The norms of the Cabinet Regulation on the implementation of the mandatory electricity procurement – control of self-consumption and calculation of overcompensation – comply with Article 64 of the *Satversme*

On 18 April 2019, the Constitutional Court passed the judgement in case No. 2018-16-03 "On Compliance of Para 91, Para 92, Para 98 and Para 99, and Para 2 of Annex 8 of the Cabinet Regulation of 10 March 2019 No. 221 "Regulations Regarding Electricity Production and Price Determination upon Production of Electricity in Cogeneration" and of the last sentence of Para 63^8, Para 106, Para 107, Para 113 and Para 114, and Para 2 of Annex 10 of the Cabinet Regulation of 16 March 2010 No. 262 "Regulations Regarding Electricity Production and Price Determination upon Production of Electricity from Renewable Resources" with Article 64 of the *Satversme* of the Republic of Latvia".

The Contested norms

The Cabinet Regulation of 10 March 2009 No. 221 "Regulations Regarding Electricity Production and Price Determination upon Production of Electricity in Cogeneration" (hereinafter – Regulation No. 221):

Para 91 provides that Para 28 ^{21} of Regulation No. 221 shall be applied from 1 June 2019.

Para 92 provides that Para 29.4. ^{2} of Regulation No. 221 shall be applied from 1 July 2019.

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[1] Para 28^2 of Regulation No. 221 provides: "The merchant, who has acquired the right to sell electricity produced in cogeneration in the framework of mandatory electricity procurement, shall submit to the system operator, the trader and the Ministry the principal scheme of electric connection certified by the merchant referred to in Para 28^1 of this Regulation. After the agreement referred to in Para 24 of this Regulation has entered into effect, the trader shall commence purchasing the electricity produced in cogeneration at the cogeneration plant if the merchant has submitted to the system operator, the trader and the Ministry the principal scheme of electric connection referred to in Para 28^1 of this Regulation. If any changes have been made to the cogeneration plant, the merchant shall ensure that the principal scheme of electric connection, referred to in Para 28^2 of this Regulation which complies with the actual situation and is certified by the merchant has been submitted to the system operator, the trader and the Ministry."

[2] Sub-para 29.4. of the Regulation No. 221 provides: "If the cogeneration power plant, which sells the produced electricity in the framework of mandatory electricity procurement, has several connections to the grid of the system operator, each hour the amount of electricity, which is constituted by the difference between the electricity fed into the grid of the system operator and the electricity received from the grid of the system operator in the framework of all

Para 98 provides: "The merchants, who by 1 June 2019 have started selling the electricity produced by cogeneration at the cogeneration power plant in the framework of mandatory procurement shall submit by 1 June 2019 to the system operator, the trader and the Ministry the principal scheme of electric connection referred to in Para 28^1 of this Regulation."

Para 99 provides that in case, if the merchants have not met the requirements referred to in Para 98 of this Regulation, the trader shall discontinue the purchase of the electricity produced in cogeneration in the framework of the mandatory procurement from 1 July 2019. The trader shall resume purchasing the electricity produced in cogeneration in the framework of the mandatory procurement beginning with the first date of the successive full calendar month after the principal scheme of electric connection referred to in Para 28^1 of this Regulation has been submitted to the system operator, the trader and the Ministry.

Para 2 of Annex 8 provides the formula for calculating the total internal rate of return of capital investment of a cogeneration power plant.

The Cabinet Regulation of 16 March 2010 No. 262 "Regulations Regarding the Production of Electricity Using Renewable Energy Sources and the Procedures for the Determination of the Price" (hereinafter – Regulation No. 262):

The last sentence of Para 63^8 provides that the moment as of which the producer has begun to exercise the right granted in accordance with Section 29 of the Electricity Market Law is to be considered the beginning of the support period.

Para 106 provides that Para 56^{3}[3] of Regulation No. 262 shall be applied from 1 June 2019.

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connections of the system in accordance with the principal scheme of electric connection referred to in Para 28^1 of this Regulation, shall be calculated."

[3] Para 56^3 of Regulation 262 provides: "The merchant, who has acquired the right to sell electricity produced from renewable energy resources in the framework of mandatory electricity procurement, shall submit to the system operator, the public trader and the Ministry the principal scheme of connection certified by the merchant referred to in Para 56^2 of this Regulation. After the agreement referred to in Para 56 of this Regulation has entered into effect, the public trader shall commence purchasing the electricity produced in cogeneration at the cogeneration plant if the merchant has submitted to the system operator, the public trader and the Ministry the principal scheme of connection referred to in Para 56^2 of this Regulation. If any changes have been made to the power plant, the merchant shall ensure that the principal scheme of connection which complies with the actual situation and is certified by the

Para 107 provides that Para 56^1 and Para 57^{1}[4] of Regulation shall be applied from 1 July 2019.

Para 113 provides: "The merchants, who by 1 June 2019 have started selling the electricity produced from renewable energy resources in the framework of mandatory procurement, shall submit by 1 June 2019 to the system operator, the public trader and the Ministry the principal scheme of connection referred to in Para 56^2 of this Regulation."

Para 114 provides that in case, if the merchants have not met the requirements referred to in Para 113 of this Regulation, the public trader shall discontinue the purchase of the electricity produced from the renewable energy resources in the framework of the mandatory procurement from 1 July 2019. The public trader shall resume purchasing the electricity produced from renewable energy resources in the framework of the mandatory procurement beginning with the first date of the successive full calendar month after the principal scheme of connection referred to in Para 56^2 of this Regulation has been submitted to the operator of the system, the public trader and the Ministry.

Para 2 of Annex 10 provides the formula for calculating the total internal rate of return of capital investment of a power plant.

The Norm of Higher Legal Force

Article 64 of the *Satversme* of the Republic of Latvia (hereinafter – the *Satversme*)*:* "The *Saeima*, and also the people, have the right to legislate, in accordance with the procedures, and to the extent, provided for by this *Satversme*."

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merchant referred to in Para 56^2 of this Regulation has been submitted to the system operator, the public trader and the Ministry."

[4] Para 56^1 of the Regulation No. 262 provides: "The public trader in the framework of the mandatory procurement shall purchase only the surplus of the produced electricity, which remains after using the electricity for ensuring the operation of the power plant in accordance with the principal scheme of connection referred to in Para 56^2 of this Regulation. If the power plant has several connections to the grid of the system operator, the surplus of produced electricity, which has remained after using the electricity for ensuring the operations of the power plant, shall be calculated for each hour as the amount of electricity constituted by the difference between the electricity fed into the grid of the system operator and received from the grid of the system operator in the framework of all connections of the system in accordance with the principal scheme of connection referred to in Para 56^2 of this Regulation."
Para 57^1 of this Regulation, in turn, provides: "The merchant is allowed to consume and to purchase the electricity needed to ensure the operations of the power plant, by using the connections to the grid of the system operator."

The Facts

The case has been initiated on the basis of an application by twenty members of the 12th convocation of the *Saeima* (hereinafter – the Applicant). The Applicant holds that the unjustified excessive state aid for the production of electricity in cogeneration and from renewable resources is allowed by the contested norms. I.e., the contested norms determine without justification a delayed transitional period to control over the implementation of the self-consumption principle, thus revoking or postponing the implementation of the requirements set in the law for more than a year. The amendments to the regulation on over-compensation, in turn, allow unjustified large support for electricity operators, since the state aid granted to the merchant and other income have not been taken into account in the calculation of over-compensation. As the result of this, all final users of electricity, proportionally to their consumption of electricity, must cover the unfoundedly high payment of the component of mandatory procurement.

The Applicant holds that the contested norms are incompatible with Article 64 of the *Satversme*. They had been issued *ultra vires* because by them the Cabinet had decided on matters that fell within the competence of the *Saeima* and the contested norms are incompatible with the content and purpose of the authorising norms of laws and do not ensure that electricity is supplied to the users of electricity for justified prices.

The Court's Findings

The Constitutional Court noted that, pursuant to the principle of the parliament's supremacy, it is admissible that the Cabinet is granted the authorisation to draft the norms required for implementing a law. Whereas the *Saeima* has the obligation to decide itself, in the procedure of legislation, on the most import matters in the life of the state and society. [9.]

In the Electricity Market Law, the *Saeima* has envisaged the right of the electricity producers to sell and, respectively, to the public trader the obligation to purchase in the framework of mandatory electricity procurement the remaining amount of electricity produced from renewable energy resources and in cogeneration, which has been left over after using the electricity for the needs of the power plant; i.e., it has established the

principle of self-consumption. Moreover, the *Saeima* has stipulated in this law that the expenses caused by the guaranteed price and the mandatory procurement must be covered by all final users of electricity, for a justified price. The legislator has authorised the Cabinet to establish the procedure for implementing these requirements. [11.]

Hence, the Constitutional Court found that the legislator had set the principle of self-consumption and the requirement to supply electricity to its final users for a justified price and had authorised the Cabinet to establish a procedure for implementing these requirements. The Cabinet has been authorised to establish the procedure for the mandatory electricity procurement, which comprises the implementation of the procedure for mandatory electricity procurement, supervision of the mandatory procurement and setting the electricity price. [11.-12.]

The Constitutional Court found that in order to establish, whether the Cabinet, in adopting the contested norms, has complied with the authorisation granted by the legislator, it must establish the content and the purpose of the contested norms and then must assess, whether the Cabinet, in adopting these norms, has acted in compliance with the legislator's will. [12.]

The Court's findings regarding the control over self-consumption

The Constitutional Court noted that the State has the obligation to control the use of state aid. This means that the State must control also compliance with the principle of self-consumption. [13.]

The Constitutional Court found: since the legislator had envisaged in the Electricity Market Law a system of state aid for the production of electricity, the system of its supervision had been constantly improved. *Inter alia*, Regulation No. 221 and Regulation No. 262 provide that an electricity producer submits an annual report, through which the Ministry of Economics can control, whether the principle of self-consumption has been complied with. Moreover, the Ministry has the right to establish a control group, which verifies, as necessary, the compliance of power plants with the criteria set for them, as well as the accuracy of the information provided by the merchant. [13.]

The Constitutional Court underscored that the actions by the public administration should be such as to allow it to perform its functions as effectively as possible. Therefore the right referred to above should be exercised in a way to ensure effective control over compliance with the principle of self-consumption. [13.]

The Constitutional Court found that, thus, already prior to introducing the new requirements, a mechanism had been in place that allowed controlling the compliance with the principle of self-consumption; however, it had not been able to prevent all cases, where the right to sell electricity within the framework of the mandatory electricity procurement had been abused. Therefore Regulation No. 214 and Regulation No. 215 introduced an additional control mechanism to prevent cases, when the right to sell electricity in the framework of the mandatory electricity procurement had been exercised contrary to the statutory requirement to comply with the principle of self-consumption. [13.]

The Constitutional Court found that the compliance of the contested norms, which regulate control over self-consumption, with Article 64 of the *Satversme* had been contested because they envisaged a transitional period for introducing the additional control mechanism. [13.3.]

The Constitutional Court found that the Cabinet could set a transitional period applying the requirements regarding administrative and technological adjustments. The Constitutional Court recognised that the transitional period set for introducing additional mechanisms of control was not disproportional or excessively long, which would no longer comply with the purpose of regulation; moreover, it takes into account that in the case of not complying with the new requirements, the right to sell electricity within the framework of the mandatory electricity procurement would be denied. [14.]

The Constitutional Court underscored that within the transitional period, established with respect to the regulation, which introduced an additional mechanism for controlling compliance with the principle of self-consumption, neither the requirements to comply with the principle of self-consumption nor the obligation of authorities to perform the necessary inspections effectively had been limited. Hence, the Applicant's argument that the established transitional period revokes or delays the compliance with the statutory

requirements or the obstacles are created for conducting inspections with regard to past periods is ungrounded. [14.]

The Constitutional Court found that the Cabinet, by the contested norms that regulated the control over self-consumption, had validly established a transitional period for introducing such a procedure, pursuant to which the electricity producers, who wished to sell electricity in the form of mandatory electricity procurement, would have to submit to the system operator, the public trader and the Ministry the principal scheme of electric connection, and the public trader would have to discontinue the mandatory procurement if the merchant failed to submit this scheme within the term set for it. Hence, the Cabinet, in adopting the contested norms, which regulate control over self-consumption, has acted within the framework of the authorisation granted by the legislator. [14.]

The Constitutional Court recognised that the contested norms, which regulated control over self-consumption, complied with Article 64 of the *Satversme* [14.]

The Constitutional Court's findings regarding the calculation of over-compensation

The Constitutional Court found that Regulation No. 443 and Regulation No. 444, taking into account the recommendation made by the European Commission to prevent over-compensation of electricity, introduced the calculation of over-compensation with respect to the state aid for electricity production, using renewable energy resources and in producing electricity by co-generation. [15.]

The Constitutional Court found that in the calculation of over-compensation, the aid payments to the power plant, which the merchant had received in the period of exercising the right granted in accordance with the norms of the Electricity Market Law, were taken into account. It follows from the above that the contested norms, which regulate the calculation of over-compensation, do not require taking into account in calculating the total internal rate of the return the aid received before the Electricity Market Law entered into force. [15.]

The Constitutional Court noted that the limits of the Cabinet's authorisation with respect to the calculation of over-compensation were set by the legislator's requirement that electricity should be supplied to its final consumers for a justified price. [15.1.]

The Constitutional Court noted that the assessment of the exact amount of state aid that would ensure electricity for "a justified price" comprised also a political choice. Therefore it reminded that, on the one hand, the legislator enjoyed broad discretion with respect to political considerations; however, on the other hand, this freedom was not unlimited. The legislator may not exercise its discretion arbitrarily or contrary to the general principles of law, other norms of the *Satversme*, values included therein, and the European Union law. [15.1.]

The Constitutional Court found that the support for producing electricity in co-generation and from renewable energy resources had been envisaged to facilitate such production of electricity, compensating to its producers the costs and, at the same time, to ensure reasonable profit to them. Hence, in the context of the present case, the authorisation granted by the legislator to determine a justified electricity price means that the rules on setting the price must be established in accordance with the requirements of the legal system and in the scope to promote reaching the aims set for the state aid by the legislator with reasonable costs [15.1.]

In Latvia, the electricity market was liberalised from 1 July 2007. Liberalisation of the electricity market envisages free competition and, thus, facilitates the formation of an economically justified electricity price. Since this date, the state aid payments, which influence the formation of electricity price, are to be granted only insofar they ensure that the aims of the state aid are reached. Moreover, in the conditions of the free market, the aid granted by the State to electricity producers may jeopardise also the competition in the internal market of the European Union. [15.2.]

The Constitutional Court found that the Cabinet, by the contested norms that regulated the calculation of over-compensation, had established a procedure that envisaged eliminating in the future the identified over-compensation for electricity producers, who had incurred it by exercising the right envisaged in the Electricity Market Law, and the mechanism for

preventing this over-compensation had been approved by the European Commission. [15.2.]

The Constitutional Court found that, with the coming into force of the Electricity Market Law, it is envisaged to open the electricity market to free competition as well as to introduce the requirement that the costs of the mandatory procurement must be covered by all final consumers of electricity. Hence, the Constitutional Court concluded that with the coming into force of this particular law, in the aspect of free competition, as well as in the aspect that that the electricity price paid by the final consumers of electricity must be justified , the over-compensation of some electricity producers becomes relevant. [15.3.]

Additionally, the Constitutional Court found that the initial wording of the Electricity Market Law revealed also the legislator's will to respect, in particular, the rights previously granted to merchants in accordance with the norms of the Energy Law. Hence, this has been the legislator's will – to retain the rights previously granted in accordance with the Energy Law. Whereas the scope of the Cabinet's authorisation is restricted by the limits of discretion set by the legislator. [15.3.]

The Constitutional Court established that the aim of the calculation of over-compensation, prepared by the Cabinet, is to envisage such a procedure that would allow preventing, in the future, cases where the merchants would receive, in total, excessive state aid. The Cabinet has drafted such regulation for preventing over-compensation that allows to calculate effectively and to forecast, in compliance with the principle of sustainable development, commensurate profit for the electricity producers and, accordingly, justified electricity price for its final consumers [15.3.]

The Constitutional Court noted that the State's actions should be aimed at sustainable development, *inter alia*, drafting of sustainable legal regulation. Therefore legal regulation, which in the future will promote sustainable and secure production of electricity, complies with the requirements regarding sustainable national development [15.3.]

The Constitutional Court found that the Cabinet, in compliance with the principle of sustainable national development, has decreased the state aid payments so that they would comply with the aims of the state aid and that the state aid for those energy producers, who

had received it in compliance with the norms of the Electricity Market Law and from public resources, would not be excessively large. Hence, this regulation, by supporting the production of electricity from renewable energy resources and in co-generation, allows saving public financial resources. [15.3.]

The Constitutional Court recognised that the Cabinet, by adopting the contested norms, had acted in compliance with the legal norms of higher legal force and the general principles of law, as well as reasonably and proportionately with the aims of the particular state aid to be reached. Hence, the Cabinet has abided by the authorisation granted by the legislator to determine a justified price for the mandatory electricity procurement. [15.3.]

Therefore the Constitutional Court recognised that the contested norms, which regulated the calculation of over-compensation, complied with Article 64 of the *Satversme*. [15.3.]

The Constitutional Court held:

to recognise Para 91, Para 92, Para 98 and Para 99, and Para 2 of Annex 8 of the Cabinet Regulation of 10 March 2019 No. 221 "Regulations Regarding Electricity Production and Price Determination upon Production of Electricity in Cogeneration" and of the last sentence of Para 63[8], Para 106, Para 107, Para 113 and Para 114, and Para 2 of Annex 10 of the Cabinet Regulation of 16 March 2010 No. 262 "Regulations Regarding Electricity Production and Price Determination upon Production of Electricity from Renewable Resources" as being compatible with Article 64 of the *Satversme* of the Republic of Latvia.

The judgement by the Constitutional Court is final and not subject to appeal, it shall enter into force on the day it is published. The judgement will be published in the official journal "*Latvijas Vēstnesis*" within the term set in Section 33 (1) of the Constitutional Court Law.

The txt of the judgement is available on the homepage of the Constitutional Court: http://www.satv.tiesa.gov.lv/web/viewer.html?file=/wp-content/uploads/2018/08/2018-16-03_Spriedums.pdf#search=

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