II-5.8: The French Electricity Regulator can legitimately use its powers to organize Diffuse Effacement, but oversteps its mandate (ultra vires) when it mandates that intermediaries remunerate the energy supplier

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MAIN INFORMATION

The technique of "effacement diffus" [diffuse effacement] is when a number of electricity consumers agree beforehand to consume less electricity at certain times (effacement), which allows other consumers to use the network at peak hours. Corporate intermediaries arrange these diffuse effacements, thereby participating in the adjustment system vital to the security of the electricity distribution network. The Commission de Régulation de l'Energie (CRE – French energy regulator) organized the system of "diffuse seffacement" even though this measure was not contained in statute. The Council of State's Voltalis ruling, handed down on May 3, 2011, recognizes the CRE's right to organize this system. But, it also deems that the regulator exceeded its powers by mandating that the corporate intermediaries organizing diffuse effacement remunerate the electricity provider.

CONTEXT AND SUMMARY

In order to balance supply and demand for electricity, consumers can "efface" when they don't need electricity. These effacements increase the capacity available to other consumers. The phenomenon of "diffuse effacements" is organized by companies such as Voltalis.

Statute had planned for this method of adjustment by mentioning effacement, but not "diffuse effacement". Diffuse effacement is when corporate intermediaries reach out to consumers by asking them to agree not to consume electricity. These intermediaries then aggregate the available electricity, and make it available on the network. There was therefore a *non liquet* concerning this technique, which the regulator wanted to remedy.

Section 15 of the Act of February 10, 2000 organizing the regulation of the French electricity industry specifically addresses the ways that electricity transmission network managers can solicit consumers not to consume, and provides that the manager must adopt the most economically sensible solution amongst the various adjustment propositions submitted to him.

The regulator concluded that in the absence of statute, it was within its powers to "explain the general economic reasoning" behind this section, and to "indicate how the remuneration of 'diffuse effacement' intermediaries could be taken into account within the adjustment mechanism," even though the statute only addressed general methods of adjustment.

Believing that "diffuse effacements must be taken into account in the overall regulation of the electricity industry," the CRE requested the relevant operators to cooperate in developing mechanisms for diffuse adjustment. Then, the regulator laid down the contracts for accessing the network and for "remunerating this service at its just price." The regulator based this decision on the aforementioned Section 15's "economically sensible solution". The regulator therefore decided that the offers were to be classified "in function of their social surplus," which implied "reimbursing part of the effaced energy to the provider who injected it."

Concretely, the companies that organized the program had to pay EDF, the electricity provider, even though the electricity was better managed and used, and despite the fact that the unused electricity would have disappeared, since energy is not a durable good.

Voltalis appealed this deliberation, which took place on July 9, 2009, before the Council of State, on the grounds that the obligation to pay the electricity provider even though it had not bought any energy was *ultra vires*. The judge permitted the classification of "grievous administrative act", even though the CRE insisted that it was not an act, but a recommendation. The judge ruled that the mention of an obligation to remunerate the electricity provider is one of "the essential parameters of the economic equilibrium of the mechanism of diffuse effacement." Therefore, the CRE's deliberation is grievous to Voltalis, who is legitimate to attack it before a court of law for *ultra vires*.

Regarding the facts of the case, the Council of State ruled that statute mandates the network manager to maintain a balance between supply and demand, which allows it to manage transmission in a satisfactory fashion by avoiding black outs (for example), by requesting more production (for example). The manager has many tools at his disposal to perform this duty, such as contracts with consumers to reduce their consumption when there is tension on the network, thereby ensuring the entire system's security. The associated costs are divided between the network users and the managers. Section 15 of the aforementioned Act provides that the financial arrangements are subject to regulatory approval as to the calculation of spreads and the financial compensations due in virtue of the arrangement.

The Council of State ruled that the regulator was able to go beyond this arrangement by experimenting with "diffuse effacement," but the modalities of such arrangements (as the regulator recognized) must respect the general statutory principle of "the most economically sensible solution".

But, this is where the judge's approbation ends. The Council of State ruled that the Act does not mention that "the economic evaluation of an offer can involve the indirect effects on society as a whole." Therefore, by demanding that the corporate intermediary remunerate the electricity provider for arranging diffuse effacement, the regulator "misinterpreted the legislature's intent".

The deliberation was therefore annulled as *ultra vires.*

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BRIEF COMMENTARY

This Council of State ruling is important for a number of reasons. First of all, it is part of a larger movement of hostility towards regulators, whose power is often seen as illegitimate because it does not result from elections. In this very traditional point of view, regulatory power is seen as a "subdelegation," meaning that their power is delegated by the legislature. Therefore, they cannot make use of any power that has not been explicitly devolved. This is far from an economic, pragmatic, and teleological point of view, which attributes regulators all powers necessary to fulfill their missions, with the principal limit being proportionality.

However, we must do justice to the Council of State. It is true that annulling the regulator's decision was because it disapproved of its approach from a legal point of view, and not because it had a particular opinion on the question of diffuse effacement. Although the law did not explicitly mention diffuse effacement, the judge ruled that the non liquet did not disempower the regulator. On the contrary, since diffuse effacement is a method of adjustment, and statute requires adjustment to be regulated, the regulator can intervene even in a case of non liquet. Therefore, the ruling is not reactionary (in the literal sense of the term) because it recognizes the principle of the legality of regulatory intervention even in cases of non liquet, as long as the intervention: corresponds to its mission, regulation is required, and the new phenomenon (in this case diffuse effacement) is simply a variant of a scheme already contained in statute (adjustment).

What the court did not allow was the liberty the regulator took with regards to the criteria for evaluating the financial equilibrium of the system and its beneficiaries. Indeed, with such a legally and economically obscure term as "economically sensible solution," the judge might be tempted not to review the way regulators review the prices that contractually occur within regulated systems (1). It is remarkable that the parties did not spontaneously turn towards the energy provider, because they do not legally need it. The regulator required the intermediary to remunerate the provider, on the grounds that once energy has been produced, it is available and transferable from one consumer to another. It is remarkable that we find the same issues of revenue sharing within the debate on Net Neutrality. But, in order for this to take place, the regulator has to bring in the notion of "social surplus and social well-being": in order for the system to be profitable to all in the long term, energy providers who provide the raw materials must be remunerated by the intermediaries, who profit from the raw materials by playing a game between those who consume and those who consume a lot. That is fair.

But, we must take the law into account. The administrative judge is more audacious than the regular judge in reviewing administrative decisions. Therefore, the Council of State did not hesitate to annul the regulator's decision on the grounds that decisions involving systemic equity and durability must be made by the legislator, and not by regulators. Just like Net Neutrality, legitimate political powers must decide whether systems in which some companies provide the raw material without any remuneration, while other companies get rich thanks to the market and contracts, can be allowed to go on. Once again, the question of the place of contracts within regulated systems has been opened. The aggregation of non-consumption of electricity is playing with a market upon which there is sufficient supply. It is true that diffuse effacement is a method of adjustment, required to regulate the electricity industry. So, why don't we give the regulator the power it needs? Here, it is evident that this is not the case.

Of course, such powers are only legitimate when they are carried out according to due process. But, it is childish on behalf of regulators to try to escape judicial review by masking their mandatory rules under titles such as "recommendation", "communication", etc. Judges' duty is to requalify such decisions. The mandatory force of the July 9, 2009 deliberation, which came after a series of non-mandatory deliberations, led to the judge calling to order: a regulator cannot simply play with words to escape the rule of law.

1. FRISON-ROCHE, Marie-Anne, What is a price in law?,The Journal of Regulation, April 2010, I-1.4