EFET European Federation of Energy Traders

EFET Legal Committee Meeting
14 December 2023, Dusseldorf

DAY 1: MEETING AGENDA

1. Opening and introduction to agenda; approval of the A&D list from the previous Legal Committee meeting held in London (21 & 22 September 2023) – Michaela Duve, EFET
2. Board highlights and governance framework review:
   - Report from the new board and update on the EFET initiatives – Giusi Squicciarini, Shell Energy Europe
   - Discussion on the revised Terms of Reference of the Legal Committee – Michaela Duve, EFET
   - EFET new website – Our aim: where style meets convenience – Aygul Adamson, EFET
3. The German Control and Profit Transfer Agreement as a collateral (in the light of the BMP Greengas case) – Michael Cieslarczyk & Florian Bruder, DLA Piper
4. Potential categorisation of the CBAM fee as tax within the meaning of the definition "Tax" or "Other Tax" in the EFET General Agreements – Brett Hillis, Reed Smith and Michael Cieslarczyk, DLA Piper
5. Update on REMIT II - practical take and potential implementation challenges, STOR obligation vs self-incrimination – Marek Dal-Canton, Chair of Trading Compliance WG and Katharina Lüken, Co-Chair of Trading Compliance WG

1. Welcome and introduction, approval of the A&D list

Opening by Michaela Duve, EFET

2. Report from the new board and update on the EFET initiatives

Report by Giusi Squicciarini, Shell Energy Europe, new Chair of the EFET Board

3. Discussion on the revised Terms of Reference of the Legal Committee

Presentation by Michaela Duve, EFET

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What are the Terms of Reference?

- Formal document that outlines the scope, objectives, and responsibilities of committee;
- Providing a clear guide for individuals involved in the endeavour;
- Establishes a common understanding and framework for effective planning and execution.

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Specific matters:

No. of emails per member

Suggestion: two (2) per LC member on the general mailing list;

Revision period for ToR

Suggestion: every year to keep them updated;

No. meetings per year

Suggestion: four (4) per calendar year.

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Specific matters - Expression of interest

- Suggestion: annual survey, personal/hybrid member meetings;
- Determination of priorities focus of Working Groups for the year;
- Determination of initial budget allocation to Working Groups by Secretariat.

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Specific matters – Chair:

Election (Chair)

Suggestion: Every two years / every year during q3 meeting;

Expression of interest

S: Recommendation by member, suggestion by EFET Secretariat, own initiative;

Timeline

Suggestion: 4 weeks prior to q3 meeting.

Specific matters – Chair (2):

Vote of no confidence

Suggestion: Expression by [10]% of members;

Minimum participation

Suggestion: [30-40] % + simple majority for adoption;

Vice-Chair

Suggestion: follow the rules for the Chair.

Specific matters – Voting procedures

Endorsement

Develop joint understanding;

Minimum participation

To take decisions, endorse documents, difference vote during LC [30-40]% vs. electronic voting;

Handling of votes

Simple majority, Handling of abstains.

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Permanent Legal Advisors

- Appointment for two (2) year period;
- Possibility for members to request replacement;
- Advisor wishes to resign, advisor changes affiliation with law firm.

We need your input!

Deadline for comments: 19.01.2024

4. EFET new website – Our aim: where style meets convenience

Presentation by Aygul Adamson, EFET

EFET

Progress Report

- Our current website is undergoing a total overhaul (consistent with Board's priorities to raise our public profile – European elections, EFET's 25th anniversary, rebranding).
- Work to replace the existing set-up is on track steered by EFET management team. Contracted supplier is making good progress, with a view to re-launch in 2024.
- New features: more intuitive, user-friendly website reflecting work structures and current practices; more effective data storage system and member management; searchability.
- Special focus on GDPR aspects and IT security, re-organisation of legal opinions per countries, building an archive, linking up public section and members' intranet, updating EDRS platform.

5. The German Control and Profit Transfer Agreement as a collateral (in the light of the BMP Greengas case)

Presentation by Michael Cieslarczyk & Florian Bruder, DLA Piper

German CPTAs as credit support under EFET General Agreements

Michael Cieslarczyk, Partner

Florian Bruder, Partner

DLA PIPER

CPTAs under German law

Overview

- Control (domination) and/or profit transfer agreements (sec. 291 ff. AktG)
  - Typically, between affiliated companies, not necessarily between direct affiliates
  - Controlling company may be situated outside Germany

- Characteristics:
  - Control: Binding instructions / so-called contract-based group of companies (‘*Vertragskonzern*’)
  - Profit: Transfer of entire balance sheet profit
  - Consequences: Controlling company
    - to compensate losses of the controlled company (sec. 302 AktG)
    - to provide collateral to creditors following the terminaton of the CPTA (sec. 303 AktG)

CPTAs under German law

Letter of Awareness (LoA)

- Controlling companies in many cases provide additional statements to creditors of the controlled company (so-called LoA)
- Primary purpose is to inform the business partners of a controlled company that
  - the controlling company is aware of the trading relationship of the controlled company with the counterparty
  - a CPTA is in place and
  - the controlling company will adhere to any legal duties from the CPTA
- Besides, the LoA typically stipulates certain additional/modified notification obligations (and sometimes provides statements in which form credit support would be provided in case of an obligation under § 303 AktG)
- LoA is largely declaratory in nature, while it modifies or supplements the statutory rights under the CPTA and/or sec. 303 AktG

⇒ No security: No guarantee or hard comfort letter (*harte Patronatserklärung*)

CPTAs under German law

Termination of a CPTA

- Cancellation at the end of a financial year (sec. 296 AktG)
- No statutory ordinary termination; only if provided for in the CPTA
- Termination for good cause without notice period (sec. 297 AktG)
  - Good cause if the other party is unlikely to be able to fulfill its obligation under the CPTA
  - Primarily relates to obligations of the controlling company; termination by the controlling company is disputed in legal literature
  - Deterioration of the controlled company's economic situation does not generally constitute good cause. Exception according to the prevailing opinion: if reasons are due to the general economic situation, and if the controlling company's existence is threatened due to the CPTA

CPTAs under German law

No protection against insolvency of the controlled company

- A CPTA does per se not guarantee to prevent the insolvency of the controlled company – unless otherwise agreed explicitly
  - The controlling company has to compensate any balance sheet net losses
  - Such claim becomes due on the reporting date of the annual balance sheet of the controlled company

  ⇒ (Advance) compensation claims during the financial year unclear

- Recent decision of Higher Regional Court (OLG) Düsseldorf, decision of 10 October 2022 - 26 W 5/22:
  - There cannot be a threat to the existence of the controlled company while a CPTA exists, at least if the controlling company is solvent
  - "*… an advance payment to avert insolvency may therefore be necessary even before the end of the accounting period if its solvency or creditworthiness is seriously threatened…*"

  ⇒ Suggests a claim for advance payments during the financial year but in context of interim injunction to continue to deliver gas and argumentation not conclusive

  ⇒ (Imminent) illiquidity (sec. 17 and 18 InsO) and positive going concern prognosis to avoid over-indebtedness (sec. 19 InsO) are liquidity driven

CPTAs under German law

Insolvency of the controlled company

- The effects of insolvency on a CPTA are disputed in legal literature and have not been clarified by the German Federal Court of Justice (BGH)
- Ordinary insolvency proceedings:
  - According to the prevailing opinion, a CPTA terminates automatically upon the opening of insolvency proceedings
  - Claim for compensation of losses incurred up to the date of the opening of insolvency proceedings by controlled party will be pursued by the insolvency administrator
- Debtor-in-possession insolvency proceedings:
  - Strong opinion in legal literature: CPTA is automatically suspended for the duration of the insolvency proceedings
  - Effects of suspension unclear; seems reasonable to assume that also claim to compensation for the losses incurred up to the opening of the insolvency proceedings

CPTAs under German law

Claim for security (and payment) pursuant to § 303 AktG

- Within six month after a termination of the CPTA, creditors can demand security for their claims that came into existence established before the termination
- The claim for security is converted into a claim for payment (according to legal literature)
  - Once (i) claim of the creditor is finally established and (ii) the insolvency proceeding opened (disputed), rejected / discontinued for insufficiency of the estate or the company deleted from the commercial register
  - Some uncertainty as to the legal grounds: The creditor must not first turn to the controlling company and seek satisfaction by way of seizure of the claim of loss compensation based on good faith and fair dealing pursuant to sec. 242 of the German Civil Code
  - Some argue that the claim may only be pursued by the administrator
- In debtor-in-possession proceeding (*Eigenverwaltung*): Application in analogy in case of suspension of the CPTA (according to arguably prevailing opinion)
- Claim only against the controlling company who is party to the CPTA, not against group or ultimate shareholder; principle of limited liability of cooperations
- Valuable claim: Risk of insolvency of controlling company and risk of insolvency in “chain of CPTAs”

CPTAs under German law

Specific issues in the bmp greengas case

- Background:
  - Protective shield proceedings (*Schutzschirmverfahren*) / debtor-in-possession insolvency proceedings (*Eigenverwaltung*) were opened on 1 August 2023; insolvency plan was approved by majority creditors on 12 December 2023
  - Sole shareholder Erdgas Südwest GmbH (ESW) terminated CPTA on 1 August 2023
  - According to publicly available information: Confidential StaRUG proceedings regarding ESW were initiated in which the cash pool with EnBW group was terminated
- Debtor-in-possession proceedings: Due to termination of CPTA discussion on suspension avoided
- Claim for security and payment: Various objections raised by ESW in relation to statutory claim, e.g.
  - Quantification of potential claim for scope of security
  - No interest for security; discretion of ESW regarding type of security
  - Converted claim for payment may only be pursued by the administrator
- No “chain of CPTAs” and ESW subject to StaRUG proceedings

Potential effects on the EFET General Agreements

Summary of principles under German law – termination on the basis of statutory law

- EFET General Agreement: In case of insolvency proceedings in Germany, the transactions will be terminated on the basis of statutory rules, namely section 104 of the German Insolvency Code (provided transactions are in scope of section 104 of the German Insolvency Code)
- Statutory netting and resulting compensation is to be paid by the relevant party (reliance of Termination Amount provisions in the EFET General Agreement to be further analyzed but not in scope here)
- A potential claim against the insolvent party is an insolvency claim and subject to the pro-rata payments in the insolvency
- A CPTA can mitigate the risks arising from this position: right to claim collateral or even claim for payment against the controlling party; requires that the controlling party is solvent
- A LoA usually only provides for certain information and potentially undertakings in relation to reporting duties (or the kind of security to be provided).
- Where a parent company guarantee (PCG) is provided, the counterparty has a direct claim, often against the ultimate parent company; PCG is intended to provide direct credit support.

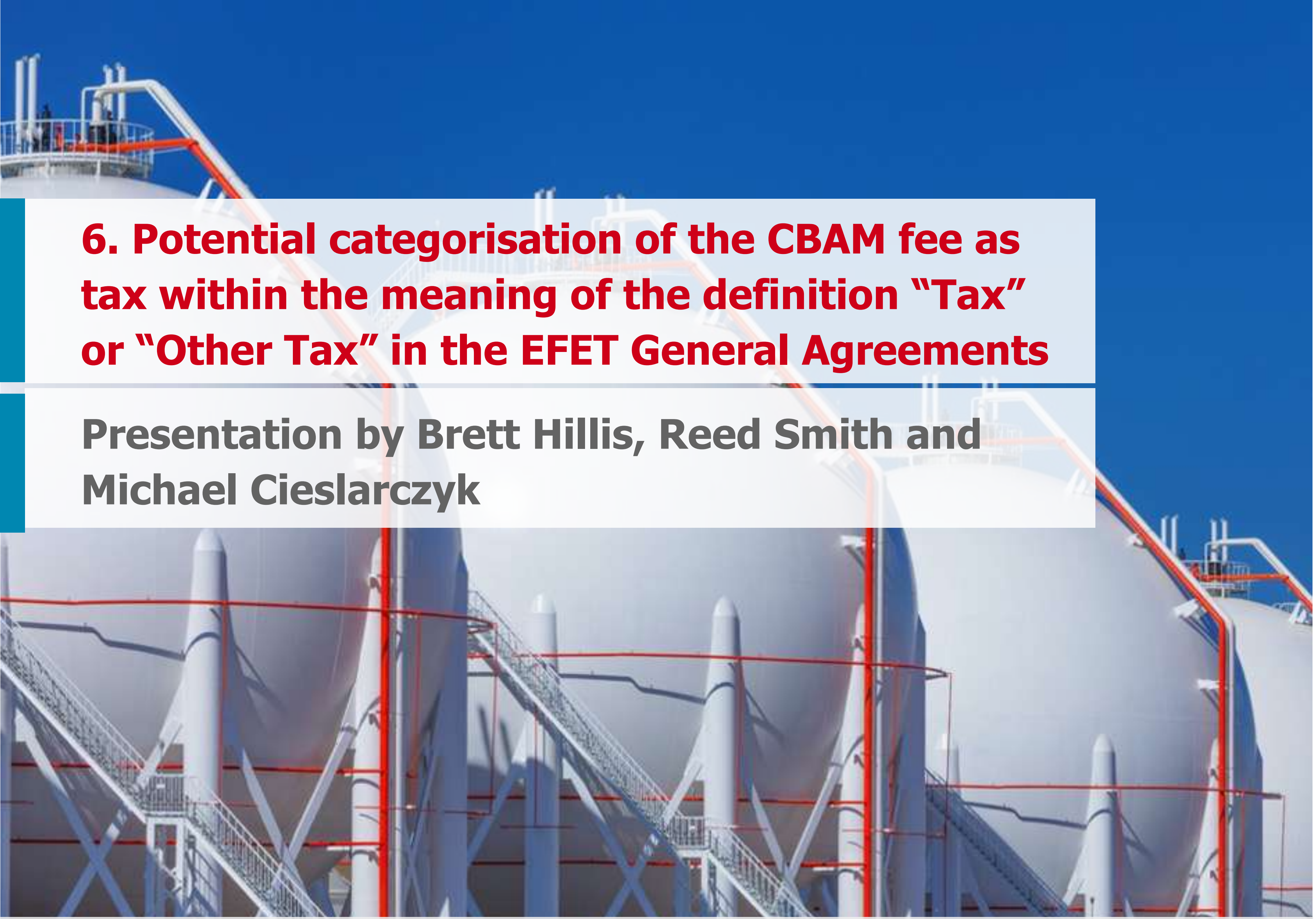
Potential effects on the EFET General Agreements

CPTA Automatic Termination (§ 10.4) + MAC (§ 17.2 (g) + LoA	CPTA No Automatic Termination (§ 10.4) + MAC (§ 17.2 (g) + LoA	PCG Automatic Termination (§ 10.4)	PCG No Automatic Termination (§ 10.4)
• Contract is automatically terminated (§§ 10.4, 10.5)	• Contract terminates based on statutory law, sec. 104 InsO	• Contract is automatically terminated (§§ 10.4, 10.5)	• Contract terminates based on statutory law, sec. 104 InsO
• Termination Amount (§ 11)		• Termination Amount (§ 11)	
• Payment obligation due to close out netting is insolvency claim	• Payment obligation due to close out netting is insolvency claim	• Payment obligation due to close out netting is insolvency claim	• Payment obligation due to close out netting is insolvency claim
• Claim under CPTA for security and payment (303 AktG)	• Claim under CPTA for security and payment (303 AktG)	• Counterparty can claim the Termination Amount from the Credit Support Provider (which might e.g. be the ultimate parent)	• Counterparty can claim the Termination Amount from the Credit Support Provider (which might e.g. be the ultimate parent).
• Performance Assurance: § 17.2 (g) seems to be unenforceable if CPTA is terminated as of the insolvency of the counterparty	• Performance Assurance: § 17.2 (g) seems to be unenforceable if CPTA is terminated as of the insolvency of the counterparty		

Potential effects on the EFET General Agreements

CPTA	Parent Company Guarantee
• Can mitigate the risk of loss in an insolvency as it results in a claim for security or payment against the controlling company • Enforcement might be more burdensome compared to PCG • Value depends on the solvency of the specific (former) controlling company • It is not possible to demand payments from other companies of the same corporate group as the controlling company • Not a formal security; no individual advantage • Less flexible	• Can mitigate the risk of loss in an insolvency as it results in a claim against the guaranteeing company • Value depends on the solvency of the guaranteeing company • The creditor of the guarantor may claim direct payment (potentially even) before insolvency proceedings have been opened • It is in principle possible to obtain guarantees from various companies • Formal security; can be an individual advantage • More flexible

Thank you



6. Potential categorisation of the CBAM fee as tax within the meaning of the definition “Tax” or “Other Tax” in the EFET General Agreements

Presentation by Brett Hillis, Reed Smith and Michael Cieslarczyk

Responses to English law questions on the CBAM and Tax provisions under the EFET Power

Brett Hillis | December 2023
Prepared for the EFET Legal Committee

Driving progress through partnership

1

Overview of the CBAM

English law approach to findings of foreign law

- We have set out our understanding of how the EU's Carbon Border Adjustment Mechanism ("**CBAM**") would operate.
- However, we note that, in general, the English courts will treat foreign law as a question of fact, which must be pleaded and proved.
- Proof of foreign law is commonly by way of expert evidence. The role of an expert on foreign law is to assist the court in determining the content of foreign law, but not to opine on its application to the case.
- The court is then entitled to evaluate and apply such cases or statutes according to its own learning and judgment, as guided by the submissions of the parties.

Overview of the CBAM

- The CBAM is one of the key components in the European Commission's 'Fit for 55' legislative package.
- Regulation (EU) 2023/956 of the European Parliament and of the Council of 10 May 2023 establishing a carbon border adjustment mechanism (the "**CBAM Regulation**") was formally adopted in April 2023.
- The CBAM aims to prevent 'carbon leakage' by subjecting the import of certain products from third countries (i.e. non-EU and non-EFTA countries) into the EU to a carbon levy linked to the carbon price payable under the EU Emissions Trading System ("**EU ETS**").
- The CBAM currently covers the following goods and selected precursors: (i) cement, (ii) iron and steel, (iii) aluminium, (iv) fertiliser, (v) hydrogen and (vi) electricity ("**CBAM Goods**").
- The scope of the CBAM may be extended to include other goods at risk of carbon leakage in the future.

Overview of the CBAM

Transitional phase: 1 October 2023 - 31 December 2025

- Intended to serve as a pilot and learning period for all stakeholders
- EU importers of CBAM Goods are required to submit quarterly CBAM reports to EU Member States' competent authorities in accordance with the reporting requirements and methodology in Commission Implementing Regulation (EU) 2023/1773 (the "**CBAM Implementing Regulation**").
- Quarterly reports must disclose: (i) the quantity of imported CBAM Goods; (ii) the embedded emissions in those goods; and (iii) if applicable, the carbon price paid in the country of origin for the embedded emissions.
- N.B. EU importers of CBAM Goods are not required to make any financial payments or adjustments by way of purchasing CBAM certificates during the transitional period.

Overview of the CBAM

Definitive phase: 1 January 2026 onwards

- EU importers of CBAM Goods will be required to:
  - obtain an authorisation in order to import CBAM Goods (i.e. become an "authorised CBAM declarant");
  - submit an annual declaration to the CBAM registry specifying the quantity of CBAM goods imported into the EU in the preceding year and their embedded greenhouse gas emissions, and a copy of a verification report issued by an accredited verifier; and
  - purchase and surrender CBAM certificates corresponding to the total embedded GHG emissions for any CBAM Goods it has imported over the preceding year (the **"CBAM Obligation**")**.**

Overview of the CBAM

Definitive phase: 1 January 2026 onwards

- A CBAM certificate is “a certificate in electronic format corresponding to one tonne of CO_2e of embedded emissions in goods”.
- The price of a CBAM certificate will be calculated based on the average of the closing prices of EU ETS allowances on the auction platform for each calendar week. For those calendar weeks in which no auctions are scheduled on the auction platform, the price of CBAM certificates shall be the average of the closing prices of EU ETS allowances of the last week in which auctions on the auction platform took place.
- The requirement to purchase CBAM certificates is triggered by the act of importing a CBAM Good into the EU’s customs territory.

Legal challenge to the CBAM

- Poland has filed a request to annul the CBAM Regulation in its entirety with the General Court of the Court of Justice of the European Union.
- Poland’s main argument is that the CBAM provisions are primarily fiscal in nature and therefore require a unanimous vote from all Council members (i.e., all 27 EU Member States) to pass.
- The CBAM Regulation was adopted by the Council and the European Parliament as an environmental measure. This is a different procedure and only required a qualified majority vote to pass.
- Poland’s legal challenge will not lead to an immediate suspension of the CBAM Regulation.
- If the action for annulment is successful, the CBAM Regulation can be annulled in full or in part from the moment of its adoption.

2

Legal analysis under English law

General principles of interpretation under English law

- Under the ‘onshored’ Rome I Regulation, parties have freedom to choose the governing law of an agreement.
- Where English law is the governing law of an agreement, the interpretation will be a matter for English law.
- No conflict of law principle that would require English courts to apply foreign law.
- The question of whether the CBAM Obligation would be considered a “Tax” or “Other Tax” under the EFET Power is therefore a question of English contractual interpretation.

General principles of interpretation under English law

- English courts' approach to interpretation of EFET agreements:
  - No English case law on interpretation of the Tax provisions, or the EFET Power more generally. However, parallels can be drawn from cases on other standard form contracts such as the ISDA Master Agreements.
  - The EFET Power will likely be interpreted in a way that achieves objectives of clarity, certainty and predictability.
  - Focus is on factual background known to the industry or the market, and not the background known to individual parties to an agreement.
  - Primary focus in construction is the words used, which are assumed to have been selected after considerable thought.
  - Care should be taken not to adopt an overly restrictive or narrow construction.

Would the CBAM Obligation be considered a "Tax" under the EFET Power?

"Tax" is defined in the EFET Power as:

"… any present or **future tax, levy, impost, duty, charge, assessment royalty, tariff or fee of any nature (including interest, penalties and additions thereto)** that is **imposed by any government or other taxing authority** (whether or not for its benefit) **in respect of any payment, nomination and allocation under any Individual Contract or under this Agreement**, and "Taxes" shall be construed accordingly. For the avoidance of doubt, Tax shall **exclude; (i) any tax on net income or wealth; (ii) a stamp, registration, documentation or similar tax; and (iii) VAT**;" (emphasis added)

Would the CBAM Obligation be considered a “Tax” under the EFET Power?

There are four limbs in the definition of “Tax”:

1. It is not: (i) income or wealth tax, (ii) stamp, registration or documentation tax (or a similar tax), or (iii) VAT
2. It is a tax, levy, impost, duty, charge, assessment royalty, tariff or fee of any nature (including interest, penalties and additions thereto)
3. It is imposed by any government or other taxing authority (whether or not for its benefit)
4. It is a tax in respect of any payment, nomination and allocation under any Individual Contract or under the EFET Power.

Would the CBAM Obligation be considered a "Tax" under the EFET Power?

Limb (1): It is not: (i) income or wealth tax, (ii) stamp, registration or documentation tax (or a similar tax), or (iii) VAT

- **The CBAM Obligation would not meet this limb of the definition.**
- It is not a tax on income or wealth, or a stamp, registration or documentation tax.
- It is not VAT, which is defined in the EFET Power as "*any value added tax or any tax analogous thereto but excluding any statutory late payment interest or penalties*".
  - Under an English law-governed EFET Power, this would cover the UK VAT tax regime, which is primarily governed by the Value Added Tax Act 1994, and any other analogous taxes whether levied inside or outside the UK.

Would the CBAM Obligation be considered a "Tax" under the EFET Power?

Limb (2): It is a tax, levy, impost, duty, charge, assessment royalty, tariff or fee of any nature (including interest, penalties and additions thereto)

- **It is not clear whether the CBAM Obligation would meet this limb of the definition.**
- English law definitions of legal terms:
  - "Tax": an "impost; a tribute imposed on the subject; an excise; tallage". Can be classified into direct and indirect taxes, and generally intended to be given to the Crown. "Duty" and "levy" have the same meaning as "tax".
  - "Tariff": a table or catalogue of rates with duties or customs to be paid on goods, as settled by authority or agreed on between several states.
  - "Assessment": periodical payments of a nature similar to rates and taxes.
  - "Royalty": royalty in respect of enjoyment or exercise of rights that constitute an intangible fixed asset.

Would the CBAM Obligation be considered a “Tax” under the EFET Power?

Limb (2): It is a tax, levy, impost, duty, charge, assessment royalty, tariff or fee of any nature (including interest, penalties and additions thereto)

- Certain features of the CBAM suggest it functions in a similar way to a tax:
  - Border adjustment element - the CBAM is triggered in a similar way to customs duties and import VAT.
  - CBAM revenues will be an EU “own resource” and are collected in a similar way to existing taxes (customs duties) in the EU.
- However, other features of the CBAM suggest it is not a tax:
  - It is not expressed to be a tax under EU law (although this is subject to legal challenge).
  - Prices payable under the CBAM are not calculated in the same way as a tax.
    - The CBAM Regulation creates an obligation on importers to purchase and surrender CBAM certificates based on the embedded emission intensity of products imported into the EU.
    - The price of CBAM certificates reference the weekly auction price of EU ETS allowances, which will fluctuate.

Would the CBAM Obligation be considered a “Tax” under the EFET Power?

Limb (3): It is imposed by any government or other taxing authority (whether or not for its benefit)

- **The CBAM would meet this limb of the definition.**
- It was proposed by the European Commission’s Directorate-General for Taxation and Customs Union, which is responsible for developing and carrying out the European Commission’s policies on customs and taxation.
- The CBAM Regulation is directly applicable in all EU Member States.

Would the CBAM Obligation be considered a “Tax” under the EFET Power?

Limb (4): It is a tax in respect of any payment, nomination and allocation under any Individual Contract or under the EFET Power.

- **The CBAM Obligation would not meet this limb of the definition.**
- The relevant tax must be in respect of any “payment, nomination and allocation” under any Individual Contract or under the EFET Power.
  - Query whether intention was to require tax to be in respect of all three actions (i.e. payment, nomination **and** allocation), or any one of the three actions (i.e. payment, nomination **or** allocation).
  - In any case, the tax must relate to a Party’s actions to deliver or accept electricity, or pay for such electricity under § 4 of the EFET Power, where the terms “pay” and “nominating” are used.

Would the CBAM Obligation be considered a “Tax” under the EFET Power?

Limb (4): It is a tax in respect of any payment, nomination and allocation under any Individual Contract or under the EFET Power.

- In some circumstances, nomination or allocation under an Individual Contract may be closely linked to when electricity is considered imported into the EU, and a court may adopt a broad interpretation on this basis, and conclude that the CBAM Obligation is imposed “in respect of” the nomination of power.
- However, such interpretation may face certain practical challenges, including:
  - whether it is possible in practice to identify whether, and to what extent, a particular nomination relates to power imported from the EU;
  - issues relating to net and gross nominations in relation to two-way cross-border flows.
- Based on our understanding of how the CBAM operates, we think the better view is that, even if the CBAM Obligation functions similarly to a tax or tariff, it would not be a “Tax” as it would not be regarded as being imposed “*in respect of*” payment, nomination or allocation of power.

Would the CBAM Obligation be considered a "Tax" under the EFET Power?

Conclusion

- We are of the view that the CBAM would <u>not</u> be a "Tax" under the EFET Power.
- Even if the CBAM Obligation functions in a similar way to a tax or tariff, it is not a measure that is imposed "*in respect of payment, nomination and allocation under any Individual Contract or under the EFET Power*", and therefore does not meet all the limbs of the definition of "Tax" under the EFET Power.

Would the CBAM Obligation be considered an “Other Tax” under the EFET Power?

- “**Other Tax**” is defined as “… any energy Tax or excise duty but not including Taxes targeted at end users;”
- “Other Tax” is a sub-set of “Tax” that specifically relates to energy, but which is not targeted at end users. Taxes targeted at end-users are dealt with in § 14(4)-(6) of the EFET Power.
- If the CBAM Obligation is not a “Tax”, then it is also unlikely to be an “Other Tax”.

Note on CBAM and the EFET Gas

- **The CBAM would not be a “Tax” or “Other Tax” under the EFET Gas.**
- Natural gas is not currently within the scope of the CBAM.
- The CBAM could not therefore fall within the definition of “Tax” or “Other Tax”:
  - “Tax” is defined in the EFET Gas with respect to “*any payment, nomination and allocation under any Individual Contract, on Natural Gas, or on the sale, transportation or supply of Natural Gas*”.
  - “Other Tax” refers to the definition of “Tax” in the EFET Gas.

3

Q&A

CBAM as “Tax” or “Other Tax” in the meaning of EFET General Agreements (German law)

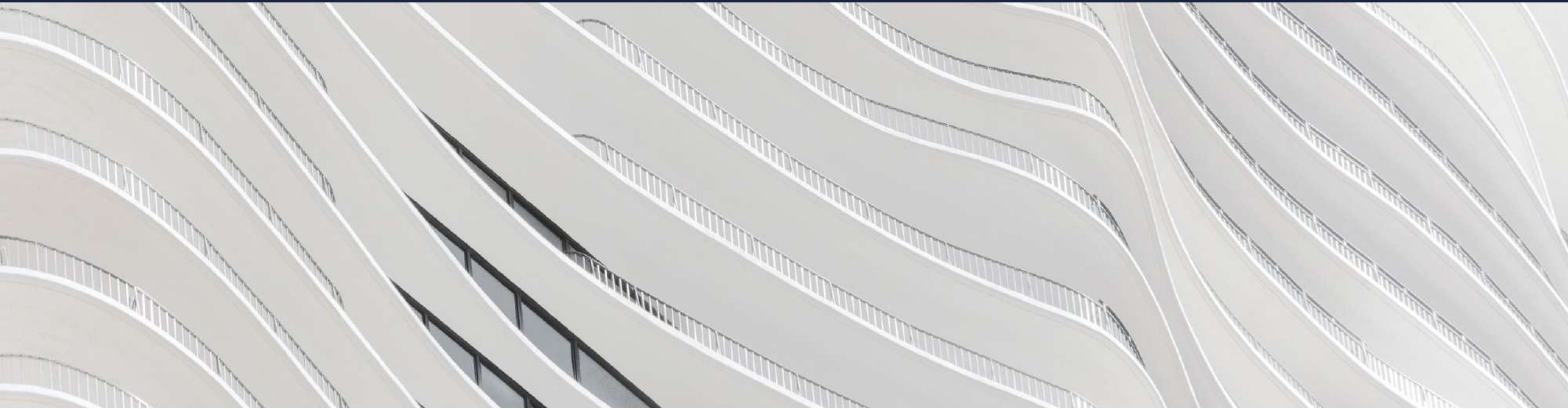
EFET Legal Committee Meeting
Düsseldorf, 14 December 2023

DLA PIPER

Scope of Review

- Can fees under the Carbon Border Adjustment Mechanism (CBAM) be considered a “Tax” or “Other Tax” in the meaning of the respective definitions in EFET General Agreements governed by German law?
  - Our analysis is limited to the EFET General Agreement concerning the Delivery and Acceptance of Electricity (EFET Power)
  - It excludes the EFET General Agreement concerning the Delivery and Acceptance of Natural Gas (EFET Gas) as natural gas deliveries are not in scope of CBAM

Legal background of CBAM fees



Legal background of CBAM fees (1)

General information

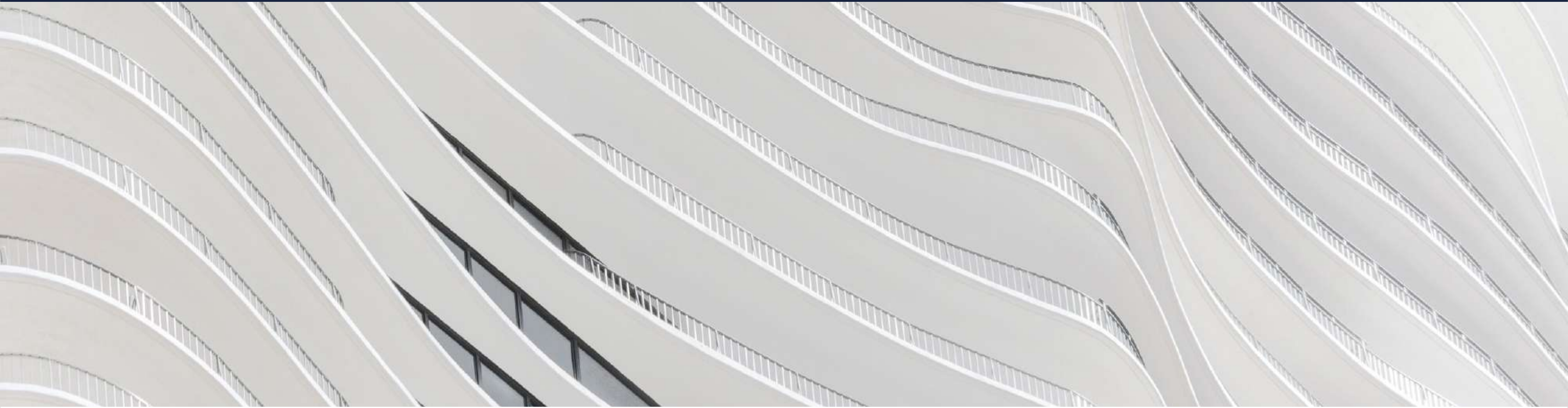
- CBAM is a regulatory and environmental policy measure of the European Union (EU)
- CBAM is established through Regulation (EU) 2023/956 dated 10 May 2023, which will fully apply on 1 January 2026
- The regulation complements and reinforces the existing EU carbon pricing mechanism of 2005, and especially the EU Emission Trading System (EU ETS)
- In its scope are products and greenhouse gases relating to imports of certain goods: cement, <u>electricity</u>, fertilizers, iron and steel, aluminum and hydrogen

Legal background of CBAM fees (2)

Obligations for importers under CBAM

- **As of today, only certain obligations under CBAM apply**
  - This especially relates to reporting duties for importers of goods in scope of the new rules on greenhouse gas emissions
  - Financial payments/compensations do not yet apply
- **As of 1 January 2026, full obligations under CBAM apply**
  - Importers will need to declare each year the quantity of goods imported into the EU in the preceding year and their embedded greenhouse gases
  - Based on the respective declarations, importers will have to surrender a number of CBAM certificates corresponding to their total embedded greenhouse gas emissions
  - For these purposes, importers must buy certificates to comply with the respective obligation
  - Payment reductions can be claimed on the basis of any carbon price paid in the country of production

Interpretation of the definition of “Tax” under the EFET Power



Interpretation of the definition of “Tax” (1)

The wording states three (key) requirements.

*“__Tax__” means **any present or future tax, levy, impost, duty, charge, assessment royalty, tariff or fee of any nature** (including interest, penalties and additions thereto) that **is imposed by any government or other taxing authority** (whether or not for its benefit) **in respect of any payment, nomination and allocation under any Individual Contract or under this Agreement**, and “Taxes” shall be construed accordingly. For the avoidance of doubt, Tax shall exclude; (i) any tax on net income or wealth; (ii) a stamp, registration, documentation or similar tax; and (iii) VAT;”*

Interpretation of the definition of “Tax” (2)

(1) “any present or future tax, levy, impost, duty, charge, assessment royalty, tariff or fee of any nature,”

- The wording is very broad
- It is explicitly not limited to taxes but instead also refers to any levy, impost, duty, charge, assessment royalty, tariff or fee of any nature
- From our perspective, payments to be made in connection with CBAM (even if for certificates to be acquired under CBAM) could well be considered a “payment” in the meaning of the definition
- The costs for certificate can at least be considered as a “fee of any nature” in the meaning of the definition
- Importers have to pay the fee in order to import electricity from a third country and to fulfill their obligations arising from a trading contract with a counterparty in the EU

Interpretation of the definition of "Tax" (3)

(2) "imposed by any government or other taxing authority,"

- This requirement is also met
- In our view, it is intended to ensure that the payment is raised by any government or other taxing authority, i.e. by a public authority, as the responsible institution
- In this context, we feel that a German court would interpret the term "imposed" in a wider sense and, thus, as raised/levied/collected by the responsible public authority
- The CBAM certificate is to be obtained from a governmental authority of the relevant Member State and the importer of electricity must pay for such certificate

Interpretation of the definition of "Tax" (4)

(3) "in respect of any payment, nomination and allocation under any Individual Contract or under this Agreement."

- It could be questionable whether the payments in connection with the CBAM are made "in respect of" any payment, nomination and allocation under an Individual Contract or the EFET General Agreement
  - CBAM does not impose any direct payments/charges in relation to any payment, nomination and allocation under an Individual Contract or the EFET General Agreement
  - Instead, CBAM implements a requirement for CBAM certificates for any imports of electricity into a Member State
  - Consequently, based on a narrow interpretation of the term "in respect of", it could be argued that the third requirement is not met

Interpretation of the definition of “Tax” (5)

(3) “in respect of any payment, nomination and allocation under any Individual Contract or under this Agreement.”

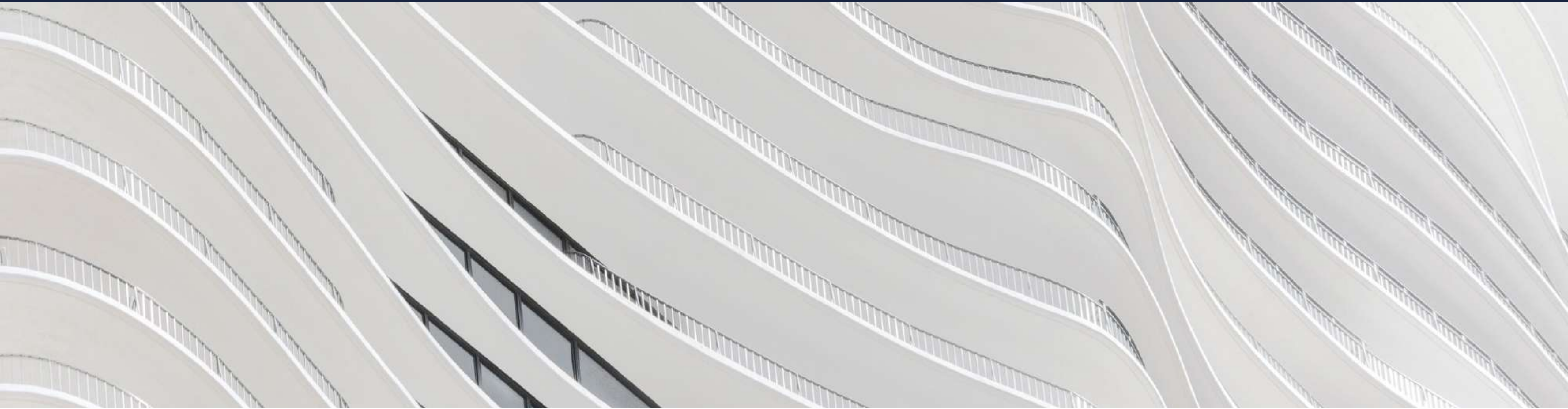
- However, it is to be noted that the definition also explicitly refers to “nomination and allocation” under the respective agreements
  - In the EFET Power, the term “nomination” refers to the action to be taken in order to arrange for the delivery of electricity (in a trading environment usually by way of nominations from one balancing group to another)
  - Consequently, there seem to be good arguments that a payment requirement in relation to a respective delivery should be in scope of the definition
  - In this context, it is however important to note that this interpretation would require clear evidence that specific deliveries under Individual Contracts and an EFET General Agreement have triggered the relevant payments in connection with CBAM

Interpretation of the definition of “Tax” (6)

Tax shall exclude; (i) any tax on net income or wealth; (ii) a stamp, registration, documentation or similar tax; and (iii) VAT

- For completeness: We do not expect that the statement “*For the avoidance of doubt, Tax shall exclude; (i) any tax on net income or wealth; (ii) a stamp, registration, documentation or similar tax; and (iii) VAT*” in the definition of Tax excludes the CBAM fees from the definition.

Interpretation of the definition of “Other Tax” under the EFET Power



Interpretation of the definition of "Other Tax"

> *"**Other Tax**" means any energy Tax or excise duty but not including Taxes targeted at end users;*

- From our perspective, CBAM certificates and the related payment requirements are neither to be considered an energy tax nor an excise duty as it does not constitute a tax on energy production or energy consumption
- Instead, the CBAM certificates and the related payments are required for any import of electricity into the EU

7. Update on REMIT II - practical take and potential implementation challenges, STOR obligation vs self-incrimination

Presentation by Marek Dal-Canton & Katharina Lüken, Chairs of EFET Trading Compliance WG

REMIT refit – Update

August 2023

Katharina Lüken & Marek Dal-Canton

Agenda

1

(Implementation) Timeline

2

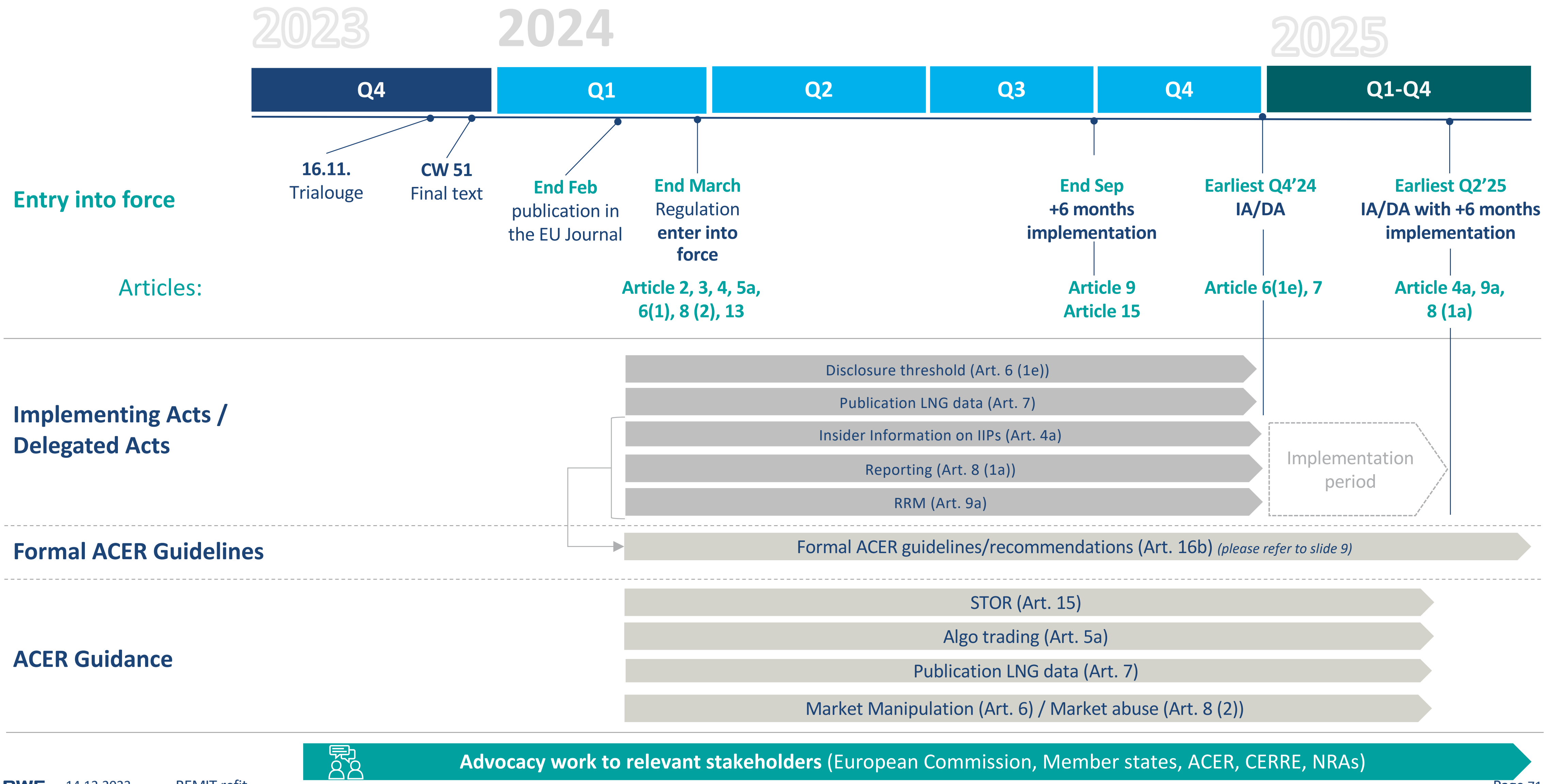
What changed?

3

Impact for Legal Departments

Where are we now?

Implementation timeline



Implementation Timeline

In general	• In force **20 days** after publication
Exemptions	• **Defined** in some Articles • Will probably apply where **implementation** is required (e.g. Balancing Market Data) • In some cases (such as STOR), **requested** by the industry (e.g. via EFET)

What changed?
- selection of topics -

What is new?

Definition of market manipulation (Art. 2)	• Added: “engaging in any other behaviour” • Including benchmarks
Definition of wholesale energy product (Art.2)	• ….”may result in the delivery in the Union, as a result of single day-ahead and intraday coupling”
Obligation to use Inside Information Platform (IIP; Art. 4)	• What to do if IIP is not available? • Back up in recital (11)
Algorithmic trading (Art. 5a)	• Systems and controls required • Notification to NRAs

What is new (2)?

Threshold (Art. 6)	• ACER might develop such
Intermediate steps	• Need to be published as inside information
Hydrogen & storage	• Contracts relation to the storage of electricity or natural gas are added
Third country firms (Art. 9)	• Must designate a representative (authorized to act on the firm's behalf)

ACER Powers (Art. 13)

- ACER has **only** powers to **investigate (including conduct on-site inspections)** and **request information** if the competent national energy regulators do **not object** to it

- ACER can open investigation only for **cross-border cases**, i.e., when 2 EU Member States are concerned

- ACER **cannot** directly themselves determine and impose **sanctions** for REMIT breaches regarding **market abuse** cases

- only impose sanctions in case firms do not comply with the ACER request for investigations and information

Maximum administrative fines (Art. 18)

2. Member States shall, in accordance with national law, and the ne bis in idem principle, ensure that the national regulatory authorities have the power to impose at least the following administrative sanctions and administrative measures relating to breaches of the provisions of this Regulation:

[…]

e) adopt a decision **imposing administrative fines**

in respect of legal persons, maximum administrative fines of at least:

- **for breaches of Articles 3 and 5:** 15% of the total turnover in the preceding business year;
- **for breaches of Article 4 and 15:** 2% of the total turnover in the preceding business year;
- **for breaches of Article 8 and 9:** 1% of the total turnover in the preceding business year.

in respect of natural persons, maximum administrative fines of at least:

- **for breaches of Articles 3 and 5:** EUR 5 000 000;
- **for breaches of Article 4 and 15:** EUR 1 000 000;
- **for breaches of Article 8 and 9:** EUR 500 000.

[…] **the amount of the fine shall not exceed 20 % of the annual turnover of the legal person concerned in the preceding business year**. In the case of **natural persons, the amount of the fine shall not exceed 20 % of the yearly income in the preceding calendar year**. Where the person has directly or indirectly benefited financially from the breach, the amount of the fine shall be at least equal to that benefit. "

- **Recap**

Art.3: insider trading
Art. 5: market manipulation
Art 4: inside information
Art. 15: STOR
Art. 8: Data collection
Art. 9: Registration of market participants

STOR (Art. 15)

- Obligation to send **S**uspicous **T**ransaction and **O**rder **R**eports to NRAs
- Covers **Art. 3** (insider trading), **Art. 4** (publication) and **Art. 5** (market manipulation)
- All **p**ersons **p**rofessionally **a**rranging and **e**xecuting **t**ransactions **(PPAET)**

  What means executing?

- Monitoring of all wholesale energy products
- Includes “errors” that fall in the scope of market manipulation (no distinguishment between “intentional errors” and “fat fingers”)

  Self-incrimination?

STOR (Art. 15)

Open points:

- What is the consequence of Art. 15(2) on the scope of the obligation?

2. Any person professionally **executing transactions under Article 16 of Regulation (EU) No 596/2014 who also executes transactions in wholesale energy products that are not financial instruments, and who reasonably suspects that an order to trade or a transaction, including any cancellation or modification thereof, whether placed on or outside an OMP, might breach Article 3, 4 or 5 shall notify the Agency and the relevant national regulatory authority without further delay but no later than four weeks as of the day in which the person professionally executing transactions is aware of the suspicious event.**

End

Q&A