EU electricity market reform
The European Commission is preparing a reform of EU electricity market rules, aiming to address price volatility caused by the gas crisis and adapt the power market to an energy system increasingly dominated by renewables.

In this special report, EURACTIV explores the different aspects of the EU electricity market reform, due to be presented on 16 March.
LEAK: Brussels plans to inject more stability in EU electricity market

EU unveils power market reform to tame volatile electricity prices

Academic: EU power market reform hits ‘political sweet spot’ but risks backfiring

Spain aims for electricity market reform deal during EU Council stint

PGE: We need a fair and well-functioning power market to finance renewables
The European Commission is preparing to table a reform of EU electricity market rules next week, aiming to introduce more stability through a greater use of long-term contracts and a renewed focus on demand reduction measures, according to a leaked draft seen by EURACTIV.

The changes come in response to the energy crisis that “showed how exposed consumers and industries are and our lack of resilience to energy price spikes”, says the draft proposal, due to be tabled on 16 March.

EU electricity prices have increased sharply since mid-2021, leading to calls for the EU to ease the burden on consumers and ensure sufficient incentives for investments in cheap renewables like wind and solar.

“Whilst the EU’s single market delivers huge gains and growth across Europe, the recent energy crisis has highlighted that the energy market’s short-term focus can distract from broader, longer-term goals,” the draft says, referring to the EU’s goal of reducing emissions to net-zero by 2050.

“The reflection of short-term prices in consumers bills led to price shocks where energy bills of many consumers tripled or quadrupled, even as the costs of wind and solar power were declining,” it adds.

To tackle this, the European Commission’s reform looks at complementing short-term markets with “a greater role of longer term...
instruments", including more fixed-priced contracts for consumers and easier investments in clean technology.

The proposal swerves away from demands from EU countries like Spain and France, which had initially pushed for a radical overhaul to decouple electricity prices from the wholesale gas market.

While gas is used for power generation in countries like Germany and Belgium, this is hardly the case in Spain and France, which produce most of their electricity from renewables or nuclear energy.

This means that the retail price of electricity in those countries is vulnerable to variations in gas prices, even though they may not use gas for power generation.

“We are convinced that this impact could be modulated if the functioning of the market were different,” said a Spanish government official.

“The electricity market is designed in such a way that it is efficient when the power generation technologies that are used have very similar prices. When this is not the case, it works badly,” the official told EURACTIV.

Long-term contracts

Rather than the radical overhaul pushed by France and Spain, the leaked proposal is closer to what the industry has called for – a more targeted approach focused on long-term contracts.

“The Commission has listened to the long-standing recommendation of the industry on long-term signals – signals both for investors and customers – so that they can choose their exposure to extreme price volatility,” said Kristian Ruby, the secretary general of electricity industry group Eurelectric.

A key objective of the reform is strengthening the EU’s industrial competitiveness, both by incentivising more investment in renewable energy and keeping prices down for EU industry, which faces global competition from places with cheaper energy, like the US.

Support for power generation includes “direct price support schemes” for new investments in electricity production in the form of two-way contracts for difference (CfDs) for wind, solar, geothermal, hydropower, and nuclear projects.

CfDs are countersigned by the state and offer a guaranteed level of revenue to energy generators, ensuring they invest in new production capacity even when wholesale electricity prices are low. When prices are high, excess revenues are distributed to final electricity customers based on their share of overall consumption.

Alongside CfDs, the European Commission is looking at boosting other long-term contracts, like power purchase agreements (PPAs) that are passed between private producers and buyers of electricity. Under the proposal, EU countries would have to put in place instruments to reduce the financial risks of PPAs.

Long-term contracts like PPAs and CfDs are expected to “enhance the competitiveness of EU industry facing excessive volatile prices”, according to the draft.

The long-term revenue stability provided by CfDs is valuable, especially for technologies like offshore wind and nuclear power that require significant capital expenditures and involve low operational expenditures, says PGE, the Polish electricity utility.

However, it should be kept only as a voluntary option for generators and as an alternative to market revenues. “Generators should be incentivised, but not forced to use this option,” PGE says.

France too is looking at CfDs to provide stable revenues for its existing fleet of nuclear power plants. “We think the possibility of putting existing installations under contracts for difference is a possibility that should be open to the member states,” said a source at the cabinet of Agnès Pannier-Runacher, the French energy transition minister.

However, CfDs have one big disadvantage – they rely on governments to foot the bill when electricity prices are low. As such, they need to be vetted by the European Commission, which enforces state aid rules within the 27-country bloc.

“There is the question of how much ability states actually have to provide significant fiscal resources for the power system for something like power purchase agreements and contracts for difference,” said Georg Zachmann from the Bruegel economic think-tank.

“We’re talking about a lot of money because those power investments are something to the tune of €80 billion a year,” he told EURACTIV.

And, while it is good that the European Commission is pointing out best practice in long-term
contracts, their design is key and there should be more guidance from the Commission on that, said Bram Claeys, an electricity market expert with the Regulatory Assistance Project (RAP), another think-tank.

**Small consumers and SMEs**

Another part of the reform relates to households and small and medium enterprises (SMEs). It looks at increasing their ability to be active players in the electricity market by enabling power sharing within communities and increasing access to more long-term, stable contracts.

“Active customers shall be entitled to share renewable energy between themselves based on private agreements or through a legal entity and up to 100 MW (megawatts) of total installed capacity,” according to the leaked draft.

This will increase access to local consumption of solar electricity while supporting the grid, according to SolarPower Europe, an industry body.

“That means neighbourhoods can collectively benefit from their solar rooftops,” said Naomi Chevillard, head of regulatory affairs at SolarPower Europe.

Consumers will also be provided with the right to fixed-price contracts alongside dynamic contracts, as well as better information.

This will allow them to choose between long-term, stable prices or adjusting their consumption to take advantage of rises and falls in the price of electricity – for instance, by charging electric vehicles overnight.

The draft also introduces measures to ensure affordable energy in times of crisis, like when wholesale prices are substantially above the five-year average or when there are sharp increases in retail prices.

In these cases, EU countries can “apply public interventions in price setting for the supply of electricity” to SMEs, limited to 80% of their highest annual consumption as an incentive to reduce demand.

EU countries may also set the household electricity price lower than that at which it is provided as long as it is 80% of median household consumption to incentivise demand reduction.

“The crisis has demonstrated how important it is to have well-conceived consumer protection mechanisms in place, especially for vulnerable consumers,” said Claeys.

But while he welcomed some measures to protect consumers, he added that Europe needs to do more to enable them to partake in the value of flexibility and renewables.

**‘Peak shaving’**

To tame excessive price volatility, the European Commission is looking at building more flexibility in the electricity market, by supporting demand-side measures that reduce peaks in electricity consumption.

“The more flexible the system is [...] the more stable prices can be and the more renewable energy the system can integrate,” the draft reads.

It includes an obligation for EU countries to define an indicative national objective for demand-side response and storage in their updated National Energy and Climate Plans.

At the grid level, system operators will be expected to assist in the integration of renewables by increasing transparency around the availability of grid connection capacity to help developers know where to build projects.

This has been a problem in countries like Poland, where 30 gigawatts of mostly renewable power have been denied access to the grid.

The draft also introduces measures that can be brought in to reduce demand during peak hours, when the most expensive power plants are called in – usually those running on gas.

Under the draft proposal, transmission system operators will be enabled to procure so-called “peak shaving” products in order to call for electricity demand reduction during peak hours.

Reducing demand at these times would limit the use of the most expensive electricity and contribute to better integration of renewables in the system, the draft document says.

The reform will be proposed on 16 March and will then be handed over to the European Parliament and EU countries for approval.

Read the full draft electricity market reform proposal here.
The European Commission published its proposal to reform the EU electricity market on Tuesday (14 March), focusing on countering volatile gas prices by providing consumers with more protection, boosting renewables and supporting demand-side measures.

“For over two decades, the electricity market design has served European companies and consumers well, letting them enjoy the benefits of a single market,” said EU energy chief Kadri Simson as she announced the proposal.

“However, the energy crisis spurred by Russia’s attack on Ukraine exposed a number of shortcomings in the current system, which needed to be addressed,” she told journalists.

The proposed reform seeks to accelerate the deployment of renewables, which need to triple before 2030 if the EU is to meet its climate targets.

It also looks at reducing the impact of volatile fossil fuel prices on electricity bills and protecting consumers from future price spikes.

But the proposal will not change the fundamentals of the EU market, which will remain rooted in the current marginal pricing system where cheap renewables and nuclear power are called in first to meet consumer demand, said Kadri Simson, the EU’s energy commissioner. [European Union, 2023]
nuclear power are called in first to meet consumer demand, Simson said.

“The design of short term markets remains the most efficient when it comes to ensuring that the cheapest and cleanest technologies are used first,” the EU’s energy commissioner said.

“The current design also guarantees that there will be trade between member states at moments of scarcity,” she added.

This was welcomed by the renewable energy industry, which had warned against radical reform.

“We’re glad to see that today’s proposal builds on the well-established foundation of the European electricity markets, without upheaving fundamental market principles,” said Naomi Chevillard, head of regulatory affairs at SolarPower Europe.

Giles Dickson, CEO of WindEurope, said: “The problem of Europe’s electricity market these last two years has not been the market design. It’s been high gas prices, made worse by the war.”

**Empowering consumers**

The proposal includes measures enabling EU citizens to become more active players in the energy market, granting them a wider choice of contracts and clearer information.

Suppliers will be required to inform households about the “advantages and risks of different types of contracts,” according to a Commission official, who called this “a very important addition” to consumer protection.

In addition, consumers will be able to combine fixed and flexible pricing for electricity with several suppliers if they wish.

“A consumer may in the future have a fixed and a flexible contract at the same time – with one supplier or even two different suppliers,” explained a senior Commission official.

For instance, households may opt for a fixed price contract for their ordinary consumption – such as lights, TV, internet, etc. – and choose a flexible or dynamic contract for their heat pump or electric vehicle in order to benefit from low night prices, they added.

Consumers will also enjoy a new right to share energy within a community, for example by selling excess rooftop solar power to neighbours, a move described as “historic” by the industry.

“New proposals literally put the power in citizens’ hands. For the first time ever, we’ll have a legal framework to share electricity, complementing the energy communities’ framework,” said Chevillard.

Alongside this, the reform reinforces protection for small consumers.

For instance, EU countries will be able to intervene in times of crisis and set retail prices for households and small businesses, provided the limit is set below their average consumption in order to incentivise demand reduction.

Consumers will also be offered greater protection when energy suppliers go bankrupt, with EU countries obliged to designate a supplier of last resort and prevent vulnerable consumers from being disconnected.

**Demand reduction and ‘peak shaving’**

Another key aspect of the reform is making the market more adaptable to changes in supply and demand, helping to displace pricey gas and coal power during peak demand.

“The Commission plans to tackle high prices from gas power generation in the best way – by reducing its significance,” said Vilislava Ivanova, research manager for clean energy systems at climate think tank E3G.

One way to do this is by allowing power grid operators to use “peak shaving” products to incentivise energy savings when demand is highest, in order to keep prices down.

“The peak shaving product has the potential to stimulate flexibility from end-users,” commented Michael Villa, executive director at Smart Energy Europe, an industry association.

EU countries will also be required to define national objectives for demand-side response and storage in their updated National Energy and Climate Plans, a move hailed by Villa as “a major step forward to quantify, track and stimulate the activation of flexible demand”.

But while flexibility targets are broadly welcomed, they are not sufficient, Ivanova said.

“More action will be needed, especially by network operators, to ensure the EU takes advantage of 21st-century digital technologies and promotes consumer-focused
innovation,” she commented.

**Long-term contracts**

The Commission’s reform also seeks to reduce the exposure of industrial electricity consumers to volatile prices with measures to support long-term contracts for power supply and demand.

“The dominance of the short-term market has amplified the effects of the gas price rise and has been the source of various problems during the crisis,” Simson explained, saying the benefits of cheap renewable power was not sufficiently passed on to industrial consumers.

Long-term contracts includes power purchase agreements (PPAs) that create a stable power price for consumers and guaranteed revenue for producers. EU countries will be required to remove barriers to PPAs with market-based guarantees tackle risk.

Alongside this, any public support for new renewable or nuclear capacity will now have to be done via a two-way contract for difference (CfD), which will ensure guaranteed revenue for energy producers while shielding consumers against excessive price fluctuations.

This means that, when the market price is low, producers will be guaranteed revenues and, when the market price rises, excess profits will be channeled back to consumers.

“We are not proposing contracts for difference for any investments but for investments where public support is deemed necessary,” a senior Commission official explained, saying this will also apply to repowering projects or the lifetime extension of nuclear power plants.

The move was welcomed by Eurelectric, the European electricity industry association.

“Long-term instruments are the key element in this reform as they provide benefits for both customers and investors,” said Kristian Ruby, the secretary general of Eurelectric.

“Access to fixed-price offerings allow customers to limit their exposure to extreme price volatility. At the same time, long-term signals will give investors better visibility on their cash flows,” he added.

Crucially, the proposal does not impose PPAs or CfDs but lets EU countries decide which solution to choose depending on their national circumstances. It is a less radical approach than the mandatory contracts for difference proposed by some EU countries that raised heckles in the renewables industry.

“We're particularly grateful to have avoided CfDs as the only route to market for new solar, or retroactive CfDs on existing solar projects. Investors can trust that the terms of their investments won't suddenly change,” said Chevillard.

**Brussels aiming for swift adoption**

The European Parliament and EU countries will now examine the proposal with the objective of reaching agreement in the autumn.

“We would certainly hope that the co-legislators would come to an agreement rapidly, ideally before next winter” so that the measures are already in place for the next heating season, the Commission official said.

This could put EU countries at odds, with Paris pushing for a swift review and Berlin preferring to delay the overhaul until after the European elections in Spring 2024.
The European Commission “hit a political sweet spot” by allowing more nationalisation of electricity markets in its reform proposal tabled last week, according to Georg Zachmann. However, the focus on long-term contracts risks locking some EU countries into costly deals that will make the green transition more expensive, he warns in an interview.

Georg Zachmann is a senior fellow at the Bruegel economic policy think-tank, focusing on energy and climate policy.

INTERVIEW HIGHLIGHTS:

- The focus on long-term contracts is the main novelty of the European Commission’s proposed reform of EU electricity market rules, presented on 14 March.

- However, the proposal risks deepening inequalities, as some EU countries have less credibility on financial markets and will find it more difficult to secure long-term contracts with investors.

- Governments in these countries could come under pressure to commit to very high electricity prices for the next 20 years.
Another issue is that long-term instruments do not ensure coordination of cross-border investments, leading to sub-optimal allocation of energy assets at the European level.

The proliferation of national remuneration schemes also lacks a European dimension to ensure decisions in one country do not negatively affect others.

For consumers, the renewed focus on fixed-price contracts may have unintended consequences by prompting greater concentration among energy retailers, which could push prices up.

Who are the winners and losers of the EU's electricity market reform, presented by the European Commission on 14 March?

Consumer protection was the dominant narrative pushed forward by the European Commission.

But the big news for me is Article 19 of the directive, which talks about investment instruments and long-term contracts, for which no direct European framework existed before.

In the past, the hope was to unify the EU's internal market with electricity-only markets. Now, the Commission essentially formalises that member states can support the technologies of their liking with long-term contracts that are backed by the state – be them Contracts for Difference (CfDs), Power Purchase Agreements (PPAs) with state guarantees, or forward contracts that energy market operators might now be obliged to buy and sell.

Did this come as a recognition that short-term markets were too volatile and did not deliver the investments needed for the green transition, which requires long-term price signals?

That is fair to say, yes. The Commission's analysis is that we didn't develop the long-term markets that were meant to protect consumers and secure investments. And therefore, the Commission realised it had to do something.

Now, on a national level we had a lot of instruments such as capacity mechanisms or support schemes for renewable energies. In Germany, there are network and capacity reserves, which are pseudo capacity mechanisms. And in France, the ARENH regulates the price EDF obtained for much of its nuclear electricity output.

So member states already did have a wide array of idiosyncratic long-term contracts. And the ideal in the past was to get rid of that through the European short-term markets on which specific financial instruments would be built, in order to deliver investments for the long-term.

Now, the desire of member states to do this themselves essentially prevailed. And the Commission has acknowledged this. So that is for me the paradigm shift – the door is opened for ultimately handing the responsibility for delivering long-term investment signals to the member states.

Do you think this focus on long-term contracts will eventually reduce the volatility in electricity prices?

This will depend on the details of how it’s going to be implemented. The Commission has made those tools available and every member state can play with them.

But it also made clear that those long-term contracts – CfDs and state guarantees for PPAs – will need to be vetted by the Commission’s competition authority.

You have argued that the Commission’s proposed reform is a quick fix that does not really address the underlying issues with the EU electricity market. Can you explain why? And when will a new reform be needed in your view?

The big issue is getting substantially higher investments into electricity supply. My big worry is that some EU countries will find it more difficult than others to roll-out those state-backed contracts, because they have less credibility on financial markets.

We might for example see issues with subscription to those contracts in some countries, where investors will doubt the ability of the state to provide financial guarantees over a 20-year period.

Those governments could therefore come under pressure from investors to sign long-term contracts where they commit to very high electricity prices for the next 20 years. Eventually, governments may find this unaffordable, meaning investments risk not being made at all.

Now, if the transition gets expensive, if we lock in investments at high prices, we will have to live with this problem for decades to come.

Do you see other potential
issues with long-term contracts?

Another issue is that long-term instruments do not necessarily deliver the products we need to decarbonise the electricity system on a European level.

In a decarbonised electricity system, power prices will be very low for 70-80% of the year because renewables will run at full speed. And the remaining 30% of the time, you will have rather high prices because you need to curtail demand or run your hydrogen plants.

However, too simplistic long-term contracts only remunerate the production of bulk electricity – the amounts of kilowatt-hours being produced. Then investments are going first to wind capacity in some scarcely populated windy regions, or in sunny regions where a maximum of kilowatt-hours can be produced at lowest cost.

But this may not be suitable to cover electricity demand when and where it is most needed. This is why more cooperation between member states is needed – to ensure coordination within the power system.

That in the past has been delivered by the short-term markets, at least to some degree. If you now take away this coordination function away from short-term markets, it means you will have to do it elsewhere. And for the moment, it’s not clear who or what is going to fulfil that essential role.

This is why I believe another reform will be needed at some point: to ensure cross-border coordination of power system investment.

Cross-border cooperation was already an issue when the last power market reform took place in 2018: interconnectors were being utilised at around 30% of their capacity because transmission system operators essentially do not really trust each other... Has this changed?

With the energy crisis, EU countries have realised the value of cross-border cooperation. France, for instance, was essentially supplied by the rest of Europe last year when its nuclear reactors experienced widespread failures, whereas it was a net exporter of electricity the years before.

The Commission didn’t acknowledge the French situation in its electricity market reform and only referred to the Russian aggression against Ukraine, which I find interesting in terms of narrative.

More broadly, getting the right co-dimensioning between infrastructure and generation across 27 countries is like five-dimensional chess – there are many parameters to consider.

To manage this complexity, I believe the EU needs some sort of European electricity system modelling – something that is done by an independent EU agency, not the national Transmission System Operators (TSOs) like it is done now. This would allow checking what the member states are proposing and have some sort of benchmark to understand whether we are on the right track or not.

And currently, we don't have that. The US has a public energy data and modelling agency, the Energy Information Administration, and I think Europe should have one too. At the moment, we are more and more outsourcing energy analytics to the International Energy Agency (IEA), which is doing a great job. But a sovereign Europe might at some point want to rely on an EU institution in such a strategic policy area.

Doing this would require a federalist leap forward, giving away more national powers to the European level, no?

Implicitly, it would be a push for a more coordinated approach. But constitutionally, it would not require changes to the way competences are shared between the EU and the member states – I don’t think it would require changing Article 194 of the EU treaty, for example.

And some of the provisions are in fact already there – the Commission is empowered to check the National Energy and Climate Plans put forward by the member states, for example. The Agency for the Cooperation of Energy Regulators (ACER) is also empowered to check what the TSOs are proposing.

The only problem is that they don’t have the tools to conduct those checks. And so, we should give them the tools, it would be a relatively soft and low-cost approach to get to a more consistent system.

Doing this will make it more explicit that there is an EU aspect to energy infrastructure planning. But I think we need to make those things explicit and discuss them.

If the result of the discussion is that we allow the French to...
build an electricity system relying on nuclear for 80% or 90%, then so be it. But at least we should understand what it means for the neighbouring electricity systems that are connected with France and how we can ensure a low-cost and efficient system complementing national policy choices.

The European Commission placed a lot of emphasis on consumer rights in its proposal, with more options to choose fixed price contracts for electricity and a new right for consumers to share self-generated electricity. Do you think this is a step in the right direction?

It sounds good in principle but there might be unintended consequences.

For instance, if EU regulators force retailers to offer fixed price contracts to consumers or forces them to formally hedge their portfolios, will it make electricity cheaper or more expensive?

Not all retailers will be able to do that. So it will force them to become bigger to be able to hedge their positions. With fewer, bigger players, will consumers benefit? Or will that lead to a situation where energy retailers become more systemic? It’s not clear at this stage.

My fear is that retailers will find it difficult to hedge against the variability of renewable power generation. Because currently there are no liquid hedging-products out there guaranteeing that consumers will get electricity even in the hours when the wind is not blowing or the sun is not shining.

And that’s the kind of product consumers would need in a system where renewables become the dominant form of electricity. Because, as a retailer, it’s easy to buy a PPA from large wind and solar developers. But when they are not producing, all your customers with solar panels on their roof are calling for a lot electricity because they are not producing themselves. And during those hours, electricity is going to be super expensive.

This is a double problem and the corresponding hedging products still need to be developed to ensure consumers get electricity at all times. This is a gap that needs to be filled, either by regulators or the market. But it’s clear to me that such products will be needed.

About consumers’ right to share energy, do you believe this will help lower prices?

The right to share energy is a good idea in principle but it also raises new issues.

If the two of us share electricity because you have a solar panel and I have a battery, that allows us to buy less electricity from the grid. And potentially, that could mean that we stop paying for grid services.

But in case the solar panel does not produce for some weeks – in winter for example – we will have to draw electricity from the grid.
instead. And then somebody else that doesn't have solar panels will have to pay grid services for us during the rest of the year.

So we need to be careful with these energy sharing services, to make sure they don't have negative distributional consequences for people who are unable to afford a solar panel or a battery.

**One of the objectives of the reform was to introduce more 'flexibility' in the market by requesting EU countries to define national objectives for demand-side response and storage. What are your views on this?**

There is no doubt that the electricity system needs more flexibility – be it demand-response, storage, grids or more flexible generation units.

What’s not clear in the Commission proposal is how to prioritise these options and ensure the cheapest are selected in an optimal way. Member states are essentially asked to tick boxes and install certain amounts of flexibility assets in a very simplistic way that is not optimised as a portfolio of systems.

And my take is that this can be substantially more expensive. Now, I cannot prove it because I haven't modelled it myself. But I think the Commission should model it, actually.

**This is linked to the broader question of remunerating those flexibility services, whatever they may be. Has this been addressed?**

There are different types of remunerations schemes – the wholesale market, capacity mechanisms, flexibility mechanisms, etc. Then you might have Contracts for Difference (CfDs) and guarantees for PPAs which come on top of this.

This means power plants sometimes get three to five different cash flows, which they optimise internally. But does this lead to an optimal power plant park at European level? If every member state does it differently and cross-border trade is free, that makes the whole electricity system extremely complex.

And at the moment, there is no consistent picture at European level of how the electricity system should look like.

**Do you think more harmonisation is needed on national remuneration schemes?**

Not necessarily. Regulators could leave remuneration schemes largely up to EU member states knowing that, in the end, there is some sort of kind of catch-all European instrument that acts like a like a rubber band and pulls it all together.

What’s missing is a European mechanism to ensure that remuneration schemes decided at national level do not create problems elsewhere. And that question is left unaddressed in the Commission’s proposal.

**One of the novelties in the Commission proposal is a new ability for TSOs to introduce ‘peak-shaving’ products on the market to decrease electricity consumption at peak hours. Do you think this is a good idea?**

Variable electricity tariffs are already commonplace, for example to incentivise night-time consumption.

The challenge is when these pricing mechanisms overlap with existing ones. In normal conditions, the electricity-only market should provide extremely high prices in times of scarcity, which is supposed to incentivise peak shaving.

Now, if you introduce special peak-shaving products, you might end up depressing the wholesale market substantially, thereby reducing incentives to build those flexibility resources.

In the end, the wholesale market might be more efficient at providing those services. So, the added-value of creating a new peak-shaving product needs to be clarified. Why create something new when the wholesale market already does it?

**A key aspect of the Commission’s reform proposal is to encourage long-term contracts like Power Purchase Agreements (PPAs) and Contracts for Difference (CfDs). Do you believe this is something that will reduce price volatility?**

Short-term price volatility is a good thing because price spikes send a signal to market players that they should consume less or produce more.

What we don't want is this short-term volatility to be reflected in household energy bills. And here, fixed-price contracts for the bulk of household consumption are a step in that direction.

Now, long-term contracts
between generators and large buyers of electricity might help lowering prices if they lead to more investment in new generation capacity. So, in that sense, they could make a positive contribution.

**Two-way CfDs are now becoming the norm whenever state support is involved. Does that mean the end of Germany’s feed-in tariff for renewables? And the end of the regulated price of historical nuclear power in France, the ARENH?**

I don’t believe this would be a big thing in Germany. The country has a floating premium system, which is pretty similar to a CfD.

In France, the ARENH – which establishes a selling price for legacy nuclear output – is supposed to run out in 2025. And the CfDs could fulfil a similar function, so I don’t see this as a big issue either.

My sense is that politics will prevail anyway. Nobody in Brussels will be crazy enough to tell the French they cannot repair their nuclear power plants.

**One open question with the CfDs is how the money potentially collected from energy suppliers will be used. The Commission said the surplus money will need to be “channelled back to all consumers equally according to their consumption” but they did not say more than that. What are the options for redistributing that money?**

My main concern about CfDs is not how to use the surplus money. My worry is that the CfDs that we sign now risk looking extremely expensive a few years down the road when renewables start cannibalising themselves by lowering electricity prices in the hours when they are producing. I wonder what people will say in 2030 about this.

Regarding the surplus money collected from CfDs, the big question is whether it should be targeted at specific consumer groups. Every member state has their own preferences – Germany for instance wants to introduce a special industrial power tariff, others might want to support vulnerable households, etc.

My understanding of the Commission proposal is that the money will have to be redistributed back to consumers in proportion to their consumption. So if the price of electricity is €0.5 per kilowatt hour and the contract is €0.7/kWh, then €20 goes to everybody per megawatt hour.

**In a country like France, could a public company like EDF use this money to finance further investments into nuclear or renewables?**

This is a question for lawyers, I believe.

**What is the least known aspect of this reform that has been overlooked by commentators and deserves more attention?**

When I spoke to industry, some were concerned about the creation of regional hubs for forward markets. The good element is that this encourages cross-border trading for example by allowing a French energy retailer to hedge its portfolio by buying transmission rights for solar power coming from Spain three years in advance.

And as electricity will become the main form of energy in Europe, a liquid asset representing “European electricity” might serve hedging needs at a more macro-economic level. But some in the industry seem not too happy with this Commission proposal, saying it is impeded by physical constraints.

**Are these the regional trading hubs that the Commission always wanted to create and would this be a step towards a more Europeanised electricity system like the one you have called for?**

The direction looks very good. But, as always, the devil is in the detail. Last year for instance, Uniper lost a lot of money because they hedged their German products with Nordic electricity that they weren’t able to bring over because of congestion. So, these topics need to be dealt with.

**Do you believe there is a chance that this reform can be concluded before the winter of 2023-2024, as the Commission wants?**

The proposal did not trigger a huge outcry from member states, which is a sign that things could be concluded rapidly.

**Countries like France and Spain, which had initially called for a decoupling of gas prices from electricity spot prices did not complain. And Nordic countries are not unhappy either because the reform doesn’t go too far.**

So, it seems the Commission managed to hit a political sweet spot by essentially allowing more nationalisation of electricity markets.
Spain aims for electricity market reform deal during EU Council stint

By Frédéric Simon | EURACTIV.com

Languages: Deutsch

Spain will seek a deal on the EU’s proposed power market reform during its six-month EU Council presidency ending on 31 December, a less hurried timetable than that of the European Commission.

“I guess we should reach a political agreement during the Spanish Presidency by the end of the year,” said Teresa Ribera, Spain’s minister for ecological transition, at an event organised last week (28 March) by the Financial Times newspaper.

Ribera’s comments came after a meeting of the EU’s Energy Council in Brussels where the bloc’s 27 energy ministers debated the European Commission’s proposed electricity market reform presented two weeks before.

The Commission’s proposal seeks to lower electricity bills, which went through the roof last summer after Moscow turned off gas supplies to Europe in retaliation for sanctions imposed on Russia for its military aggression in Ukraine.

As part of the EU’s response, Brussels tabled a reform of electricity market rules that placed greater emphasis on long-term contracts with renewable energy producers, a move aimed at providing guaranteed revenues for investors and more stable prices for consumers.

“The current framework gives too much weight and importance to short-term markets,” which are “volatile by definition”, Energy Commissioner Kadri Simson, who opened the event with a video address, said.

Brussels wants new EU rules ‘in place before the winter’

The Commission is currently pushing for a rapid approval of the reform by the European Parliament and EU member states in the Council of Ministers.

The objective is to have the new rules “in place before the winter,” Simson said after last week’s Energy Council meeting, adding that she expected “a general
approach” among EU countries to be agreed upon during the Swedish Presidency, which ends on 30 June.

But Ribera appeared less hurried on the timeline, saying she expected “a political agreement during the Spanish Presidency by the end of the year”, so that the new EU rules are in place in 2024 during the Belgian Presidency, ahead of the 2024 European Parliament elections.

Indeed, Ribera said Madrid would seek a deeper reform than what was contained in the Commission’s proposal, something that may require more time to agree on.

“We need to go much faster and much deeper than what we have on the table right now,” she told the Financial Times event, which was supported by Polish energy utility PGE. For instance, “there are things that are still missing” in the current electricity system, she said, citing the need to “build a business case” for solutions like demand-side management and storage of electricity.

“Of course we need to create a business case for storage,” Ribera said, citing batteries and pumped hydro as examples. “And I think this is what the European legislation should be addressing in this market design directive.”

Europe also needs a more coordinated approach when it comes to protecting vulnerable consumers in times of crisis, the Spanish minister argued, noting that EU countries do not all have the budgetary capacity to do this.

“We cannot rely just on the fiscal space of each member state. Because that would mean there are some member states where citizens and SMEs can be covered and others not,” she said.

**Worries about finance**

Concerns about financial restraints are also prevalent in Poland.

Last year, European Union countries including Poland introduced emergency measures to put a ceiling on electricity prices and tax the revenues generated above the cap by energy companies because of soaring gas prices.

That is causing concern for PGE, which estimates the investment gap in Poland at around €90 billion until 2030 – mainly in new renewable energy facilities.

“Squeezing the revenues of energy companies is maybe not the right choice from our perspective,” said Wanda Buk, vice president for regulatory affairs at PGE.

WindEurope, a trade association, is also a big critic of the electricity price caps that have sprouted across EU countries since the beginning of the crisis. According to the trade association, investments last year were severely hampered by the price caps, combined with soaring inflation and regulatory hurdles.

“There was not a single final investment decision in any normal-sized offshore wind farm in Europe for 15 months until last week,” said Giles Dickson, the CEO of WindEurope.

“Europe has become an unattractive place to invest in renewables – especially in offshore wind, which are big-ticket items,” Dickson argued, saying “investors have been scared away” by uncoordinated interventions on national electricity markets.

‘Please don’t mess it up’

Dickson praised the Commission’s power market reform proposal for scrapping the national revenue caps, saying the move “will bring investors back to Europe” and “send the right signals to investors”.

“Please don’t mess it up in the Council and the Parliament,” he pleaded, urging policymakers to adopt the Commission proposal with as little change as possible.

Buk also praised the Commission’s power market reform, saying the proposal was “narrow enough to address the challenges of the last 16 months” while promoting long-term contracts to address current market failures.

Still, she said PGE was looking for flexible power generation capacity to back up its growing fleet of renewable energy plants and upcoming nuclear reactors.

“There are companies in Poland that are asking themselves very seriously whether this is the moment to invest into gas capacities that will have a lock-in effect” on the country’s energy mix for the next 30-40 years, Buk said.

But if the EU’s reformed electricity market excludes investments in new gas power plants, then Poland will have no alternative but to keep its coal plants running as backup, Buk said.

“This is the question mark that is still there. And it’s the elephant in the room.”
The context for this power market reform has been formed on one hand by the security concerns, and high energy prices on the other. Do you think that this proposal brings us closer to a more secure power system and lower prices?

Wojciech Dąbrowski is the CEO, PGE Polska Grupa Energetyczna

The Commission has proposed a dozen of measures that are working in at least some of the EU member states. For example, two-way contracts for difference (CfDs) will provide financing for our offshore wind farms in Poland. This instrument, together with PPAs can contribute to lowering prices, but only in the long run.

In the short term, we need to ensure a timely delivery of our renewable projects pipeline as they are key in ensuring affordable and secure electricity. To this end, CfDs signed before the market turmoil and the war in Ukraine started should be adjusted to reality. For example, it should be possible for their reference price to be
dynamically adjusted and indexed to change the market situation, where the costs of labour, capital, and manufacturing have been increasing at the fastest pace witnessed in the last couple of decades.

It will take time to develop PPA markets across the EU and to build new renewable and nuclear power plants. People in the Commission understand it very well, and I appreciate, that they remained immune to calls for a revolution in the EU power market. We need a well-functioning, fair market, that sends the right price signals to all market participants and ensures the security of supply.

Before the war, offshore wind development has been one of the fastest-growing and most strategic energy sectors in Europe. Since then, the investment climate has significantly deteriorated, which calls for urgent action from the Commission to facilitate the timely delivery of projects. Especially because the Baltic region’s commitment in the Marienborg Declaration to achieve ca. 20 GW of installed capacity in offshore wind energy by 2030 will require speeding up the development of new projects, as currently the total installed offshore wind capacity on the Baltic Sea is ca. 2.8 GW.

With a potential of at least 7.1 GW of offshore wind projects, PGE can certainly play an important regional role in ensuring Europe’s security of supply. But, to make this happen we need to be working hand in hand with the Commission. These projects are not only capital-intensive but also require strengthened grids. As lowering the electricity bills for consumers becomes more important than ever before we need to look at the transition costs from the holistic system perspective. This is why we believe that the excess profits from CfDs above the reference price should be redirected to finance renewables, storage, and grid development, which is necessary to enable faster deployment of renewables.

With such an ambitious strategy, what is the main obstacle to faster deployment of renewables?

For example, technical limitations of the grid are the single biggest reason behind the number of refusals to connect renewable installations in Poland, and the number is on the rise: in 2017/18 all grid network operators made more than 200 refusal decisions, in 2021/22 nearly 3,500. Even if almost all of them are related to the PV photovoltaics boom, in most recent months almost 80% of the applications are being refused due to technical limitations of the grid. In total, between 2015 and 2021, operators issued more than 6,000 refusals to connect to the grid installations with a total capacity of 30 GW. This represents almost half of the currently installed generation capacity of all types of sources in Poland.

If technical difficulties to integrate renewables into the grid prevail, the outdated transmission and distribution infrastructure will remain the biggest barrier to accelerated renewables development so the investment incentives here should come from the adequate market design. This is why we call on policymakers to ensure a stable regulatory framework for distribution grids, which guarantees a satisfactory rate of return on grid modernisation and reinforcement investments.

So what should the Parliament and the Council do with this proposal in your opinion?

First of all we need to ensure, that neither PPAs nor CfDs are transformed by co-legislators into a regulated mandatory instrument that aims first of all to cap revenues of renewable and low-carbon generators, because this would significantly limit investments in the green transition. And by the way, there is not much about the “security of supply” issue in the Commission’s proposal. To a certain extent, the so-called “non-fossil flexibility” services will contribute to the grid stability, but here the Commission’s main intention is to cut prices. We agree, that it makes sense to develop flexibility markets based on demand side response and storage. We understand the Commission’s intention to incentivise this kind of flexibility service to cut the consumption of gas. Nevertheless, DSR and storage is not sufficient to secure an electricity supply, with several weeks in January with very low production from PVs and wind farms. My point is that the electricity market design has to address also investments in and operation of dispatchable generation. Simplified and flexible rules that would allow to prolong the current capacity markets and create new ones in these countries that are interested, would improve the security of supply in the EU.

If implemented in the proposed shape, what would this reform mean for companies like PGE? Will it...
make your decarbonisation plans easier and faster to implement, or maybe the contrary is true?

PGE is the major producer of power and heat in Poland. We are eager to engage in the development of PPAs, we already implement very ambitious offshore wind plans, and our distribution company is a co-author of the Polish rooftop solar revolution. This reform can further empower customers with ideas like “energy sharing”, but we need to remember, that in the power system, a balance is inevitable. Not only between supply and demand, but also between the development of generation and development of grid, and between the rights of suppliers and the rights of consumers. CfDs are a good direction is that contracts for difference are to be voluntary, it will be up to the MS to decide whether to use them. The inclusion of nuclear power is also positive.

However, we are against transferring CfD-based revenues to all customers based on their electricity consumption, since this solution is counterproductive in terms of generating price signals for reducing consumption in peak hours. The price agreed in CfDs should be responsive to overall macroeconomic changes. The provision of obligatory CfDs for new RES installations lacks any capacity threshold, which might create difficulties with potential CfDs application for small installations. Also, the relation of the new CfDs provisions to the existing regulatory framework (especially RED and State-aid rules) should be clarified.

Finally, we have some reservations when it comes to mandatory financial hedging for energy suppliers as it is not the only solution to ensure the financial stability of these entities. The introduction of mandatory collateral, in particular with the obligation to use one specific instrument, may negatively affect the competitiveness of energy suppliers and their ability to manage resources and plan investments efficiently. The reduced competition also negatively affects end users and may reduce market liquidity. The introduction of Virtual Hubs in the proposed form for trading on the markets may disrupt long-term markets without solving liquidity problems. It increases risks associated with long-term hedging and its costs.

Some of the commentators lamented, that with the Commission’s proposal, the inframarginal generators would continue to obtain excessive rents in cases of price crises – what is your response to this kind of argument?

This is a popular misunderstanding. The fact is that the revenues of the power generators have significantly increased last year, but our net profit in 2022 decreased by 16% and EBITDA decreased by 9%. The money paid for expensive electricity bills was not transferred to our pockets, it went to fuel producers and to the EU ETS system. Last year we spent more than EUR 4.2 billion on carbon allowances, more than twice the amount from the previous year. This is not a favourable environment for the accelerated deployment of renewables, which the Commission formally promotes. We are committed to building 3 GW of PVs, 2.5 GW of offshore wind farms, and 1 GW of onshore wind farms by 2030. Therefore, we need a fair, well-functioning power market to finance these plans, any sort of revenue cap can ruin it. I hope, that all stakeholders want companies like ours to invest more in renewables, not less.