



EUROPEAN COMMISSION

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COMMISSION DECISION

of 4 February 2014

on Spanish electricity tariffs: distributors

**SA.36559 (C3/2007) (ex NN 66/2006)
implemented by Spain**

(Only the Spanish version is authentic)

(Text with EEA relevance)

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THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union, and in particular the first subparagraph of Article 108(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having called on interested parties to submit their comments pursuant to the provisions cited above¹ and having regard to their comments,

Whereas:

PROCEDURE

- (1) By letter dated 27 April 2006, the undertakings Centrica plc and Centrica Energía S.L.U. (hereinafter collectively referred to as 'Centrica') filed a complaint with the Commission regarding the system of regulated electricity tariffs implemented in Spain in 2005.
- (2) By letter dated 27 July 2006, the Commission asked the Spanish authorities to provide information on the above measure. The Commission received this information by letter dated 22 August 2006.
- (3) On 12 October 2006, the case was registered as non-notified aid (Case NN 66/2006).

¹ OJ C 43, 27.2.2007, p. 9.

- (4) By letter dated 9 November 2006, the Commission asked the Spanish authorities for additional clarifications on the measure. The Spanish authorities replied by letter dated 12 December 2006.
- (5) By letter dated 24 January 2007, the Commission informed the Spanish authorities that it had decided to initiate the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union (TFEU) in respect of the measure.
- (6) The Commission decision was published in the *Official Journal of the European Union*². The Commission invited interested parties to submit their comments on the measure.
- (7) Spain submitted its observations by letter dated 26 February 2007.
- (8) The Commission received comments from the following interested parties: the Government of Galicia (letter dated 23 March 2007), Centrica (letters dated 26 March and 3 July 2007), ACIE – Association of Independent Energy Suppliers (letter dated 26 March 2007), Government of Asturias (letter dated 27 March 2007), AEGE – Association of Energy-Intensive Users (letter dated 2 April 2007), Asturiana de Zinc – AZSA (letter dated 3 April 2007), Ferroatlántica – a metal producer (letter dated 3 April 2007), Alcoa (letter dated 3 April 2007), UNESA – Spanish Electricity Industry Association (letter dated 25 April 2007), ENEL Viesgo (letter dated 26 April 2007), Iberdrola (letter dated 26 April 2007), Union Fenosa Distribución (letter dated 27 April 2007), Hidrocantábrico Distribución Eléctrica (letter dated 27 April 2007), Endesa Distribución Eléctrica (letter dated 27 April 2007).
- (9) By letters dated 15 May and 6 July 2007, the Commission forwarded the interested parties' comments to the Spanish authorities, who were given the opportunity to react; their comments were received by letter dated 2 August 2007.
- (10) Further information was submitted by Centrica by letters dated 1 June 2007, 28 August 2007, 4 February 2008 and 1 March 2008.
- (11) By letters dated 30 July 2009, 19 March 2010, 6 October 2011, 12 April 2012, 31 August 2012, 4 February 2013 and 17 July 2013, the Commission asked the Spanish authorities to provide further clarifications on the measure. The authorities replied by letters dated 5 October 2009, 26 April 2010, 7 December 2011, 12 June 2012, 18 October 2012, 11 February 2013 and 4 October 2013.
- (12) On 19 April 2013 the case was split into two parts: Case SA.21817 (C3/2007 ex NN 66/2006), which concerns aid to electricity end-users, and Case SA.36559 (C3/2007 ex NN 66/2006), which concerns aid to electricity distributors. The present Decision deals only with aid to electricity distributors.

DETAILED DESCRIPTION OF THE MEASURE

THE SPANISH ELECTRICITY SYSTEM IN 2005

Distinction between regulated and non-regulated activities.

² See footnote 1.

- (13) In the legislative framework laid down by Law 54/1997 of 27 November 1997 (*Ley del sector eléctrico* - LSE) which is the cornerstone of the Spanish electricity system, a fundamental distinction is made between regulated and liberalised activities.
- (14) The generation, import, export and retail supply of electricity are liberalised activities, i.e. activities which can be freely exercised by economic operators on market terms, and over which the State does not exercise strict regulatory control, for example by controlling prices and conditions of supply.
- (15) By contrast, distribution, transport and the activities carried out by the Market Operator³ and by the System Operator⁴ are fully regulated by the State. These activities are normally regulated by the State in any electricity system, since the operators which perform them hold *de facto* or *de jure* monopolies and, otherwise, the operators would not face any constraints in breaching the competition rules and would be able to charge monopolistic prices above the normal market price.

Pure distribution and supply at regulated tariffs

- (16) In 2005, distribution covered three types of regulated activity in the Spanish electricity system. The first was pure distribution. Pure distribution consists in the transmission of electricity to points of consumption over the distribution networks, and is a monopoly in the absence of alternative networks. The second includes certain commercial management activities closely related to distribution, such as reading meters, concluding contracts, invoicing, providing customer service, etc. The third regulated activity in 2005 was supply at the regulated tariff, and it was assigned by law to distributors in addition to their main statutory task (managing and providing access to electricity distribution networks)⁵. After the reform completed in 2009, distributors no longer supply electricity at regulated tariffs.
- (17) Distributors were required by law to purchase the electricity required to supply regulated customers in the organised wholesale market (the ‘pool’) at the daily price (the marginal system price or ‘pool price’) or directly from renewable energy producers⁶ and then to resell the electricity to final consumers at the applicable regulated tariff.

Role of distributors as financial intermediaries of the system

- (18) In 2005 there were no fewer than 25 different regulated tariffs for end-users, depending on the consumption level, the consumption profile and/or use of consumption and the network connection voltage. At the same time, 9 other regulated network access charges applied to end-users in the free market, also based on

³ The Market Operator (OMEL) handles purchases and sales of electricity in the wholesale market.

⁴ The System Operator (*Red Eléctrica de España*) is responsible for guaranteeing the security of electricity supply and the coordination of the production and transport system.

⁵ Article 11 of Royal Decree 281/1998 defines distribution as ‘that [activity] the main objective of which is the transmission of electrical energy from the transport network to consumption points under adequate quality requirements, as well as the sale of electrical energy to users or distributors at regulated prices’.

⁶ The so-called ‘special scheme’ generators. The ‘special scheme’ is a feed-in tariff system: distributors (and the transmission system operator) are obliged to purchase the entire output of eligible cogeneration and renewable-based installations located in their area of responsibility at a cost-covering rate set by the State.

connection voltage and other characteristics⁷. In the free market, network access charges were paid by end-users to suppliers, who passed them on to distributors. In the regulated market, network access charges were embedded in the all-inclusive regulated tariff paid by end-users to distributors (they were *implicit*). Since 2005 Spain has introduced changes to the system of regulated tariffs. The latest change dates from 2013, when Spain adopted a new legislative framework for the electricity sector (Law 24/13) which includes, among other measures, the reform of the regulation of retail market prices. Spain announced that this new law and its implementing provisions would be applied during 2014.

- (19) The levels of the regulated integral tariffs and the regulated network access charges were decided *ex ante* once for the whole year, normally before N-1 year end, but could be adjusted in the course of the year⁸. However, annual tariff increases were subject to a maximum cap⁹. In principle, all tariff and charge levels were set, on the basis of forecasts, in such a way as to ensure that the regulated revenues resulting from their application would suffice to cover the electricity system's total regulated costs. These regulated costs of the system included, in 2005, the costs of energy supply for integral tariffs, the costs of purchasing energy from special support schemes (renewable sources, cogeneration, etc.), transport and distribution costs, demand management measures, additional electricity generation costs in the Spanish islands, support for coal, previous years' deficits, etc.
- (20) In the regulatory set-up in Spain, distributors were (and still are) the main financial intermediaries of the system. Distributors handled all the revenue from the regulated tariff system, i.e. the network access charges and the revenue from integral tariffs. This revenue, collectively referred to as 'payable revenue' (*ingresos liquidables*), was used to cover all the regulated costs of the system. There were no rules earmarking a particular category of revenue, or a proportion thereof, for a particular category of costs or proportion thereof. As a result, revenues from network access charges were not earmarked in whole or in part to finance the higher costs of support for electricity generated from renewable sources or the costs of generation in the Spanish islands.
- (21) The clearance of accounts took place within the framework of a settlement process carried out under the direct control of the Spanish regulator, the *Comisión Nacional de Energía* (hereinafter: 'CNE'). The remuneration of distributors (for the activities related to pure distribution) was also drawn from the payable revenue, after deduction of all other costs.

Distributors vs suppliers and respective prices

- (22) Therefore, in 2005 two distinct categories of operator were active in the retail electricity market in Spain: distributors, who were obliged to sell at regulated tariffs, and suppliers, who sold on freely negotiated terms. For historical reasons, distributors in Spain are part of vertically integrated groups (incumbent operators) which have

⁷ Royal Decree 2392/2004, of 30 December, establishing the electricity tariff for 2005; Official State Gazette 315, p. 42766, Annex I.

⁸ Article 12(2) of the LSE provided that electricity tariffs were, in principle, set once a year but could be adjusted during the year.

⁹ Under Article 8 of Royal Decree 1432/2002, the average tariff could not increase by more than 1.40 % (year on year), whereas individual tariffs could increase only by a percentage calculated as the increase in the average tariff + 0.60 % (2 % in total).

traditionally operated distribution networks in specific geographic areas, and which have changed only owing to past mergers and consolidations. In the regulated market, distributors charged integral tariffs which did not distinguish between the costs of energy procurement and network access costs.

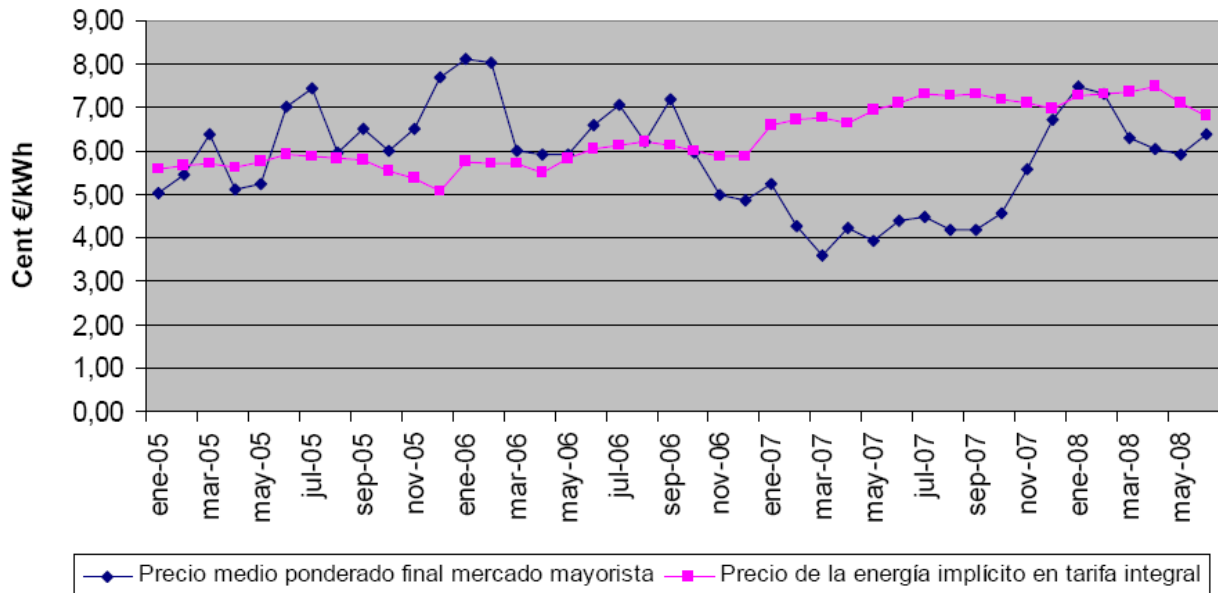
- (23) Suppliers can either belong to vertically integrated groups (which typically have separate generation, distribution and supply divisions) or be new market entrants. New entrants often do not own generation capacity and are active only in the retail market. Centrica is one such new entrant. In the free market, suppliers charged prices which had to cover the network access charge (payable to distributors), energy procurement costs (energy procurement costs in the wholesale market or own-generation costs in the case of a vertically integrated company) and a 'commercialisation margin', covering other costs (commercialisation costs, IT systems, billing, etc.) as well as a return on invested capital.
- (24) In 2005, the coexistence between the free and regulated markets, and in particular the possibility for end-users to switch freely between the two, meant that the regulated tariffs acted as a price reference (or *de facto* cap) on free-market prices. Therefore, a supplier could operate profitably in a given market segment only if there was a positive commercialisation margin, i.e. some headroom between the retail price - in this case the regulated tariff, to which the customer was entitled - and the overall costs incurred in serving customers.

The 2005 tariff deficit

- (25) In 2005, the level at which the regulated tariffs and the network access charges were set did not generate sufficient revenues to enable the system to recover all costs documented ex post for the entire year. The final settlement process for 2005, carried out by the CNE at year-end, established a deficit of EUR 3 811 million. It was not the first time that the settlement process had given rise to a deficit, although the size of the 2005 deficit was unprecedented. Lower deficits had already been recorded in 2000, 2001 and 2002.
- (26) Among other things, the Government underestimated actual electricity procurement costs. Whereas, in general terms, electricity consumption by end-users in both the regulated and the free market developed in 2005 roughly as predicted in December 2004, the unforeseen price increases during the year set wholesale prices at EUR 62.4/MWh in 2005 compared with EUR 35.61/MWh in 2004, bringing the average wholesale price in 2005 to EUR 59.47/MWh. The causes of this increase include an unusually dry year, which reduced hydroelectric power production by 55 %, a rise in oil prices, the passing on of the market price of CO₂ emission allowances received free of charge under the Emissions Trading System and an increase in the demand for energy higher than GDP growth.
- (27) The Spanish regulator, the CNE, pointed out that, in 2005, on average integral tariffs did not reflect all the costs of supply and, in particular, the cost of purchasing energy in the wholesale market. In particular, as shown in the graph below, only in five months, between January and February 2005, and then again between April and June 2005, were the energy prices implicit in the average regulated integral tariffs below average prices in the wholesale electricity market. However, the opposite was true between October 2006 and December 2007: during this 14-month period, average

wholesale prices fell sharply below the energy prices implicit in the average regulated integral tariffs, well in excess of the difference observed in the seven months of 2005 when wholesale prices were above those implicit in the integral tariffs.

Graph 1: Weighted average wholesale price vs energy price implicit in integral tariff



Source: CNE - Informe sobre la evolución de la competencia en los mercados de gas y electricidad. Periodo 2005/2007, p. 84.

- (28) An important factor which also contributed to increasing the general costs of the system was the high level of support for the production of renewable energy. In particular, renewable producers could opt for direct participation in the ‘pool’. In 2005, this option was particularly attractive and, as a result, more renewable producers than expected participated in the pool, leading to higher costs for the system. In addition, direct support for the energy costs of electricity from the special scheme (renewables, cogeneration) not sold to the pool, which was entered in the accounts as a regulated cost, amounted to EUR 2 701 million in 2005, an increase of 5.75 % over 2004. By way of illustration, the system’s transport and distribution costs amounted to EUR 4 142 in 2004, EUR 4 410 million in 2005 and EUR 4 567 million in 2006.

Mechanism adopted to pre-finance the deficit

- (29) The development of the deficit did not go unnoticed. Already in March 2005, when it became clear that a tariff deficit was developing, by Article 24 of Royal Decree-Law 5/2005¹⁰ the Spanish authorities stipulated that the funds required to bridge the gap between the costs and revenues of the electricity system would be provided by Spain’s five biggest ‘entitled electricity utilities’, which were those entitled to receive compensation for stranded costs¹¹, on the basis of the following percentages:

¹⁰ Royal Decree-Law 5/2005 of 11 March 2005 on urgent reforms to promote productivity and improve public procurement. Official State Gazette 62, 14.3.2005, p. 8832.

¹¹ Stranded costs are losses sustained by incumbent electricity providers as a result of non-recoverable investments carried out before liberalisation. The Commission authorised the granting of compensatory aid to cover such losses, on the basis of the criteria outlined in the Stranded Costs Methodology (Commission Communication relating to the methodology for analysing State aid linked to stranded costs),

- Iberdrola, S.A.: 35.01 %;
 - Unión Eléctrica Fenosa, S.A.: 12.84 %;
 - Hidroeléctrica del Cantábrico S.A.: 6.08 %;
 - Endesa, S.A.: 44.16 %;
 - Elcogás, S.A.: 1.91 %
- (30) The negative balance on the stranded costs account would give rise to collection rights, consisting in the right for the companies to collect revenue from electricity consumers in the future. The companies could securitise these rights and sell them in the market. These companies, with the exception of Elcogás S.A., are parent companies of vertically integrated groups which usually operate in the electricity generation sector, and in the distribution sector through distribution divisions. As Article 24 of Royal Decree-Law 5/2005 lays down, the motives and criteria governing the designation of these five companies for the purposes of pre-financing the 2005 tariff deficit – and not other companies operating in the Spanish electricity market - appears to be their right to receive compensation for stranded costs and not, for example, their activity in the distribution sector. Elcogás S.A. was and continues to be a company solely active in electricity generation¹². In the same way, for the purposes of pre-financing the deficit in the electricity system in later years, Spain has designated either the parent company of the group (e.g. Endesa S.A., Iberdrola S.A.) or its generation division (Endesa Generación S.A., Iberdrola Generación S.A. in Royal Decree-Law 6/2009), but never the distribution division (i.e. Endesa Distribución Eléctrica, S.L., a wholly owned subsidiary responsible for distributing electricity under the system of regulated tariffs in 2005).
- (31) In June 2006, the Spanish authorities took a decision concerning the arrangements for recovering the 2005 deficit from electricity consumers via the regulated tariffs. By Royal Decree 809/2006¹³, the Spanish authorities laid down that the 2005 deficit (or, more precisely, the collection rights granted to the five selected utilities) would be repaid by consumers over 14.5 years by means of a special surcharge applied to both integral and access tariffs. The surcharge, calculated as the yearly amount required to recover linearly the net present value of the 2005 deficit over 14.5 years, was set at 1.378 % of the integral tariff, and at 3.975 % of the access tariff for 2006. The applicable interest rate was the 3-month Euribor.
- (32) The surcharge was regarded as a ‘specifically earmarked contribution’ (*cuota con destino específico*). The Spanish authorities established that the revenues from the contribution to finance the 2005 deficit would accrue in the deposit account managed by the CNE. The CNE would then transfer the funds to the owners of the collection rights, i.e. the utilities that financed the deficit or the entities that had subsequently purchased the collection rights from them, according to the share of the deficit financed by each of them.

Effects of the tariff deficit on the Spanish market

by letter SG (2001) D/290869 of 6 August 2001. By Decision SG (2001) D/290553 of 25 July 2001 in Case NN 49/99, the Commission authorised Spain to grant compensation for stranded costs until 2008 to the same companies which were asked to pre-finance the 2005 deficit.

¹² Annual Report 2005, Elcogás SA, available at <http://www.elcogas.es/images/stories/3-principales-indicadores/1-datos-economico-financieros/esp2005.pdf>

¹³ First additional provision of Royal Decree 809/2006 of 30 June 2006 revising the electricity tariff from 1 July 2006. Official State Gazette 156, 1.7.2006.

- (33) In 2005, 37.49 % of electricity demand in Spain was procured in the free market. This quantity corresponds to a relatively small number of consumers; only 8.5 % of consumers purchased in the free market, whereas 91.5 % remained on regulated tariffs (down from 97 % in 2004). High-voltage customers (above all industrial customers) were the main category present in the free market; 38.9 % of them had exercised their option and their purchases accounted for 29 % of total electricity consumption in mainland Spain in 2005. The vast majority of households and small low-voltage consumers, which could opt for the free market from 2003¹⁴, were still on regulated tariffs; however, in 2005 a large number of them also opted for the free market. On 31 December 2005, over 2 million consumers were in the free market (compared with 1.3 million in 2004).
- (34) However, the price advantage afforded on average by the regulated tariffs in 2005 should be considered in parallel with the return of consumers to the regulated market, albeit with a certain time lag. As shown in Table 2 below, the number of consumers supplied in the free market increased throughout 2005 but declined in 2006, bringing the percentage (8.15 %) to that reached in the first half of 2005. Likewise, the decline in the amount of energy supplied to end-users in the free market that was apparent in December 2004 continued in the first half of 2005. Although it halted significantly between June and September 2005, it continued in December 2005 and throughout 2006.

Table 2 – Share of supply sites and energy in the free market (as a percentage of the whole market) 2004-2006

Electricity	2004				2005				2006			
	Mar	Jun	Sep	Dec	Mar	Jun	Sep	Dec	Mar	Jun	Sep	Dec
As a % of supply sites	1.53	2.82	4.21	5.73	7.42	9.42	10.37	10.66	10.20	9.28	8.86	8.15
As a % of energy	29.30	33.60	36.19	33.57	33.15	35.34	41.39	37.41	29.38	27.10	25.74	24.87

Source: CNE Report 'Nota Informativa sobre los suministros de electricidad y gas natural en los mercados liberalizados, actualización 31 de diciembre de 2006'.

- (35) Although the impact of the losses borne by suppliers began to be felt by mid-2005, when wholesale prices started to increase considerably, supply contracts could not be terminated immediately. As a result, suppliers in the free market, particularly those which did not have generation capacity but had to procure electricity in the wholesale market, were forced to choose between making offers under free-market conditions which matched the regulated tariff, despite the possibility of incurring losses, and charging higher prices reflecting actual procurement costs, thereby losing market share.

¹⁴ Spain liberalised the retail electricity market earlier than required by the 1996 and 2003 Electricity Directives, which provided for a liberalisation timetable between 1999 and 2004 for business end-users (starting with the largest) and made the liberalisation of the household segment mandatory only from 1 July 2007.

DECISION TO INITIATE THE PROCEDURE UNDER ARTICLE 108(2) OF THE TFEU

- (36) The Commission decision to initiate the formal investigation procedure was based on the following grounds:
- (37) The decision compared the regulated tariffs paid by the various categories of end-user with the estimated prices they would have had to pay in the free market in the absence of the tariffs, and found that there seemed to be an advantage in favour of most user categories. The alleged aid in favour of end-users is the object of a separate decision in Case SA.21817 - Regulated Electricity Tariffs: consumers.
- (38) As regards distributors, the opening decision indicated that, by encouraging end-users to switch back to the regulated market, the system might have benefited distributors, who appeared to have enjoyed a guaranteed profit margin on their regulated activities. This advantage seemed to have been granted selectively to distributors, as they were the only market operators allowed to sell electricity at regulated tariffs.
- (39) The decision also found that the system involved a transfer of state resources, since the price surcharge used to repay the deficit constitutes a parafiscal levy, the proceeds of which transit through the Spanish regulator CNE (a public body) before being channelled to the final beneficiaries. The decision concluded that, in the light of Court of Justice case-law on this matter, these funds should be regarded as state resources.
- (40) Considering that both large end-users and distributors operate in markets which are generally open to competition and trade within the Union, in the opening decision the Commission concluded that all the criteria laid down in Article 107(1) TFEU were fulfilled and the measure constituted state aid in favour of end-users and distributors.
- (41) After noting that none of the derogations provided for in Article 107 TFEU seemed applicable, the opening decision assessed whether the supply of electricity at regulated tariffs could be considered a service of general economic interest (SGEI) and as such benefit from the derogation provided for in Article 106(2) TFEU. The opening decision stated that, in the electricity sector, Member States' margin of discretion in establishing public service obligations is limited by the provisions of Directive 2003/54/EC of the European Parliament and the Council of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC¹⁵ ('The Electricity Directive'). The Electricity Directive requires Member States to establish a universal service obligation (including notably the right to be supplied at reasonable prices) only for household consumers and small enterprises¹⁶. The decision concluded that, in the light of the above Directive, the supply of electricity at regulated tariffs to medium-sized and large undertakings, as

¹⁵ OJ L 176, 15.7.2003, p. 37.

¹⁶ Article 3(3) of the 2003 Electricity Directive states: 'Member States shall ensure that all household customers, and, where Member States deem it appropriate, small enterprises, (namely enterprises with fewer than 50 occupied persons and an annual turnover or balance sheet not exceeding EUR 10 million), enjoy universal service, that is the right to be supplied with electricity of a specified quality within their territory at reasonable, easily and clearly comparable and transparent prices. To ensure the provision of universal service, Member States may appoint a supplier of last resort.'

opposed to households and small businesses, could not be considered an SGEI in the strict sense of the term.

- (42) The Commission thus expressed serious doubts as to whether the elements of aid in the regulated tariffs that were applied to undertakings other than small enterprises and to distributors could be considered compatible with the internal market.

COMMENTS BY INTERESTED PARTIES

- (43) The Commission's invitation to submit comments on the decision to open the in-depth investigation attracted numerous submissions from large industrial consumers, distributors, independent suppliers and governments of Spain's Autonomous Communities. Only the observations relevant to the position of distributors will be examined here.

COMMENTS FROM INDEPENDENT SUPPLIERS

- (44) Comments were received from Centrica and ACIE, the Association of Independent Energy Suppliers. Their arguments and conclusions are largely equivalent and will be dealt with together.
- (45) The main focus of Centrica's submission is the alleged state aid granted to electricity distributors. Centrica points out that in 2005 the average cost of buying electricity in the wholesale market was nearly 70 % higher than the forecast average procurement cost embedded in the integral tariffs set by the Government by Royal Decree 2329/2004.
- (46) As a result of this discrepancy between these forecasts and actual costs, the revenue from the system was insufficient to cover costs, mainly because the price paid by distributors to purchase electricity was higher than the regulated price at which they had to sell it. The distributors therefore recorded a deficit in their accounts. However, as a result of the mechanism adopted by the Spanish authorities to fill the revenue gap (which consisted in requiring eligible generators to pre-finance the deficit against a claim for subsequent reimbursement), the distributors' accounts remained balanced, and their losses were *de facto* offset by the State.
- (47) A different treatment was reserved for free-market suppliers, despite the fact that they also suffered similar losses. According to Centrica and ACIE, suppliers in the free market were subject to similar procurement costs as distributors¹⁷. Moreover, they were *de facto* bound by the level of the integral tariff set by the Government for each customer category because otherwise they would have been unlikely to attract new customers or retain existing customers. In particular, ACIE points out that, at the beginning of 2005, its members concluded contracts based on government forecasts of wholesale prices and that they later had to honour such contracts even though they turned out to be unprofitable. As a result, independent suppliers suffered losses. However, unlike distributors, independent suppliers' losses were not offset by the

¹⁷ Suppliers also bought power in the wholesale market ('the pool') and even though, theoretically, they could have entered into bilateral agreements with generators, in reality there was no incentive for generators (mainly vertically integrated groups) to do so.

State. Centrica estimates that in 2005 it suffered losses of EUR 10 million. According to ACIE, several suppliers, including Saltea Comercial, Electranorte, CYD Energia and RWE, were forced out of the market.

- (48) According to ACIE and Centrica, the compensation of distributors' losses distorted competition, created discrimination vis-à-vis independent suppliers and should be regarded as state aid. Apart from asserting that the compensation of losses constitutes an advantage per se, Centrica argued that incumbent market players (vertically integrated undertakings) could retain their market share and avoid losses by encouraging customers to switch from their loss-making supply divisions to their distribution divisions, which would receive compensation, where appropriate.
- (49) According to ACIE and Centrica, the advantage for incumbent undertakings was 'specific' i.e. selective, since the financing and compensation mechanism specifically benefited distributors by giving them a financial and competitive advantage over free-market suppliers. Centrica argued that the distinction between distributors and free-market suppliers was purely formal, because both categories competed in the same market (retail electricity sales), both were affected by integral tariffs (either because they had been imposed by law or because they acted *de facto* as a cap on market prices) and both procured electricity at the same price and suffered the same losses.
- (50) In Centrica's view, the preferential treatment of distributors was not justified by any reason pertaining to the logic and structure of the electricity system, nor could it be considered compensation for a service of general economic interest. Centrica maintains that the system breached the Electricity Directive, not only because of the discriminatory nature of the deficit arrangements, but also because consumers were deprived of the right to transparent prices and tariffs¹⁸. Since part of the electricity price payable for 2005 was deferred to future years, the final prices charged were not clear to consumers.
- (51) Centrica takes the view that the selective advantage afforded by the deficit arrangements benefited not only distributors, but also the vertically integrated undertakings to which they belonged. According to Centrica, a vertically integrated group should be regarded as one undertaking for the purpose of applying the state aid rules. Centrica alleges that the Spanish system allowed generation companies to raise prices in the wholesale market and continue to make profits. In these circumstances, the groups had a vested interest in maintaining the market share that their distribution divisions counted on. Therefore, the vertically integrated groups should also be regarded as recipients of state aid.

COMMENTS FROM DISTRIBUTORS

- (52) Comments were received from UNESA (the association representing distributors), Iberdrola Distribución, Union Fenosa Distribución, Enel Viesgo Distribución and Endesa Distribución. Their observations largely overlap and will be dealt with together.

¹⁸ See Annex I, letters (b) and (c) to Directive 2003/54/EC.

- (53) Distributors (as represented by UNESA) make a distinction between pure distribution/commercial management activities, which they view as an SGEI, and supply at regulated tariffs, which according to them did not involve any state aid because it did not provide a financial advantage.
- (54) Distributors recall that the legal context in which suppliers and distributors carried on their activities was very different; distributors were obliged to purchase electricity for supply at regulated tariffs in specific ways (either from the pool or from ‘special scheme’ producers), whereas suppliers were free to negotiate their prices. Distributors could not refuse to supply regulated customers and could not acquire customers other than those opting for regulated tariffs. Distributors could not offer auxiliary services either, whereas suppliers were free to establish their supply conditions.
- (55) The table below summarises the differences between free-market suppliers and distributors as regards retail sales of electricity¹⁹:

	Obligation to supply	Potential market	Energy purchases
Suppliers	No	All Spanish users	Any mechanism
Distributors	Yes	Only users connected to their networks	Via the pool or from special scheme generators
	Wholesale purchase price	Sales price	Profit margin
Suppliers	Free	Free	Margin on sales
Distributors	Pool price or regulated ‘special scheme’ price	Regulated tariffs	No profit margin

- (56) Distributors thus conclude that, given the different legal and factual context, free-market suppliers were not in competition with distributors, but rather with the regulated tariffs, which acted as the reference price in the market.
- (57) Distributors submit that the activity of supplying electricity at the tariff did not bring them profits or advantages of any nature. Whereas for pure distribution and commercial management the distributors’ remuneration included a profit margin to remunerate invested capital, for supply at regulated tariffs, distributors obtained only a reimbursement of their costs without any profit margin. In particular, the costs ‘recognised’ to a distributor were based on the average weighted price paid for electricity during the reference period. In certain circumstances, these recognised costs could be lower than the actual total costs borne by a distributor. When the regulated sales activity yielded a surplus, these funds did not stay with distributors but were allocated, during the settlement process, to the financing of other general costs of the system. The amount recognised by the State equalled the difference between the average weighted price of electricity purchases, multiplied by the quantity of energy transported by each distributor, after correction for standard losses.

¹⁹ Source: observations by Iberdrola dated 26 April 2007.

- (58) Distributors further contend that they did not draw any direct or indirect financial benefit from free-market customers switching back to regulated tariffs, as their remuneration for pure distribution and commercial management was entirely independent of the number of customers on regulated tariffs or the quantity of electricity sold at the tariff.
- First, as explained above, for supply at the regulated tariff there was only a reimbursement of costs.
 - Second, the remuneration of pure distribution was also independent of the number of customers on regulated tariffs, as it was based on the volume of ‘transported energy’, which included all electricity transported by distributors on the network, irrespective of whether the energy was sold at the regulated tariffs or at free-market rates.
 - Third, the remuneration for commercial management activities was also independent of the number of customers supplied on regulated tariffs, as the law provided for payments based on the number of contracts concluded (for both access tariffs and regulated tariffs) and was therefore unrelated to the number of customers on regulated tariffs. Distributors were required in any event to manage all customers’ requests, such as changes in the type of connection, contracts, invoicing of access tariffs, metering, etc., regardless of the type of supply.
- (59) Distributors thus conclude that the ‘compensation’ they received in respect of supplies at regulated tariffs should be viewed rather as the reimbursement of sums they were required to advance in application of the law, or as compensation for loss and damage.
- (60) Iberdrola specifically contends that it would be legally and economically incorrect to impute the deficit to distributors. The costs incurred in purchasing electricity for the regulated market were imputable to the electricity system, not to distributors, which merely implemented legal provisions. The proceeds of sales at regulated prices never became the property of distributors, but belonged to the electricity system as a whole, and therefore the system should be seen as the ‘seller’ of electricity at regulated prices. In a system as highly regulated as the Spanish one, it would be unreasonable, according to Iberdrola, to impute to distributors the financial imbalances caused by the regulatory structure or by errors in estimates of future energy costs.
- (61) Iberdrola also points out that distributors did not retain the revenue from the surcharge, which, as a ‘specifically earmarked contribution’, was transferred immediately to the deposit account opened by the CNE and passed on to the generators who pre-financed the deficit.

COMMENTS BY THE REGIONAL GOVERNMENT OF ASTURIAS

- (62) The comments by the Regional Government of Asturias are equivalent to those set out below by the Spanish Government, to which reference is made.

COMMENTS BY SPAIN

- (63) Spain maintains that the regulated tariffs system in 2005 did not involve aid, either for end-users or for distributors. In particular, as regards distributors, Spain considers that the compensation they received is in line with the *Altmark* case-law of the Court of Justice and does not, therefore, constitute state aid.

EXISTENCE OF AID

NO CAUSAL LINK BETWEEN STATE ACTION AND THE DEFICIT, AND NON-IMPUTABILITY OF THE DEFICIT TO THE STATE

- (64) Spain contends that the deficit was not imputable to the State, in that it was caused by unpredictable external circumstances and not by the State's deliberate intention to subsidise certain activities.
- (65) Spain submits that supply at regulated tariffs set by the State was not precluded by EU law in 2005. Therefore, state regulatory intervention was legally valid, as it was the expression of national sovereignty. One of these sovereign prerogatives consists in setting the tariffs so that expected costs match expected demand.
- (66) Distributors collected funds through integral and access tariffs, and then transferred part of this revenue to dedicated accounts (according to percentages set in the annual tariffs decree). Afterwards they deducted electricity purchases from the pool and from 'special scheme' generators. If the revenue from integral and access tariffs did not cover the cost of regulated activities, a tariff deficit was generated.
- (67) Spain submits that the 2005 deficit was caused by a discrepancy between government forecasts of wholesale electricity prices and the actual prices recorded on the pool. The exceptionally high prices of 2005 were driven by unpredictable causes amounting to force majeure (see recital (26)).
- (68) Since the event generating the alleged aid was a higher-than-forecast increase in wholesale prices, the alleged advantage could not be imputable to any legal act. Even assuming that this advantage had existed, it would have been caused by circumstances unrelated to the State's intentions. The existence of force majeure, according to Spain, breaks the causal link between the administrative decision setting the level of the tariffs and the competitive advantage giving rise to state aid. Even assuming that the objective condition of the causal link was met, the subjective condition of intention (imputability) on the part of the State would be absent.

NO STATE RESOURCES

- (69) Spain submits that the tariffs did not involve public funds. First, Spain claims in this respect that the surcharge is not a 'charge' within the meaning of the case-law of the European Court of Justice on parafiscal levies, because it is not collected by the State and does not correspond to a fiscal levy. According to Spain, the surcharge is an integral part of the tariff and is tariff-like in nature. The tariff is thus a private price.
- (70) Second, the funds were not collected by the State and were not paid into a fund designated by the State. The tariffs were collected by distributors, not by the State, and therefore they were private prices which ensured the equitable remuneration of the

players (as laid down in the LSE). They were neither taxes nor public prices. The State did not remunerate anything, since it was the system that provided remuneration by virtue of market forces for non-regulated activities and by virtue of access tariffs set by the State as regards regulated activities. Since in such a system there is no burden for the State, no state resources would be involved, according to the *Sloman Neptune* case-law²⁰. Furthermore, these funds never flowed into the state coffers, were not mentioned in budgetary laws, were not subject to verification by the Court of Auditors, and could not be recovered from debtors by means of administrative recovery procedures. Debts vis-à-vis the electricity system were not subject to the interest rate applicable to debts owed to the State.

- (71) Spain insists that these funds were handled by the Spanish regulator, the CNE, acting as a mere accounting intermediary. The Spanish authorities point out that in its 2001 decision on the Spanish stranded costs (SA NN 49/99) the Commission had already established that ‘the transit of funds through the CNE is of an essentially accounting nature. The funds transferred to the account in the name of the CNE never became the property of this body, and were immediately paid to the beneficiaries according to a pre-determined amount which the CNE is unable to modify in any way’. On the basis of this consideration, the Commission came to the conclusion that ‘it [was] not in a position to determine whether the proceeds of the levy established within the framework of the Stranded Costs scheme constitute state resources’.
- (72) Third, Spain contests the Commission’s conclusion that regulated sales by distributors were financed via a ‘special tax’ payable by all Spanish electricity end-users. According to Spain, distributors were not ‘financed by the State’, but received a reasonable and equitable remuneration for the performance of a statutory task which they were obliged to discharge.
- (73) Besides, in selling electricity at regulated tariffs and purchasing it on the ‘pool’ from generators, distributors generated a deficit (which was covered by the pre-financing mechanism laid down by Royal Decree-Law 5/2005) but it was the generators, not the distributors, which would receive the revenue from the surcharge added to the tariff.

NO ADVANTAGE

- (74) Spain disagrees with the Commission’s preliminary conclusion that regulated tariffs conferred an economic advantage on distributors.
- (75) As regards distributors, Spain contests the Commission’s conclusion that the tariff systems guaranteed a minimum profit margin to distributors. Spain submits that supply at regulated tariffs by distributors was justified by the need to guarantee a service of general interest, and that the remuneration of regulated activities was intended exclusively to cover the costs of discharging the obligations linked to these activities.

²⁰ Judgment of the Court of Justice in Joined Cases C-72/91 and C-73/91, paragraph 21: ‘The system at issue does not seek, through its object and general structure, to create an advantage which would constitute an additional burden for the State’.

NO IMPACT ON COMPETITION AND TRADE BETWEEN MEMBER STATES

- (76) According to the Spanish authorities, the regulatory provisions applicable to supply at regulated tariffs did not curtail the freedom of establishment of electricity suppliers and there was no preferential treatment of Spanish suppliers compared with suppliers from other Member States.
- (77) In 2005 the Iberian Peninsula had such a low interconnection capacity that there was no real internal market for energy. The Spanish authorities take the view that, given this situation of isolation, it would be disproportionate to conclude – as the Commission does – that the tariff had an impact on competition and trade between Member States.
- (78) The Spanish authorities maintain that electricity was not exported outside Spain and distributors operating in Spain could not sell Spanish energy outside the national territory. On the other hand, any eligible company could take part in the distribution business on an equal footing with Spanish undertakings and enjoy the same legal and economic treatment.
- (79) Spain takes the view that suppliers, by contrast, exercised a free, non-regulated activity. They faced the corresponding risks and advantages. Taking these risks meant accepting that, under certain unpredictable conditions, their retail activity might not be profitable. Profitability would nevertheless return as soon as the tariffs allowed or the exceptional circumstances ceased to exist.

ANALYSIS IN THE LIGHT OF THE *ALTMARK* CASE-LAW

- (80) Spain submits that in 2005 the existence of regulated tariffs was not contrary to Union law, given that the deadline for opening up the market to all consumers, including households, was 1 July 2007.
- (81) According to Spain, the coverage of the costs incurred by distributors in supplying at regulated tariffs complied with the four criteria of the *Altmark* case-law and therefore this intervention does not fall within the scope of state aid.
- (82) First, the supply of electricity is a service of general interest and the State must intervene to prevent abuses of dominant positions arising from the existence of a single network (natural monopoly). Therefore, companies which carry on regulated activities discharge public service obligations.
- (83) Second, the parameters for setting the tariffs were set in an objective and transparent manner. The remuneration of regulated activities was objective and transparent. Other EU undertakings were also able to enter the distribution market.
- (84) Third, payments for regulated activities covered only the costs of discharging the public service obligation. Distributors could obtain repayment only of the costs related to regulated activities.
- (85) Fourth, the complex regulatory framework for setting the tariffs and the settlement procedure demonstrate that the tariff system was based on a thorough analysis of the costs and revenues of the system, and an analysis of electricity demand.

- (86) On this basis Spain concludes that the tariff system did not constitute state aid because it complied with the *Altmark* case-law.

ASSESSMENT OF THE MEASURE

- (87) The scope of this Decision is confined to the supply of electricity to large and medium-sized undertakings by distributors at regulated tariffs, and does not cover the other activities carried on by distributors and pertaining to pure distribution. The latter are entirely independent, both legally and financially, from the activity of selling at regulated tariffs, and in any event, fall outside the scope of the opening decision, which raised doubts only about the compatibility with the internal market of the alleged advantage granted to distributors as a result of the low level of the regulated tariffs and the measures taken to compensate and refund the deficit in 2005.

EXISTENCE OF STATE AID PURSUANT TO ARTICLE 107(1) TFEU

- (88) A measure constitutes state aid within the meaning of Article 107(1) TFEU if all of the following conditions are fulfilled: the measure (a) confers an economic advantage on the beneficiary; (b) is granted by the State or through state resources; (c) is selective; (d) has an impact on intra-Community trade and is liable to distort competition within the Union. Since these conditions must be met cumulatively, the Commission will confine its assessment to the existence of an economic advantage conferred on the beneficiaries.

Existence of an economic advantage

- (89) Undertakings are favoured within the meaning of Article 107(1) TFEU if they obtain an economic advantage which they would not otherwise obtain under market conditions. In this respect, the Court of Justice of the European Union has held that, in specific cases, fees for services provided in return for obligations which Member States impose, which do not exceed annual uncovered costs and which are intended to ensure that the undertakings concerned do not make losses, do not constitute aid within the meaning of Article 107(1) TFEU but rather consideration for the services performed by the undertakings concerned²¹.
- (90) More specifically in the electricity sector, nor has the Commission taken the view, in its extensive decision-making practice in application of Article 107(1) and (3)(c) TFEU regarding the obligations imposed on distributors to purchase electricity from certain energy sources at a price above the market price, that compensation covering the difference between purchase costs and market prices entailed an economic advantage benefiting distributors. In those cases, the operators in question were acting under regulatory obligations as mere intermediaries in the electricity system and were compensated for their costs, without this compensation being held to entail an economic advantage, whereas, arguably, the legislation could have merely imposed a purchase obligation without cost compensation.
- (91) The same is true, more specifically in the area of the supply of electricity at regulated tariffs, as regards compensation intended to finance differences between revenues and

²¹ Judgment of the Court of Justice in Case C-240/83 *Procureur de la République v Association de défense des brûleurs d'huiles usagées (ADBHU)* [1985] ECR 531, especially pp. 543-544 and paragraph 18.

wholesale electricity procurement costs at regulated tariffs requested by eligible consumers²². It follows that compensation of the electricity purchase costs of distributors in the electricity sector does not necessarily imply an economic advantage within the meaning of Article 107(1) TFEU. The alleged compensation to Spanish distributors for the costs of supply at regulated tariffs must be examined in the light of these precedents.

- (92) The preliminary conclusion of the Commission decision opening the formal investigation was that there was an economic advantage over market conditions in favour of Spanish distributors on the basis of two arguments. First, distributors allegedly obtained a guaranteed profit margin on the activity of supply at the regulated tariff. Second, by encouraging users to switch to the regulated market served by distributors, the tariffs allegedly increased the distributors' income. These two arguments can be subsumed into the single proposition that distributors' profit increased in proportion to their supplies of electricity at regulated tariffs in 2005.
- (93) The available description of the Spanish electricity system and the information supplied in the course of the proceedings, which is reflected in recitals 16, 19, 20, 57 and 58, does not lend support to this proposition. Whereas, for pure distribution, the remuneration received by distributors in 2005 included a profit margin, for supply at the regulated tariff distributors received only a reimbursement ('recognition') of costs without any profit margin. Similarly, the distributors' remuneration in respect of their pure distribution activities was independent of the number of customers on regulated tariffs and the quantity of electricity sold at the tariff, and therefore their revenue would not have increased if they had served a larger number of customers on regulated tariffs.
- (94) It follows that the information gathered during the proceedings does not support the assertion that sales of electricity at regulated tariffs increased the profits of Spanish distributors in 2005 because they enjoyed a guaranteed profit margin.
- (95) On the question whether the recognition of supply costs and compensation thereof provided distributors with an economic advantage which they would otherwise not have obtained under market conditions, it must be stressed that the recognition of the costs incurred in the form of collection rights granted to the five undertakings designated by Article 24 of Royal Decree-Law 5/2005, namely Iberdrola, S.A., Unión Eléctrica Fenosa, S.A., Hidroeléctrica del Cantábrico S.A., Endesa, S.A. and Elcogás, S.A., was not remuneration for their distribution activity. As already explained in recitals 29 and 30, although Elcogás S.A., which did not own any subsidiaries, was not operating in the distribution sector in 2005 (or in later years), the undertakings in questions were designated by virtue of their existing right to receive stranded costs, possibly taking into account their generation activity, but not their distribution activity at regulated tariffs.
- (96) Second, even assuming that the collection rights that reflect the obligation for the five undertakings referred to above to pre-finance the deficit in the electricity system

²² Commission Decision of 12 June 2012 on state aid SA.21918 (C 17/07) (ex NN 17/07) implemented by France — Regulated electricity tariffs in France, OJ C 398, 22.12.2012, p. 10, especially paragraphs 30 to 37 and 134 to 137.

for 2005 could be interpreted as compensation for the costs of distribution for the four undertakings that operated in the distribution sector at regulated tariffs, account should be taken of the actual conditions under which distributors were obliged to carry on this fully regulated activity. As already described in recitals 54-55, distributors could make neither profits nor losses, could not choose how to procure electricity, could not select their customers, could not determine the sales price or offer any additional services yielding a profit margin. The distributors themselves, and also the vertically integrated groups to which they belonged, had no economic interest, whether direct or indirect, in engaging in the supply of electricity at the regulated tariff. A vertically integrated group would rather have an interest in serving end-users on free-market terms, as its supply division would have made a profit on such sales, which would not be the case if users were supplied by the group's distributor at regulated tariffs.

- (97) It follows that a comparison with the terms of supply under free market conditions disregards the different legal and factual situation between free-market suppliers and distributors supplying at regulated tariffs. Whereas the State can, in principle, impose purchase and selling prices and other trading conditions on distributors in an electricity system, this does not mean that the compensation of costs incurred by the latter confers on them an economic advantage which they would not otherwise obtain under market conditions. Indeed, tariff regulation further backed with an obligation to supply leaves no freedom to decide on the most fundamental drivers of supply, such as prices and output. It is not only under hypothetical market conditions, i.e. in the absence of regulatory constraints regarding such fundamental parameters, that distributors would be able to charge a much higher, cost-covering tariff to end-customers. Moreover, and even more importantly, in the Spanish electricity system in 2005, as in every electricity system, the distributor – or the operator of the high-voltage network for energy-intensive consumers - is simply an intermediary which physically connects the user to the network, as a necessary condition for the supply of electricity. Given the absence of a hypothetical alternative distribution network in Spain in 2005, the distributors in question were designated and supplied both the free market and the regulated market. Distributors play an essential role because they make the supply of electricity possible, regardless of the specific regulatory arrangements or policy, or of whether the competitive conditions governing supply are based on market mechanisms or regulation.
- (98) In a regulated tariff system, such as the Spanish system in 2005, in the ordinary course of business, a shortfall of resources in the system's overall accounts one year would usually be recouped the following year through higher tariffs and/or access charges for end-users, whereas cost decreases might result in a surplus, allowing lower tariffs or charges thereafter. However, in the absence of the earmarking of specific categories of revenues to costs, the increase (decrease) in revenues and/or costs may not result in a corresponding deficit or surplus benefiting distributors. For instance, as shown in recital 27, graph 1, whereas the energy prices implicit in regulated tariffs were generally below wholesale market prices in most months of 2005, the opposite is true in the period from November 2006 to December 2007, without this being reflected in increased profits for distributors' activity of supply at regulated tariffs. This is consistent with the regulatory set-up of the system, whereby distributors would not bear the costs of imbalances in the system's costs and revenues as a whole or in part, just as they would never make a profit on this activity, and any surplus arising from sales of electricity at regulated tariffs would be used to cover other system costs.

- (99) Distributors acted as financial intermediaries of the electricity system in that they centralised all the financial flows, both incoming (regulated revenues from tariffs and access charges) and outgoing (all the general costs of the system). The electricity system's regulated revenues and costs in 2005, as described in recitals 19, 20 and 28, include a wide variety of market-driven and policy-driven regulated costs, such as costs of electricity purchases, including from renewable sources, additional electricity generation costs in the Spanish islands and transport and distribution costs, etc., without the earmarking of specific revenues to certain costs. Regulated revenues never became the property of distributors, with the exception of the remuneration for pure distribution, which was retained by them after deduction of all other system costs.
- (100) Any deficit in the accounts such as the one that occurred in 2005, regardless of its causes, would therefore appear in the distributors' accounts, without them having any leeway to decide either on the level of regulated revenues and costs or on the financing of specific costs with specific revenues. Indeed, as is apparent from the figures cited in recital 28, the transport and distribution costs of the electricity system in 2005 stood at EUR 4 410 million, consistent with the same cost categories in 2004 and 2006 respectively. So the level of the distributors' costs bears no relation to the amount of the deficit in 2005.
- (101) Therefore, the classification of the 2005 deficit as 'distributors' losses' does not seem justified because the deficit is not imputable to action on the part of distributors, but rather to the regulatory provisions establishing the right of end-users to be supplied at regulated tariffs and, to a certain extent, to the regulatory and policy choices made to support electricity production from renewable sources and cogeneration, for instance. It follows that the financing of the deficit in the electricity system's accounts through the mechanisms described in recitals 29 to 32 is not a way to absorb the distributors' specific losses but rather the system's overall losses. Indeed, without the recognition of the EUR 3 811 million deficit in 2005 and its pre-financing by the five major electricity utilities, it would not have been possible to pay the system's transmission and distribution costs incurred for the benefit of all users, whether in the regulated or free market.
- (102) The formal investigation does not establish the existence of any other elements of advantage in favour of distributors. Distributors passed on the entire benefit of low regulated tariffs to end-users, did not make any profit on sales and did not draw any benefit from users returning to the regulated market. It follows that, from a financial perspective, the position of distributors in Spain was fully comparable with that of a system intermediary. In that respect, the recognition of the costs of supplying at regulated electricity tariffs under the Spanish electricity system in 2005 is, in its principle, no different from the compensation of the costs of purchase of electricity which the Commission has not classified as state aid within the meaning of Article 107(1) TFEU, both as regards electricity from certain sources (recital (90)) and wholesale electricity for supply at regulated tariffs (recital (91)).
- (103) Even though the opening decision does not target the vertically integrated entities to which distributors belong, with accounting and partial legal unbundling, with a view to addressing Centrica's representations, the Commission has also assessed whether such entities may have reaped indirect advantages liable to constitute state aid. Centrica notably submitted that integrated entities active in electricity retail sales in the free market (through a supply division) were able to avoid losses by encouraging users to

switch to their own distribution division. It also maintained that there was an incentive for a generator belonging to an integrated entity to keep wholesale prices high, considering that the distribution division of the integrated entity (selling at the regulated tariff) would be shielded from losses.

- (104) The Commission has not been able to establish the presence of an economic advantage arising from electricity users choosing distributors rather than suppliers. Economically, the switch from supply to distribution did not generate profits but merely avoided losses for the supply divisions of the four vertically integrated groups, Iberdrola, S.A., Unión Eléctrica Fenosa, S.A., Hidroeléctrica del Cantábrico S.A. and Endesa, S.A.; for its part, Elcogás operated only in the electricity generation sector. However, this cannot amount to an advantage for the other four companies in question, as the supply divisions could have avoided these losses in any event by simply terminating the supply contracts. For the supply divisions, therefore, the system did not entail an advantage but a penalty: they lost customers. The system was financially neutral for distributors too (for the reasons explained above). The generators, for their part, would have sold their electricity anyway on the wholesale market.
- (105) With regard to the generators' alleged incentive to keep wholesale prices high, it should be noted that, although the market environment created by the Spanish authorities might arguably have created an incentive for generators to raise prices, the tariffs per se did not lead to higher wholesale prices. Actually raising prices would have required complex strategies and anti-competitive behaviour on the part of generators. No direct and discernible direct causal link between the tariffs and a possible artificial increase in wholesale prices is established; it remains an unproven theoretical hypothesis.
- (106) The Commission has also considered the possibility that the system, by squeezing free-market competitors out of the electricity market, might have conferred an advantage on incumbent groups by increasing and 'remodelling' their market share so that it tended to coincide, broadly, with the size of each group's distribution network in the case of the four vertically integrated groups. This hypothetical advantage could not be established either, for the following reasons:
- First, it was not always possible to 'move customers around' within the same group. A customer served by Endesa's supply division in an area where the local distributor was Iberdrola could not switch to Endesa's distribution division, but only to Iberdrola's. Moreover, this switch to the regulated market resulted in a net cost to the integrated entities, since it increased the deficit that they had to finance on unfavourable terms.
 - Second, the groups did not make any profit on sales made by distributors. Therefore, the potential benefit stemming from a higher market share could not translate into profits in 2005 (the year covered by the investigation) but only in later years, when the free market was viable again. For this advantage to materialise, users served by a group's distributor would have had to switch back to the group's supply division. However, at that stage, a client contemplating a new change of supplier would have been free to select among all the suppliers active in the Spanish market. Therefore, the Commission has not established the presence of a concrete advantage linked to the mere

existence of a higher market share held by the groups in the period covered by the investigation.

- On the contrary, integrated groups were subjected to an objective penalty: the obligation to finance the deficit on terms which were non-remunerative, since the interest rate yielded by the collection rights was lower than an adequate market rate and, thus, the securitisation of the collection rights was carried out with a remuneration arguably lower than that obtained if a market rate had been applied.
- (107) On the basis of the foregoing, the Commission has concluded that, as far as supply to business users is concerned, the regulatory system put in place by Spain in 2005 did not confer an economic advantage, whether direct or indirect, either on distributors or on the integrated groups to which they belonged.
- (108) Finally, with regard to Centrica's allegation that the system discriminated between distributors and free-market suppliers, the Commission points out that discrimination may occur when persons who are in the same factual and legal position are treated differently or, vice versa, when the same treatment is applied to persons who are in a different factual and legal position.
- (109) First, the allegation is clearly without foundation in the case of Elcogás S.A., which was granted collection rights even though it did not operate in the distribution sector. Second, it has not been demonstrated that the other four designated companies, Iberdrola, S.A., Unión Eléctrica Fenosa, S.A., Hidroeléctrica del Cantábrico, S.A, and Endesa, S.A., were compensated because of their activity as distributors supplying electricity at regulated tariffs, as already pointed out in recital 30. Third, and in any event, in the Spanish electricity system, distributors and free-market suppliers were not in the same factual and legal position. The obligation of supplying electricity at regulated tariffs was carried out under regulatory constraints which made distributors act as mere financial and supply intermediaries that implemented legal provisions, whereas supply on free-market terms was a fully liberalised activity. Therefore, the difference in treatment contested by Centrica cannot amount to discrimination, notwithstanding the fact that the level of regulated tariffs may have been detrimental to the liberalisation process. However, this was not the consequence of the granting of unlawful state aid to distributors.

CONCLUSION

- (110) The doubts expressed by the Commission in its opening decision were allayed in the course of the formal investigation. The Commission is satisfied that the recognition by Spain of the costs borne by electricity distributors in respect of their activity of supplying electricity at regulated tariffs to medium-sized and large business users did not confer an economic advantage on distributors within the meaning of Article 107(1) TFEU.
- (111) Since the criteria set out in Article 107(1) TFEU are cumulative, there is no need to examine whether the remaining criteria are fulfilled. The Commission therefore concludes that the measure does not constitute state aid in favour of electricity distributors. This conclusion refers to the situation and period of time covered by the

complaint, and is without prejudice to the possibility of the Commission examining measures taken by Spain since 2005,

HAS ADOPTED THIS DECISION:

Article 1

The recognition by the Kingdom of Spain of the costs incurred by distributors in supplying electricity to medium-sized and large business end-users at regulated tariffs during 2005 in the form of the collection rights of Iberdrola, S.A., Unión Eléctrica Fenosa, S.A., Hidroeléctrica del Cantábrico, S.A., Endesa, S.A. and Elcogás, S.A. established in Royal Decree-Law 5/2005 does not constitute state aid within the meaning of Article 107(1) of the Treaty on the Functioning of the European Union.

Article 2

This Decision is addressed to the Kingdom of Spain.

Done at Brussels, 4 February 2014.

For the Commission

Joaquín ALMUNIA
Vice-President

Notice

If this Decision contains confidential information which should not be published, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to publication of the full text of the Decision. Your request specifying the relevant information should be sent by registered letter or fax to:

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