahead, intraday and balancing). The parties are to ensure the conclusion between relevant TSOs of a multi-party agreement relating to the compensation for the costs of hosting cross-border flows of electricity which will aim to ensure that GB TSOs are treated on an equivalent basis to a TSO in a country participating in the inter-transmission system operator compensation mechanism. Until such time as this agreement is concluded, a transmission system use fee may be levied on scheduled imports and exports between the EU and the UK.

## **POWER TRADING**

GB TSOs will require certification to continue activities within the EU and will cease participation in EUPHEMIA, the single allocation platform for forward interconnection capacity, European balancing platforms such as TERRE and MARI, and the single day-ahead and intraday coupling mechanisms.

The UK market is now therefore de-coupled from the EU and has reverted to the situation which existed prior to market coupling in 2014. This means, amongst other things, that the UK market is moving to new access rules and losing access to the Joint Allocation Office, the single platform for allocation of long-term electricity transmission capacity to TSOs and short notice electricity balancing.

Once the UK became a third country to the EU, new access rules for all interconnectors were needed in the UK and with the relevant EU member state authorities in order for cross-border electricity trade to continue between the UK and the EU. In preparation for this, all operational interconnectors between the UK and continental Europe (France, Belgium and the Netherlands) had published modified access rules in the event of a no-deal Brexit, and Ofgem had approved the proposed modifications in each case. Broadly, this resulted in 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, which, according to the European Federation of Energy Traders (EFET) has led to increased costs in energy trading.

On a practical level, the UK's exit from the market coupling arrangements has had consequences for the European electricity markets: From 31 December 2020 Nord Pool's day-ahead auction has a new gate closure time of 09:50 GMT with results available no later than 10:00 GMT; in Ireland the SEM-GB intraday auctions (IDA1 & IDA2) continue to operate with shared order books between power exchanges, offering implicit capacity between the island of Ireland and GB. Explicit capacity auctions will be staggered throughout the morning, starting with the BritNed interconnector, followed by IFA, IFA2 and finally Nemo Link.

On electricity trading arrangements, the Specialised Committee on Energy, established under the TCA, will ensure that TSOs develop arrangements for technical procedures within specified timeframes - technical procedures must enter into force by 2022. The committee will keep the arrangements under review and, if not satisfied with those arrangements, can take decisions and make recommendations as necessary for each party to request its TSOs to prepare technical procedures in line with the timeframes.

## RENEWABLE ENERGY

The TCA contains a number of references to renewable energy and commitments by the EU and UK to maintain their current commitments in this regard (ie the commitments given under the relevant EU legislation and UK law, respectively). It does not however create any common climate change objectives or any new targets for renewable energy sources as between the EU and the UK. Instead, the TCA creates the bare regulatory minimum in terms of grid access and support for renewable energy sources.

In relation to renewable power, Article ENER.6 provides that the parties will enable the integration of electricity from renewable energy sources, and ensure the efficient and secure operation and development of the electricity system. In particular, the EU and the UK commit to ensuring that balancing markets are organised in such a way as to ensure that producers of renewable energy are accorded reasonable and non-discriminatory terms when procuring products and services.

In the same spirit, Article ENER.8 provides that the parties will ensure that TSOs treat producers of renewable energy on reasonable and non-discriminatory terms regarding connection to, and use of, the electricity network.

The TCA further provides, in Article ENER.21, that the parties commit to promoting energy efficiency and the use of energy from renewable sources, and ensure that its rules that apply to licencing or equivalent measures applicable to energy from renewable sources are necessary and proportionate. The parties are also committed to defining technical specifications which are to be met by renewable energy equipment and systems in order to benefit from support schemes.

Given the renewable energy potential in the North Sea, the parties will cooperate on establishing a specific forum for the development of renewable energy in the region and the development of an offshore grid. The parties' cooperation in relation to the development of renewable energy in the North Sea region will include hybrid and joint projects, sharing of information on new technologies, best practices on onshore and offshore grid planning and exchanges of best practices on rules, regulations and technical standards. This is an area that will be of particular relevance for the development of multipurpose interconnectors in the North Sea (eg, HVDC cables linking wind farms in different countries) and an area in which innovations in both EU and UK law will be necessary in order to accommodate such projects.

## **CLIMATE CHANGE**

The TCA does not provide for any substantive new objectives in relation to climate change. More broadly, the parties acknowledge that climate change represents an existential threat to humanity and reiterate their commitment to strengthening the global response to this threat. Both the EU and the UK commit to continuing to work towards the objectives of the Paris Agreement on Climate Change.

Accordingly, each party will respect the Paris Agreement and the process set up by the United Nations Framework Convention on Climate Change (UNFCCC) and refrain from acts or omissions that would materially defeat the object and purpose of the Paris Agreement. The parties also commit to advocating the fight against climate change in international forums, including by engaging with other countries and regions to increase their level of ambition in the reduction of greenhouse gas emissions.

The UK reaffirms, in Article ENER.21, its commitment for the share of energy from renewable sources in gross final energy consumption in 2030 and its ambition for the absolute level of primary and final energy consumption in 2030 as set out in its National Energy and Climate Plan, which was originally set up in compliance with the EU Governance Regulation adopted in December 2018.

## **CARBON PRICING**

The UK left the EU Emissions Trading System (“EU ETS”) at the end of the transition period, however UK participants in the EU ETS must continue to comply with their obligations under that system for the 2020 compliance year.

The TCA provides for the UK to introduce its own emission trading system (“UK ETS”) from 1 January 2021. Whilst it was intended for the UK ETS to commence operation from 1 January 2021, the system is not yet operational and a number of technical questions still need to be clarified by the UK’s Department for Business, Energy and Industrial Strategy, who will run the system, such as the level of free allocations, how many UK ETS allowances should be auctioned, and how exactly will the auctions work, including the auction schedule. The following elements of the UK ETS are currently known:

- Auctions will have a floor price of £15 per tonne and are understood to commence in the second quarter of 2021.
- ICE Futures administer the auctions for UK ETS allowances and launch spot and futures contracts.
- The UK ETS will cover energy intensive industries, power generators and aviation with a threshold of 20MW thermal input.

In the event of a no-deal Brexit, the UK Government had stated that it might introduce a carbon tax of £16 per tonne of CO<sub>2</sub>, and the anticipated introduction of a carbon floor price of £15 per tonne echoes this pricing level.

## NUCLEAR POWER

In addition to the TCA, the EU and the UK entered into the EU-UK Agreement for cooperation on the safe and peaceful uses of nuclear energy (“**NCA**”), which sets out the future relationship between the UK and Euratom. The scope of nuclear cooperation under the NCA includes the facilitation of trade and commercial cooperation, the supply of nuclear and non-nuclear material and equipment, safe management of spent fuel and radioactive waste, nuclear safety and radiation protection, monitoring of levels of radioactivity in the environment, and nuclear safeguards and physical protection. The UK will continue to participate in EU research and development programmes such as the Euratom Research and Training programme.

# SINGLE ELECTRICITY MARKET ON THE ISLAND OF IRELAND (ISEM)

The iSEM is based on a bilateral cooperation agreement between the Irish and UK Governments (rather than as a matter of EU legislation) covering both Northern Ireland and the Republic of Ireland. The UK leaving the EU will therefore not have the effect of repealing or terminating this arrangement. However, the iSEM is subject to EU regulation for the energy sector as it is regulated by the Irish Commission for Regulation of Utilities (CRU), together with the Northern Irish regulator, which, as regulator of an EU member state, is bound to apply EU regulations.

A consequence of the UK being de-coupled from the IEM is that, in practice, Ireland would also be de-coupled from the immediate benefits of being in the IEM as the Republic of Ireland is currently dependent on a single cross-border interconnector with the UK (pending the construction of the Celtic Interconnector between Ireland and France, which is expected to be commissioned in 2026).

The EU has been mindful of the interests of Ireland (as an EU member state) in the negotiations and, in relation to energy, of the future of iSEM to avoid stranding Ireland from its supplies of electricity and gas. Article 194(1) TFEU, after all, provides that EU energy policy shall ensure supply security in the EU in a spirit of solidarity. As a result, the EU has requested that the UK Government “take[s] all possible measures to maintain [the iSEM]”.

In Northern Ireland, the Ireland/Northern Ireland Protocol to the Withdrawal Agreement provides the basis for the continued operation of the Single Electricity Market (“**SEM**”) after 1 January 2021. As part of the Withdrawal Agreement, the UK Government committed to implementing the iSEM provisions at Article 9 and Annex 4 of the Protocol, which apply key elements of European energy law in Northern Ireland to enable the effective operation of the SEM across the island of Ireland.

## OUTLOOK

Due to the TCA’s ‘skinny’ scope and its architecture, which provides for a series of regular review dates and interim deadlines to negotiate further issues, it is likely that the UK will continue to negotiate various aspects of its relationship with the EU on a near-permanent basis.

One of the key issues for the immediate negotiations between the parties will be to establish the various cooperation arrangements between regulators and TSOs, and also to establish the procedures for the practical implementation of the TCA.

The provisions of the TCA related to energy are to cease to apply on 30 June 2026, but the Partnership Council (established under the TCA and to comprise representatives of the EU and the UK) may thereafter decide on an annual basis whether these provisions should continue to apply. The effect of the TCA energy provisions ceasing to apply will depend on how they are implemented by the EU and the UK, it is therefore too early as yet to judge the full impact these provisions will have on the UK and EU energy markets.

## KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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