

Comments of the European Commission on a request for information from the European Ombudsman

- Complaint by ██████████ of CEE Bankwatch Network, ref. 327/2021/KR regarding the sustainability assessment of the gas projects on the List of Projects of Energy Community interest (PECIs) and Projects of Mutual Interest (PMIs), that was published on 14 January 2021

I. BACKGROUND/SUMMARY OF THE FACTS/HISTORY

Priority projects of Energy Community (PECIs) refers to infrastructure projects that comply with the general and specific criteria, as defined in the incorporated and adapted **Trans-European Networks for Energy (TEN-E) Regulation** (EU) 347/2013 on guidelines for trans-European energy infrastructure that was adopted in the Energy Community by a Decision of the Ministerial Council on 16 October 2015.

The purpose of this Regulation is to streamline the permitting procedure and facilitate investments in energy infrastructure, in order to achieve the Energy Community's energy and environment policy objectives. The Regulation also establishes rules for identifying projects of Energy Community significance, called Projects of Energy Community Interest (PECIs) and Projects of Mutual Interest (PMIs). The lists cover energy infrastructure (electricity, gas and oil) either connecting EnC Contracting Parties (for a PECE) or an EU Member State with a Contracting Party (for a PMI, or a PECE if the EU part of the project is a PECE). The projects can obtain the priority status, based on individual cost/benefit analysis.

The criteria applied for the assessment of Projects of Energy Community Interest (PECIs) are described in Article 4 and Annex III of the incorporated and adapted Regulation (EU) 347/2013 on guidelines for trans-European energy infrastructure adopted by the Energy Community on 16 October 2015.

Article 4(2) provides for specific criteria applying to PECIs in each category. In line with Article 4(2) (b) *“for gas projects falling under the energy infrastructure categories set out in Annex I.2, the project is to contribute significantly to at least one of the following specific criteria”: (i) market integration; (ii) security of supply; (iii) competition and (iv) sustainability* inter alia through reducing emissions, supporting intermittent renewable generation and enhancing deployment of renewable gas. In line with Article 4(3): *“For projects falling under the energy infrastructure categories set out in Annex I.1 to 3, the criteria listed in this Article shall be assessed in accordance with the indicators set out in Annex III.2 to 5.”*

According to Annex III(3)(d) sustainability for gas projects *“shall be measured as the contribution of a project to reduce emissions, to support the back-up of renewable electricity generation or power-to-gas and biogas transportation, taking into account expected changes in climatic conditions”*.

According to Article 4(6), *“project that directly crosses the border of one or more Contracting Parties and one or more Member States which is not granted a status of Project of Common Interest within the European Union may be developed on voluntary basis as a project of Mutual Interest”*.

The PECEI and PMI lists are adopted by the Energy Community's Ministerial Council. The Energy Community Ministerial Council is the highest decision-making body of Energy Community. The European Commission sits (on behalf of the EU) in the Ministerial Council together with one representative from each Contracting Party (Albania, Bosnia and Herzegovina, Georgia, the Republic of North Macedonia, Kosovo, Moldova, Montenegro, Serbia and Ukraine).

For the Ministerial Council decision to be taken, **a preliminary list of proposed PECEI and PMI projects is endorsed by the decision-making body of two Groups** (for gas and for electricity) established under the incorporated and adapted Regulation 347/2013. Annex II of the incorporated and adapted Regulation 34/2013 envisage that these Groups include representatives of the Contracting Parties and Member States concerned, the Commission, national regulatory authorities, TSOs, as well as the Energy Community Secretariat and upon invitation the ENTSO-E and ENTSO-G. **The proposal to the Ministerial Council is in practice presented by the Energy Community Secretariat.**

II. THE COMPLAINT TO THE EUROPEAN OMBUDSMAN

On 19 April 2021, the European Ombudsman sent to the Commission an inquiry linked to complaint 327/2021/KR from Mr Gligor Radevic of 'CEE Bankwatch Network'. The complaint regards the alleged failure to carry out a sustainability assessment of the gas projects on the lists of Projects of Energy Community interest (PECEIs) and Projects of Mutual Interest (PMIs) that were published on 14 January 2021.

The complaint is related to the Decision of the European Ombudsman in case 1991/2019/KR2 on the European Commission's action concerning the sustainability assessment for gas projects on the current list of the Projects of the Common Interest.

III. EUROPEAN OMBUDSMAN'S INQUIRY

The European Ombudsman's inquiry concerns the examination of the following two issues:

1. Can the Commission explain why the methodology used to assess the sustainability of the gas projects concerned was fit-for-purpose?

The process to prepare and adopt the 2020 lists of PECEI and PMI projects followed the applicable legislation and selection rules at that time. The selection process is described in Part I of this reply. The development and content of the methodology used in the 2020 selection process is explained in reply to question 2 in Part IV.

As regards the adequacy of the environmental assessment of projects included in the PECEI/PMI lists, it is to be noted that, **while being similar to the ENTSO-G assessment of projects in the EU, the Energy Community assessment differs in some aspects, as it is a dynamic market simulation.** The model identifies a supply/demand-based market equilibrium found via a market simulation based on a number of input data (among them a CO₂ price). This supply/demand-based market equilibrium is identified per country, for flows between countries, and per energy market (electricity and gas). This exercise is done to obtain a reference scenario and allows in a second step to identify socio-economic welfare changes, covering environmental aspects, for each project proposed.

Concerning the evaluation of the climate and sustainability impact of proposed projects, it needs to be stated that CO₂ emissions are priced in the model and the model allows for fuels substations. In cases where an increase of use of natural gas would result in decrease of more

emitting fuels such as coal or oil, the modelling shows the reduction of the emissions. The CO₂ emissions factors for fossil fuels used come from the United Nations Framework Convention on Climate Change (UNFCCC)¹. **It is also worth noting that the CO₂ price was set in the modelling exercise, while the region is not covered by a pricing system today, which means that the project assessment was stricter than the existing legal framework of the Energy Community Treaty. It is a forward-looking move that confirms the will to avoid stranded assets.** Moreover, the methodology used by the Energy Community also included a more progressive, green scenario and sensitivity analysis on the gas demand. Finally, to illustrate the complexity of this assessment, it is key to recall that in 2019, according to Eurostat data², the combined share of i) solid fossil fuels (mainly coal and lignite) and ii) oil in the total energy supply of the Energy Community Contracting Parties was about 50%, whereas the share of these two fuels in electricity and heat generation in the same year was 56%. Based on these fundamental characteristics of the energy sector, which are very dissimilar to those in the EU27³, in some cases in the Energy Community Contracting Parties, natural gas can contribute to significantly reducing CO₂ emissions and to improve local air quality by radically reducing pollutants, which have detrimental health effects. At the same time, the Commission fully agrees that a lock-in effect needs to be avoided and investment in new infrastructure, which might soon become stranded asset, has to be avoided, making it necessary to assess such investment on a case-by-case basis.

2. What does the Commission do within the Energy Community to advance the methodology it considers to be the right one?

It is important to emphasise that the selection of the PECIs and PMIs is based on a different methodology than the one used in the EU PCI selection procedure. The Energy Community Secretariat, in cooperation with the Commission, leads the preparation of the PEI/PMI assessment methodology and outsources specific tasks to external consultants.

As indicated above, the Commission was involved in the main stages of the methodology preparation and assessment for the 2020 PEI and PMI lists. **The role of the Commission was to transmit the experience gained in the PCI assessment within the EU and to provide guidance on the new policy orientation of the EU in order to establish right methodological basis for the 2020 lists, which would be oriented towards the European Green Deal as well as fit for the realities and the energy and climate objectives of the Energy Community Contracting Parties.** In this context, it should be emphasised that the Commission actively sought to incorporate various elements of sustainability, based on available and credible data, which could be used in measuring the projects' impact on decarbonisation and climate.

The Commission's engagement in the process of the methodology preparation led to the incorporation of joint scenarios of ENTSOs, in particular the National Trends scenario from the latest TYNDP 2020, which is in line with EU 2030 targets. Additionally, the Commission promoted the use of the EU's PRIMES EUCO 3223.5 scenario for the purpose of the development of the green scenario for the PEI/PMI assessment. This was done exactly with the purpose to align the input data with that of the European Union, complying

¹ https://unfccc.int/resource/docs/publications/09_resource_guide3.pdf

² <https://ec.europa.eu/eurostat/documents/38154/4956218/Energy-balance-sheets-February-2021-edition.zip/4b1d6665-f303-be7d-a7e5-1e0da16ec0d9?t=1612709565471>

³ In the EU, national energy mixes in most cases are not dominated by the fossil fuels: <https://ec.europa.eu/eurostat/cache/infographs/energy/bloc-2a.html>

with EU target setting. Moreover, **the Commission expressed its preference to use a carbon price in the methodology even if the Energy Community Contracting Parties, at the moment, are not legally required to use such a mechanism which disincentives the use of more polluting fuels.** The outcome of the Commission's engagement is elaborated in detail in Section IV below.

IV. THE COMMISSION'S COMMENTS TO THE COMPLAINANT'S ARGUMENTS

1. a. What was the Commission's contribution to the selection procedure for candidate gas projects for the Energy Community's list of projects of regional significance (comprising 'Projects of Energy Community Interest' (PECIs), between Energy Community 'contracting parties', and 'Projects of Mutual Interest' (PMIs), between contracting parties and EU member states):

- **as member of the Energy Community's Group for gas projects,**
- **as member (and in its capacity as Vice-President) of the Energy Community's Regulatory Board, and**
- **ahead of the proposal of the Energy Community Secretariat to the Ministerial Council on 14 January 2021, which was stated to have happened in agreement with the services of the Commission? At this stage, what exactly happened for the Commission to arrive at this agreement?**

From a procedural point of view, Regulation (EU) 347/2013 as adapted and adopted by the Energy Community, provides under Article 3 (4) that **a PECI list shall be established by the Ministerial Council every two years.**

The process to prepare and adopt the 2020 lists of PECI and PMI projects followed the applicable legislation and selection rules and criteria at that time. The Commission indeed participated in the selection process.

It must be stressed that the Energy Community follows the EU *acquis* with a time lag necessary for political endorsement and transposition and while the EU has already initiated the revision of the EU's TEN-E Regulation (EU) 347/2013 in December 2021, the legislation in force in the Energy Community, as well as in the EU, is still the 2013 Regulation and its provisions have been implemented by developing the 2020 lists. **Although the Regulation in force does not foresee provisions for this purpose, the change in the political context with the Green Deal agenda have been underscored for the Contracting Parties during the list development process by the European Commission and the Commission insisted on the need to avoid stranded assets and presented some natural gas projects in clusters as competing in order to clarify that not all of these projects will need to be realised.**⁴ As explained under point 1., the use of a CO₂ price in the modelling, although currently not applicable in the Energy Community countries, already ensured a forward-looking assessment of the candidate projects from a sustainability standpoint.

⁴“pointed to the potential impact of EU climate policies. Fossil projects need to demonstrate that they respond to specific goals of member states. TEN-E regulation is need to be streamlined to better fit the goals of the Green Deal. These developments are starting in the EU but the EnC CPs will follow suit in the coming years.”
https://www.energy-community.org/dam/jcr:b078f45c-8266-4035-97a9-214198421954/PECI_MoM_012020.pdf

It is also worth underlining that the **inclusion on the lists does not guarantee financial support from the EU nor from IFIs**. Receiving the PECEI status or the PMI label is only a facilitating factor for each project promotor to seek public and private financing. Various EU programmes and EU institutions have been involved in the past to finance *parts* of those projects within the framework of our financial support for the accession countries and for the neighbourhood countries. Most of the listed projects have been already on the previous lists, in a similar way to the EU PCI list.

In particular, the **PMIs remain outside of the framework of the Regulation 347/2013** as adapted and adopted in the Energy Community. Hence, this status, for instance of the IAP project, does not lead to material benefits. Moreover, the proposed new lists specify for some projects that they are in competition and not all of them would therefore bring value if all were constructed. Finally, **once the new legal and political framework is in place, new lists of PECEI and PMIs will be prepared in a different manner, taking into account new sustainability criterion, developed for the TEN-E/PCI process, to be used also for the PECEI/PMI selection.**

The European Union's position at the Energy Community's Ministerial Council is established by a Council decision and is represented by the European Commission at the meeting. The Union's position for the Ministerial Council of 17 December 2020 included an agreement to a Decision and a Recommendation regarding lists of priority infrastructure projects for the Energy Community Contracting Parties.

1. b. Did the Commission have other roles or tasks in the selection and adoption of the Energy Community's PECEIs and PMIs?

No.

2. Did the methodology for assessing sustainability of candidate gas PECEIs and PMIs take into account potential negative impacts, such as possible increases in greenhouse gasses from these projects were they to be implemented? If so, can the Commission describe this methodology and related data collection? If the methodology for assessing sustainability did not take into account potential negative impacts, why was this not the case?

The Energy Community Secretariat, leading this process, relied on input of external consultants for the preparation of the methodology. For the 2020 lists, the Energy Community Secretariat has contracted the consortium of REKK and DNV GL after an open tender to assist the Energy Community and its Secretariat in the assessment of candidate priority projects in electricity, gas and oil infrastructure, and in smart grids development, in line with the EU Regulation 347/2013 as adopted by the Ministerial Council for the Energy Community. For the assessment of candidate projects the Consortium developed an assessment methodology, building on previous assessments of infrastructure projects by the same Consortium on behalf of the Energy Community in 2013, 2016 and 2018, as well as taking into account the methodology applied for the latest selection of EU Projects of Common Interest (PCIs) under the same Regulation as well as the methodologies for the assessment of network infrastructure projects developed by ENTSO-E and ENTSG.

Therefore, a specific methodology is prepared for the Energy Community. Specific circumstances have to be taken into account when carrying out the PECEI and PMI selection process. For example, no top-down consistent modelling exists for the region that could provide input for the scenarios. As Input Data, ENTSGs jointly developed scenarios were

used, particularly the National Trends scenario from the latest TYNDP 2020, which is in line with EU 2030 targets. Additionally the EU's PRIMES EUCO 3223.5 scenario was used when developing the green scenario for the PECI/PMI assessment. This was done exactly with the purpose to align the input data with that of the European Union, complying with EU target setting. Moreover, a carbon price was used in the methodology although Energy Community Contracting Parties do not yet apply it. Please see point 1. for further details.

3. In reply to the complainant, representatives of the Commission described the methodology for assessing the contribution to sustainability of candidate gas PECIs and PMIs as being very similar to the methodology used for candidate gas projects for the 4th PCI-list. In reply to the Ombudsman, the Commission, on 11 June 2020, said that the methodology for assessing the sustainability of candidate gas PCIs lacked “reliable, accurate and consistent project specific data” and “did not allow for a non-discriminative assessment of that criterion for all candidate projects”. Did the Commission, at any point during the selection process of PECIs and PMIs, express its concerns as regards using a methodology that was similar?

The Commission has expressed the importance of the assessment of the sustainability impact as explained earlier under points 1. (CO₂ price) and 2. (Green scenario).

It must be also stressed that the selection of the PECIs and PMIs is based on a separate methodology. Therefore, the methodology is not the same as used in the EU PCI selection procedure.

4. One of the Energy Community's aims is to improve the environmental situation in relation with energy supply in the region and foster the use of renewable energy and energy efficiency. Could the Commission elaborate on how the list of projects of regional significance supports that objective?

The objectives of the Energy Community in relation to creating an integrated energy market, improving the environmental situation in relation to gas and electricity, related to energy efficiency and renewable energy have been implemented via regulatory approximation with the EU and **have been continuously supported by the Commission via a number of projects and programmes**, including financial assistance, dedicated to the development of renewable energy and energy efficiency in the region, as well as better interconnections of markets, improving business conditions for such investments.

The specific situation of the Contracting Parties must be taken adequately into account when evaluating the need for specific infrastructure projects and a **case-by-case approach should be followed to each project** in order to identify the most optimal way forward to achieve clean energy supply and avoid inefficient investments. Regarding the energy mix, solid fossil fuels still dominate in the Energy Community and in certain cases a coal-to-gas switch could bring important reductions in emissions and improvements in air quality while investing in parallel in RES and energy efficiency measures and delivering diversification benefits. Such switch would at the same time provide flexibility to the electricity grid that can help to integrate variable generation capacities. Moreover, it is important to further assess the potential to decrease the carbon-intensity of the gas in the network (bio-gas; syngas; H₂ blending) in the long-term.

The Commission's commitment to assist the Western Balkans to transition to a sustainable and climate neutral economy is implemented by initiatives such as the **Green Agenda for the Western Balkans and the Communication on comprehensive Economic and Investment**

Plan for the Western Balkans, adopted on 6 October 2020, in which it is embedded, aiming at long-term economic recovery and a twin green and digital transition, regional integration and convergence with the EU. The proposed Green Agenda has a focus on investing in clean energy as an underpinning principle but it also emphasises the role of gas as a bridging fuel during the transition away from coal as well as a source of diversification via LNG from the EU. Importantly, it specifies that any new pipeline must fully respect EU rules and demonstrate its long-term viability and gives due space to the decarbonisation agenda and means, such as renewable power, energy efficiency, low carbon/green gases. It warns against fossil fuels lock-in and stranded assets.

All these considerations must be understood in the context that the **inclusion on the PECCI and PMI lists does not mean financial support from the EU nor from IFIs and no specific amount is set aside in the Economic and Investment Plan for gas infrastructure projects.**

Efforts by the European Union on decarbonisation of the Contracting Parties are well advancing. In the context of the accession process and their membership to the Energy Community, the WB are anticipated to join the EU ETS in due course (modalities and timing remain to be defined together with DG CLIMA). The Commission is running a study on 2030 energy and climate targets for the region, while the Energy Community Secretariat has finalised one on carbon pricing. **These efforts might facilitate and contribute to setting a clear and reliable policy framework that, if included pricing carbon emissions, would allow for identifying gas related projects that are future-proof and fit for a decarbonised economy.** In the Commission's view, having a similar carbon price in the EU and in the WB would keep a level playing field in the context of further electricity market integration.

5. Could the Commission provide an update as regards its efforts to improve the sustainability criterion so that it takes into account greenhouse gas emissions and efficiency impacts, which the Commission indicated in case 1991/2019/KR it was planning to have in place ahead of the assessment of candidate gas projects for the 5th PCI list?

Article 4 (paragraph 2) of the current TEN-E Regulation sets out a number of criteria to assess projects of common interest in the field of gas. Sustainability is one of them along with security of supply, market integration and competition. The Commission is making every effort within the current TEN-E legal framework to prioritise projects that meet sustainability when selecting projects for the 5th PCI list. Since the adoption of the Green Deal and increasing the climate targets for 2030 and 2050, the Commission has decided to strengthen the role of sustainability when drawing up the upcoming 5th PCI list (within the limits of current legislation).

DG Energy commissioned a study to develop a more precise indicator for measuring the sustainability impact of gas infrastructure projects⁵. As a result, the Commission presented a new methodology for projects selection, which is being used during the ongoing 5th PCI selection process to ensure that the sustainability of all projects is assessed and taken into account. All gas candidate projects have been subject to this assessment.

Under the new approach:

⁵ <https://op.europa.eu/en/publication-detail/-/publication/364d69a4-1744-11eb-b57e-01aa75ed71a1/language-en>

- The new proposed methodology allows for either a positive or negative net impact on CO2 emissions. A project can show positive CO2 savings when gas replaces coal or oil. However, if the gas project leads to a higher consumption of natural gas not compensated by phasing out more polluting sources, it will result in negative savings. This will be reflected in its overall assessment.
- The Commission proposes a more accurate method for the allocation of CO2 savings (if there are any) to individual gas projects. The allocation is based on actual gas flows and infrastructure use. The method prioritises the use of already existing infrastructure over the new assets. If the increased gas demand can be met by existing infrastructure, the project in question shows no sustainability benefit.
- The sustainability indicator focuses on CO2 impact but it also includes an assessment of a project's impact on air quality (i.e. non-GHG emissions, such as NOx, SOx and particulate matter).

The Commission has worked very closely with all stakeholders in the process, including ENTSOG, ACER, and the TEN-E Regional Group members, to deliver a sound outcome and align the process with our Green Deal objectives.

The PCI assessment methodology has been discussed with stakeholders and validated by the TEN-E regional groups, the meetings of which are open to the public.

It is also recalled that the Commission has proposed not to include natural gas infrastructure projects under the future TEN-E Regulation. Moreover, the Commission has made the sustainability check mandatory, meaning that no project would be eligible for PCI status unless it can prove a significant contribution to this criterion.

Against this background, for the next PEGI/PMI process the Commission will seek to actively steer the discussion already at the preparatory phase in order to effectively implement new sustainability indicator and to better reflect challenges of decarbonisation.

V. CONCLUSION

The Commission is of the opinion that the sustainability assessment of all gas projects on the lists of Projects of Energy Community interest (PEGIs) and Projects of Mutual Interest (PMIs), that were published on 14 January 2021, has been carried out appropriately and in full respect of the Energy Community Treaty and was based on the “fit for purpose” principle, taking into account the regional specificities, like the existing energy mix.

*For the Commission
Kadri SIMSON
Member of the Commission*