The European Commission wants to reform “capacity mechanisms” put in place across EU member states to remunerate power plants that remain on standby in case of a demand peak, arguing they distort the market. But views differ on their value amid wide-ranging national disparities.

In this Special Report, we take a look at the situations in France, Spain and Italy where EURACTIV held a series of policy workshops dedicated to the proposed reform.
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The European Commission is trying to limit the development of so-called capacity mechanisms, which some member states have put in place as a way of ensuring electricity supply in situations of peak demand.

While the EU has come to a compromise on renewable energies on 13 June, setting the target for renewable energy at 32% by 2030, negotiations on the rest of the clean energy package are still ongoing.

The revision of the electricity market directive is at the centre of heated debates with the sensitive issue of capacity mechanisms taking centre stage.

These mechanisms consist of remunerating power generators for their “availability” to produce. Like an insurance policy, power generators commit themselves to produce a certain amount of electricity in case of need and obtain remuneration in return – even if they remain on standby.

This represents an additional financial resource and makes it possible to retain otherwise unprofitable power plants to cope with potential demand peaks. Some operators may also be compensated for their “load management capacity” – that is, their ability to save electricity in times of high demand.

Defended by several countries as a means to promote the security of electricity supply, these mechanisms do not fit well with the liberal approach of the European Commission. Capacity mechanisms take the form of public intervention that the Commission sees as a threat to competition.

In some countries like France, capacity mechanisms are market based, which raises concerns in the Commission over the establishment of national markets at the expense of a single European market.

The Commission has therefore defined obligations for Member States wishing to introduce such mechanisms, including the need to

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prove their necessity to guarantee the security of electricity supply in their country.

**TOWARDS A EUROPEAN CAPACITY MARKET?**

Last February, the Commission seemed to soften its stance by giving a green light to six capacity mechanisms – in Germany, Belgium, France, Greece, Italy and Poland.

Nevertheless, it remains firm on the European dimension that these mechanisms will have to comply with. The Commission therefore proposes in its new clean energy package for this need to be proven by means of a Europe-wide capacity assessment study, taking into account electricity supplies from other Member States.

"France is not acting alone," said Oliver Koch, head of unit at the European Commission’s Directorate-General for Energy, at an event organised by EURACTIV on the subject on 14 June. "[France’s] system is highly integrated in a European network with many interconnections," Koch underlined.

In order to accept the capacity mechanisms, the Commission requires them to be open to other Member States, which must be able to participate.

"In accordance with the European guidelines, more and more states are integrating the possibility of cross-border cooperation into their capacity mechanisms," said Colas Chabanne, Electrical Systems Director at RTE, France's electrical grid operator.

"This is a step towards building a European electricity sector: national capacity mechanisms first, with cross-border cooperation freeing the way for a gradual Europeanisation of the system," Chabanne said.

Nevertheless there is scepticism about this "Europeanisation" because the aim of capacity mechanisms – security of electricity supply – remains a member states prerogative.

"Each Member State is responsible for its supply," said Maciej Burny, Secretary General of the Polish Electricity Association.

"There was the equivalent of a total blackout last summer in Poland. And believe me nobody wanted to share responsibility for what happened in economic and social terms. We had to face these difficulties alone," Burny said.

CONTROVERSIAL ENVIRONMENTAL STANDARD

"Although we have reduced the share of coal and lignite in our consumption by 20% in recent years, most of our capacity still depends on these resources," Burny pleaded.

Poland, like other European countries still heavily dependent on fossil fuels, is concerned about another provision in the clean energy package, which would prevent plants emitting more than 550 grams of CO2 per kWh from participating in capacity mechanisms.

According to a study conducted by Compass Lexecon for the Polish electricity association, the measure could represent an additional cost for Polish consumers, because of the closure of some coal-fired power plants which, without qualifying for the capacity mechanisms, would be not profitable.

The association is considering natural gas as an alternative resource to generate electricity, which would require the development of new infrastructure or imports which would represent an additional cost.
So-called “capacity mechanisms” are being set up across EU member states to remunerate power stations that remain on standby in case of demand peak. While a European framework is needed to regulate those schemes, Fabien Roques believes they should be adapted to local circumstances.

Fabien Roques is the Executive Vice President of Compass Lexecon Consulting. He is an expert on energy and environmental issues, and an associate professor at the University of Paris Dauphine.

The European Commission wants to tighten obligations on member states which put in place so-called “capacity mechanisms” for electricity. Why is the Commission so wary of these mechanisms?

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The European Commission must ensure that capacity mechanisms do not hinder competition in the European electricity market.

However, capacity mechanisms are designed to ensure the security of energy supplies in each country; they must be adapted to the situation in each of them. Consequently there needs to be national solutions, a single European model won’t work.

**There are different models in Europe...**

Indeed, not all European countries follow the same model. France, Italy, Poland and the UK have opted for capacity markets.

In France for example, energy suppliers have to possess sufficient capacity certificates to cover the increased demand of their clients as well as a security margin, in order to operate on the market. These certificates are sold by power suppliers and load management operators, which must have the certificates delivered by the French national grid operator RTE.

In Greece, Spain and Portugal power suppliers receive capacity grants. While Germany, some Nordic countries and Belgium rely on strategic reserves: the grid operator signs agreements with load management plants outside the market, to make sure that they are available in the event of power shortages.

**Given the diversity of national schemes, what is the prospect of developing a European mechanism?**

For now, the European dimension for capacity mechanisms is limited to the possibility of cross-border cooperation, so that power plants or/and load management facilities can play a role directly or indirectly in neighbouring countries’ capacity mechanisms.

The establishment of a real European capacity mechanism would require solidarity at the European level, and would need a political agreement allowing for, in a worst case scenario, the possibility of power cuts in one state to ensure supplies in another one.

**Beyond the risks for competition which you mentioned earlier, the European Commission has expressed doubt that such mechanisms are necessary in all circumstances to ensure security of electricity supply. Have national mechanisms proven their worth?**

In Europe we have little to go on since these mechanisms have been put into place only recently. The only conclusion we can draw for the time being is that these mechanisms are still being adapted and can be improved upon.

In France, where the mechanism was introduced three years ago, it made it possible for certain plants to remain in operation. This has helped to secure the system and to cope with peaks in electricity consumption.

However, the capacity market has yet to give positive signals, particularly on long-term investment. Long-term contracts are therefore being considered which would provide more visibility to operators and encourage investment in new generating capacity.

**The European Commission wants an environmental clause banning power stations which emit more than 550 grams of CO₂ per kWh from taking part in capacity schemes. What do you think of this?**

The main problem with this rule is that the Commission is trying to kill two birds with one stone, by trying to limit greenhouse gas emissions, while at the same time securing electricity supplies in one go.

Economically, it would be more effective to use two different tools, and in particular the European carbon market.

This rule could prevent some power plants from being part of capacity mechanisms, therefore making them less profitable and forcing them out of the market. This might involve making new investments which could increase the costs for consumers in order to secure the system. I’m talking about peak-lopping plants, which only generate electricity during peaks in consumption. Consequently they produce higher emissions but over a shorter period.

Ultimately, if these plants are no longer profitable and close down, they will have to be replaced by new capacities, which will involve additional costs.
The ongoing reform of “capacity markets” for electricity, which remunerate power plants for remaining on standby in case of demand peak, should be technologically neutral in order to allow disruptive technologies like digitalisation and blockchain to develop, argue energy experts from across Europe.

In February, the European Commission approved six so-called electricity capacity mechanisms to ensure security of supply in Belgium, France, Germany, Greece, Italy and Poland.

Italy and Poland have market-wide capacity mechanisms, Belgium and Germany opted for strategic reserves and France and Greece chose capacity mechanisms specifically promoting demand response.

Each mechanism is meant to address the specific needs of each member state: in the French case, 70% of electricity supply relies on nuclear energy, while Polish and German supplies rely on coal plants.

Two weeks after the EU executive granted its blessing, the European Parliament’s industry and energy committee (ITRE) voted in favour of strict rules for capacity mechanisms in general, which will no longer be eligible for subsidies as of 2020 for new infrastructure and as of 2025 for existing plants.

The Commission’s proposal for a limit of 550g of CO2/kWh has also been tightened further by the Parliament.

“The Parliament’s proposal is a bureaucratic compromise,” said Frank Umbach, research director at King’s College London’s European Centre for Energy and Resource Security (EUCERS), at a EURACTIV event held in Rome.

Umbach added that “it is not in line

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with the original objectives and may create difficulties to existing capacity mechanisms”, particularly the Polish system.

THE ROLE OF NEW TECHNOLOGIES

In a long-term perspective, Umbach added, many disruptive technologies, including digitalisation, blockchain, robotics and artificial intelligence, will radically change business and strategic models.

These new technologies will test future energy models which is why the final compromise on the EU text should be technologically neutral, he argued.

EU talks should focus on capacity markets in the short and mid-term, Umbach insisted, but should also assess the potential long-term impact of these new business models.

PARLIAMENT’S PROPOSAL AND POLISH SUPPLY SECURITY

Poland implemented a capacity market mechanism because it needed it to ensure security of supply, said Filip Grzegorczyk, vice president of the Polish Electricity Association (PKEE).

“What’s important is to focus on the progress we made: in 1990 Poland got 99% of its energy from coal plants, now it’s 80% from coal and 15% from renewable energies. According to our estimates, in 2030 we’ll have 40% renewables.”

He added that “those numbers clearly show that Poland’s capacity market supports renewable energy development”.

The mechanism will not cause higher electricity prices for consumers (between 50 cents and €2 a month in bills), Grzegorczyk insisted.

But the main criticism expressed by PKEE was directed at the so-called Emission Performance Standard (EPS), illustrated by the 550g of CO2/kWh limit.

The Commission, he said, approved the Polish mechanism aware that they were building a capacity market using coal and gas plants, adding that the 550g criterion actually excludes coal and prevents them from implementing it.

Under German pressure, the Parliament exempted “strategic reserves” from the EPS standard, assisting the “strategic reserve” model for lignite plants in Germany.

Critics claim that the Parliament has therefore privileged strategic reserves over capacity markets, despite the Commission’s traditional preference for the latter, which is more technologically-neutral and more market-oriented.

THE ITALY EFFECT

In the cases of Italy and Poland, the Commission has authorised market-wide capacity mechanisms. These can be necessary where electricity markets face structural security of supply problems.

Under a market-wide capacity mechanism, capacity providers can obtain a payment for being available to generate electricity or, in the case of demand response operators, for being available to reduce their electricity consumption.

Both Italy and Poland have clearly identified and quantified their security of supply risks, also taking into account possible imports from neighbouring countries.

Italy has demonstrated that there are a significant amount of capacity risks exiting the market, and new investments are unlikely to take place because investors cannot earn a sufficient return from their electricity sales. Similarly, Poland is faced with market failures that prevent prices from incentivising power generators to keep existing capacity in the market or to invest in new capacity.

Both mechanisms in Italy and Poland are open to all types of capacity providers, including demand response, existing and new capacities, domestic and foreign, Grzegorczyk argued.

These measures are meant to keep costs for consumers in check thanks to regular, competitive auctions to allocate capacity contracts. In parallel, both Italy and Poland committed to implementing reforms to the functioning of their electricity markets.

But while the Polish mechanism is already on track, Italy’s is in stand-by mode, waiting for approval from the ministry of economic development.

This has so far been hindered by a number of factors, including Italy’s political crisis and a weakened energy regulatory, warned Giulio Cicoletti of Elettricità Futura, Italy’s leading association representing the electricity industry.

“The Italian mechanism already provides a 10-year duration, as ongoing EU negotiations suggests,” he explained, adding that “capacity market development is crucial considering changes in the energy market like increased renewables use, new tech and changing consumer behaviours”.

Cicoletti insisted that a “solid energy system is capable of better tackling and anticipating those changes” but warned that Italy’s mechanism could risk being too complex.

Claudio Moscardini, of renewable energy firm Sorgenia, said that “it’s still difficult for industry and consumers to say if the capacity market is going to become a strength and not a weakness”, while hydroelectric expert Paolo Taglioli warned that Italy will have “make important and maybe radical decisions”.

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European Union negotiators will turn their attention to revamping the bloc’s electricity market rules under the Austrian Presidency but the issue of so-called capacity mechanisms continues to define the debate.

Filip Grzegorczyk is vice president of the Polish Electricity Association (PKEE).

He spoke to Agencia EFE / EURACTIV-Spain ahead of an EFEfórum Energy debate, supported by PKEE, held in Madrid.

**Why did you introduce a capacity market? Was it really necessary?**

Yes, it was absolutely necessary. It is predicted that in the following years there will be a 24% increase in energy consumption, so we really needed to introduce the capacity market, which is already notified to and accepted by the European Commission and is completely in tune with European rules. It is very important to have it.

**What is your opinion on the new EU legislation referring to the energy market?**

It is a difficult question. EU legislation on the electricity market is a complex set of rules. It is as if we were in a triangle: we have security, climate protection and the market. Our opinion is that the European Union is too interested in climate and not enough in security of supply, so that would be the disadvantage.

Regarding the latest legislation which is currently in process, the so called “Winter Package”, we have a lot of question marks here, due to the fact that the winter package has such a strong connection with the capacity market. We would like to achieve some derogations to make the capacity market work. If we don’t have this derogation, the capacity market will never work.

The most important element here is the EPS 550, that is the real problem. We cannot introduce this EPS 550 to the capacity market because it would

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create a non-working market. We think that we should be treated equally in the European Union, so if in the case of a strategic reserve in Germany this EPS 550 is not applied it should not apply to the Polish capacity market either, because the schemes are more or less the same. If the situation is the same we cannot be discriminated.

If the aim is to ensure energy security, wouldn’t it be more rational to concentrate efforts on supporting the development of renewables, especially the production from wind and the increase of interconnectors capacity?

At first hand, I would say that you are right, but the issue is that all renewable sources, especially wind, regardless of its offshore or onshore, need reliable backup and conventional sources. It is a kind of paradox, we have to develop conventional sources of energy to enable renewable sources of energy to be developed. Polish energy companies are leaders in the pace of transformation into renewable sources, but each time we talk about wind farms we still have to think of back-up. We really need this capacity market to be operating so we are able to develop renewable energy sources. The paradox is that we need to support the conventional energy sources, to develop renewable energy sources that are in tune with European guidelines.

What do you think is the perception of small and medium sized enterprises on the retail market on the costs of the capacity market?

We don’t estimate very high costs, but when we talk about costs we always have to ask ourselves, what would the alternative of a blackout be? Entreprises are quite aware of the fact that the cost of a capacity shortage would be much higher than additional payment for the functioning of capacity markets. That is why we think that this regulation will be well welcomed. If you want to be secured you need to pay for it. In general, I do not see any obstacle in the perception of small businesses.

Will the introduction of the capacity market eventually hinder the development of the internal energy market of the European Union?

I absolutely disagree. We already have some examples of capacity mechanisms in Europe. Everything we did in Poland, as far as capacity markets concern, was in tune with European guidelines. For example, we have a bid and interconnectors that allow everyone to take part in this system. We do not discriminate any type of energy, so its technological neutral. Everything is transparent and in tune with European rules. If we look at the European energy market as a combination of more than twenty domestic markets cooperating well that is absolutely okay in terms of EU rules.
Decarbonising the economy and energy production is now a necessity for states and companies, although it can also be a source of business opportunities and innovation, according to experts.

Spanish and foreign experts insisted at an EFEfórum Energy debate in June that member states must prioritise interconnectors, in order to leverage the potential of energy sources like renewables, as well as making sure the process is fully democratic.

Environmental director of EFE Arturo Larena pointed out the changes that decarbonisation will mean for society in general, a whole revolution from the economic, environmental and social point of view.

“Energy is a transversal topic, with implications in our everyday life and the way in which we produce and consume is going to go through a radical change in the following years,” he explained.

ENERGY TRANSITION MEASURES

All the participants referred to the set of clean energy laws, or Winter Package, initiated by the European Commission, although they disagreed about the different capacity of the Member States to implement them and the different speeds and level of awareness within the EU.

In this regard, EUCERS energy expert Frank Umbach declared that “we have to take into account how fast we should go, but also how fast we can go”, but added that the German model cannot be extrapolated to others and suffers from some weaknesses, one of them being transport networks.

Filip Grzegorczyk, vice president of Polish electricity association PKEE, continued on Page 13
underlined the effort that Poland has made to reduce the dependence on coal (it has gone from 99% to 80%) and acknowledged the need to decarbonise and promote renewable energies, but in a balanced and coherent way.

Endesa’s representative pointed out that companies are capable of producing renewable energy at a very competitive cost, but they still lack the “firmness and flexibility” that countries need. He added that it is still essential that other forms of energy, like thermal generation, act as “an insurance”.

**TRANSFORMATION**

Juan José Alba said that these options should be replaced “and we are able to see on the horizon some solutions, such as interconnections, however, they have a high cost”. He added that companies have often decided to keep “what we already have” even though renewable capacity is increasing.

Alba advocated for a “full” reorganisation of the tax and tariff system to avoid the current situation in which more than 50% of bills paid by the citizens are taxes, and also to penalise the use of the most polluting fuels.

“We are facing something that requires an enormous transformation and at the same time an enormous opportunity; this sector generates a lot of money, but this does not mean that the energy transition has to cost us money,” he explained.

Ferran Tarradellas, the Commission’s head of representation in Spain, recalled that Europe has a problem with external energy dependence that costs €40 billion each year and also spoke in favour of interconnections between member states.

**THE COST OF RENEWABLE ENERGY**

Renewable energy costs “have dropped down, because we know how to do them better than anyone else and because our continental nature allows us to join forces for common objectives with a higher chance of success”, he insisted.

According to the EU official, citizens must have access to information “in real time, of the real price” of electricity, to install cheaper consumer technologies or put their own generated energy on the network.

Tarradellas also emphasised the fact that the EU has to guarantee citizens “the right to consume, store, generate and sell their own energy without discriminatory prices”.

Cote Romero, founder of Ecooo, believes that the Winter Package is insufficient, “but it is a fabulous tool and far exceeds the objectives of many states” and widely “includes the directives of renewables and puts the focus on consumers”.

“Today we cannot deny the economic competitiveness of renewable energies, although an electricity market based solely on these energies needs the support of other types of energy,” he warned.
The EU’s decisions to approve state support for emergency power plants in France, Germany, Poland, Italy and Greece will all have to be revisited in light of the ongoing reform of European electricity market rules, the European Commission said on Tuesday (4 September), saying it won’t make an exception for Germany.

A February state aid ruling by the Commission said support for emergency power generation in Germany – chiefly coal-fired plants – “remains uninfluenced by the future rules on the design of the electricity market” that are currently being negotiated at EU level.

The sentence, buried in a footnote on p.20 of the EU decision, remained unnoticed until now because the full text of the decision was published after the February announcement by the EU executive.

This raised accusations of double standards by other countries like Poland, which were not offered equivalent safeguards.

In similar rulings for France, Belgium, Poland, Italy and Greece, the Commission indeed stipulated very clearly that state aid for back-up power generation “will need to be interpreted in the light of...legislation that has not been adopted yet at the time of this decision.”

The review of state aid decisions will focus “in particular” on future CO2 emission limits aimed at phasing out support for coal-fired power plants, which are blamed for global warming, the Commission added.

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CLARIFICATION

But the EU executive has now clarified that the German safeguard clause was “a mistake” that will soon be rectified.

“On the German decision, indeed, it’s a mistake which is in the process of being corrected,” said Christof Schoser, deputy head of unit at the Commission’s powerful competition directorate in charge of state aid controls.

“The state aid decisions will not shelter member states or companies from any future changes in legislation,” Schoser told a EURACTIV event on Tuesday (4 September).

As a general principle, state aid decisions do not protect countries from future changes in legislation, the official explained, saying “we did it on purpose not to pre-empt the ongoing legislative process.”

The announcement will come as a relief for Poland, which has complained of “double standards” in the ongoing reform of capacity markets for electricity because it left German coal plants largely off the hook.

Germany decided in 2015 to close eight lignite power plants and transfer them in a “strategic reserve” that can be used in case of emergency. Those plants are remunerated by the “capacity mechanism” which received EU clearance last February. But future funding for those back-up schemes could once again be thrown in the balance by the upcoming review.

Contacted by EURACTIV, the German EU representation in Brussels referred the matter to the competent ministry in Berlin, which declined to comment.

GRANDFATHERING CLAUSE UP FOR DISCUSSION

“Capacity mechanisms” are national schemes aimed at remunerating power plants that remain on stand-by in case of demand peak, typically in winter or when renewables aren’t available.

The Commission considers those as state aid and wants the schemes “Europeanised” with a cross-border dimension.

Ultimately, Brussels wants to phase them out completely, arguing capacity mechanisms distort the market and subsidise the most polluting form of electricity.

But that doesn’t mean state aid for coal will disappear any time soon. The EU’s upcoming electricity market reform might indeed grant a grandfathering clause to state aid decisions that have already been approved at EU level, Schoser pointed out.

“If the legislator wants to... protect certain contracts for a certain period of time, the legislator is free to do this,” Schoser said.

The point was echoed by Florian Ermacora, head of unit for wholesale electricity and gas markets at the Commission's energy directorate, who also spoke at the EURACTIV event.

“One of the big discussion points in the legislative context at the moment is the extent to which approved state aid for capacity mechanisms or projects are exempt from future legislation” – and in particular the upcoming CO2 standards for power plants, Ermacora said.

“That is quite a tricky issue,” he added, saying he wasn’t aware of a precedent in EU state aid policy, whether in the energy or other industrial sectors.

EMISSION PERFORMANCE STANDARD

The EU official was referring to a Commission plan to phase out state aid for power plants emitting more than 550g of CO2 per kilowatt hour – a proposal, which effectively rules out subsidies for coal as well as some inefficient gas power plants.

Poland is pushing hard to obtain “grandfathering” rights for EU state aid decisions in the ongoing reform of European electricity markets.

Power companies in Poland want to protect investments made in new generation coal-fired plants, saying they are needed to prevent blackouts at a time when old inefficient coal plants are being taken offline.

“The first point is to respect the decision” taken by the Commission,
which cleared the Polish capacity scheme in February this year, including the contracts concluded under the scheme, said Maciej Burny, Director for International Relations at Polish energy company PGE.

“These contracts have to be respected because they will be signed before” the EU market design reform is adopted, said Burny, who was speaking on behalf of PKEE, the Polish electricity trade association, which supported the EURACTIV event.

It’s a matter of “legal certainty” and “protection of rights acquired” for the companies involved, Burny explained, saying any changes brought to contracts passed under the Polish scheme would cause “economic harm” evaluated at “€6 billion.”

In addition, the Polish power sector wants “derogations for existing installations” that Burny said “should last ten years” in order to give sufficient time for Poland to adjust its energy mix.

**CARBON PRICE COULD MAKE CO2 LIMIT UNNECESSARY**

The Commission agrees that investors need legal certainty. “Of course, you have the question of investor trust from the past. But that is the case for any decision applying to industrial plants. So from that point of view, I’m not sure that the state aid approval means exemption from new legislation,” Ermacora said.

That point is still up for discussion as part of the market design reform that is currently being debated in the EU Council and Parliament, the EU official said.

In any case, Burny said that placing a CO2 limit on state aid to power will become unnecessary with a carbon price above €20 per tonne.

“If coal is the problem for Europe, then we have to make sure that the EU ETS is doing its job,” Burny said, referring to the EU Emissions Trading Scheme, which places a price on every tonne of CO2 emitted by industrial installations.

“The price of carbon is around €20 per tonne today. If somebody is rationally thinking about new investments in coal power generation with a price of €20 and possibly higher due to the reform of the EU ETS, then they probably don’t have realistic assumptions,” Burny said.

**COAL-TO-GAS SWITCH**

Moreover, Burny warned that excluding transition support for coal in Poland would create other problems, leading to a “70% increase in natural gas consumption in Poland by 2040”. This, he added, would mean “a huge change” for Poland, which would become dependent on gas imports coming mainly from Russia.

Environmentalists, for their part, are crying foul. “Polluters have had a free ride for way too long,” said Roland Joebstl, from the European Environmental Bureau (EEB), a coalition of green NGOs.

“The rules of the new market design regulation must be in line with the Paris Agreement and they must apply to everybody without exemptions or grandfathering,” he told EURACTIV.

“We are all in this together,” Joebstl added, referring to this summer’s extreme weather events.
The capacity market in Poland has a so-called “green bonus”, which allows a two-year extension of the multiannual capacity contracts provided that a 450 kg CO2/MWh emission performance standard is met, says Maciej Burny.

Maciej Burny is Director for International Relations for Polish energy company PGE. He spoke on behalf of PKEE, the Polish Electricity Association.

The European Commission wants to reform capacity markets, arguing they slow down the transition to clean electricity in countries like Poland, which are heavily reliant on coal.

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**However, the electricity sector in Poland has objected to the proposed reform. Why?**

First of all, we are not against a market reform as such. We see several opportunities in empowering consumers, codification of the EU state aid rules concerning the functioning of the capacity mechanisms, enhancing cooperation between DSOs and market-based renewables integration.

However, the revised Electricity Market Regulation should address not only future ambitions but the already existing pre-conditions as well. Therefore, we should find a fair balance between security of supply and environmental objectives. After a nearly two-year long notification process, the Commission has confirmed serious adequacy concerns which are expected to occur in the Polish energy system in the long-term perspective.

The adequate measure to address these concerns is a market-based and technology-neutral capacity market. Therefore, our concerns with the capacity markets reform are connected with three main issues.

- The first one is to treat all capacity mechanisms on equal basis – no exemptions and special treatment for strategic reserves in terms of the EPS 550 measure.
- The second key issue is to recognise the protection of the legitimate expectations, which means to exempt from the new Regulation contracts concluded before the entry into force of the new legislation.
- Last but not least, we would like to introduce an adequate transitional period for existing conventional assets – if the final investment decision was made before the entry into force of the Regulation an adequate 10-year transitional period should be applied. Our concerns are based on well-known legal principles such as non-discriminatory treatment of all capacity mechanisms and the legal certainty for investors.

Similar concerns were expressed by six other member states, namely: France, Italy, United Kingdom, Ireland, Hungary and Greece, which are applying various types of capacity mechanisms or are intending to do so. Thus, we are not the only ones, who see that further negotiations need to find a fair and balanced compromise.

**Are capacity markets in Poland designed to support coal power generation?**

The capacity market in Poland is designed in a technology-neutral, non-discriminatory way. The mechanism is open to all generation technologies, including Renewable Energy Sources (RES) and Demand-Side Response (DSR) technology.

Actually, technologies with lower emissions are given a preferential treatment. Due to our energy mix historically based on coal, support will also go to this form of generation to ensure security of supply, but we should avoid a stereotype that this mechanism is a subsidy dedicated to coal.

**Can capacity markets in Poland help reduce greenhouse gas emissions?**

One of the key principles of the Polish capacity market design is to incentivise investments in new low-emission capacity. This is implemented not only by the OCGT-based benchmark, but also by the so-called “green bonus”. This “green bonus” allows a two-year extension of the multiannual capacity contract provided that a 450 kg CO2/MWh emission performance standard is met.

This means that under the Polish capacity market, there is an additional incentive to invest in low-emitting assets such as the most efficient combined-cycle gas turbines (CCGT) power plants and renewables. This is why the capacity market in Poland provides energy utilities with funds to facilitate a smooth low-emission transition.

**The Commission wants to encourage cross-border trade and electricity interconnections, saying more power trading will prevent countries from building unnecessary additional capacity. Does the Polish electricity sector support this objective?**

In principle, we see that well-placed interconnectors may help to address some adequacy concerns.

However, the key issue is to first manage already existing congestions and the so-called loop-flows to increase tradable capacity on the existing interconnectors. Secondly, I would like to point out that there is no guarantee that the neighbouring countries would be able to provide supplies in the case of a regional system stress and that additional capacities will be available at any given time.

So there is a limit to reliance in electricity imports in times of scarcity.

Finally, we need to keep in mind that the Polish capacity market legislation provides specific rules for cross-border participation in the Polish capacity market.

**Can capacity markets play a supporting role in the transition to a more European market for electricity? Or do they hinder this objective?**

I would like to point out that a vast majority of the member states is already applying some sort of capacity mechanism. Some of them are applying multiple capacity mechanisms to address the same adequacy concern. For example, there are four support schemes addressing
directly or indirectly adequacy concerns in Germany. Therefore, the capacity mechanisms are becoming more common than may be expected by external observers.

I would like to say that due to the common missing money and missing capacity concerns the capacity mechanisms are becoming an indispensable part of the European internal electricity market.

The key is to synchronise the way these mechanisms are designed to minimise possible distortion of competition between different European markets and this trend is visible in the new Electricity Market Design.

Also, introduction of scarcity pricing will be a key component which will help to integrate the EU market by minimising the extent to which capacity mechanisms will be indispensable.

The Polish electricity sector has complained about “double standards” when it comes to capacity markets in Europe, saying Germany in particular has benefitted from special treatment. Can you explain why?

The strategic reserve gains in the final text of the ITRE Committee opinion some regulatory preferences including exclusion from the emission performance standard at the level of 550 CO₂ g/kWh. The 200 kg/kW per year emissions standard is not a real constraint for the already functioning, i.e. coal-based strategic reserves.

In simple terms, a lignite-fired plant in Germany may be supported, but the same plant in Poland may not – this is difficult to explain rationally from a climate protection perspective.

The board or Energa met on 3 September to decide on the fate of the Ostrołęka C coal plant project, often branded as Poland’s “last coal plant”. By the company’s own admission, the project is highly dependent on capacity mechanisms. What’s the status? Is Ostrołęka C still happening? Can a final decision be made before the reform of the EU electricity market is agreed?

The Polish Electricity Association does not comment on this specific project. For any information please refer directly to ENEA S.A. and ENERGA S.A. which are responsible for its development.
BRUSSELS – TOWARDS GREEN ENERGY

The Polish Electricity Association summed up in Brussels its series of debates on the capacity market. During the debate in the Belgian capital, it was stressed numerous times that capacity markets give an opportunity for effectively supporting a wise and real transition of the power sector towards the RES. However, for this transition to be effectuated in the best possible way, we need to take a broader look at the European power sector. “If at present we are incurring the very high costs of purchasing the CO2 emissions allowances, then we have fewer funds left for the new investments in less emissive generating capacities” – noted Maciej Burny, PKEE’s expert.

The participants in the discussion also stressed that the Member States should be allowed their own paces of achieving the RES targets as they have different starting positions. Among the discussed topics that will substantially impact the future of the capacity mechanisms in the EU was the issue of the EPS 550 standard. So far, some of the EU Member States have introduced capacity markets, and some strategic reserves, which according to the Union's competition policy are capacity mechanisms.

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Thus, as PKEE’s representative noted, they should be subject to equal treatment. “The European Parliament in its proposal stipulates exemption of the strategic reserves from the EPS 550 requirements, and this means adopting double standards. We expect that the new regulations in practice will not be favouring some Member States at the expense of others” – pointed out Maciej Burny.

**MADRID – THE CAPACITY RESERVE SHOULD NOT BE FAVOURED**

The Madrid debate was dominated by strategic reserve and the 550g CO2/kWh emissions standard (EPS 550) for capacity markets themes. So far, some of the EU Member States implemented capacity markets, and some strategic reserves – both notified to the EC for authorisation under state-aid rules as capacity mechanisms. Thus, As PKEE stressed, both mechanisms should enjoy equal treatment. Meanwhile, according to the position of the European Parliament, the German reserve shall be exempted from the EPS 550 emissions restrictions. The participants at the Madrid debate were of the opinion that fairer treatment should be executed. “In my opinion, Poland’s capacity market, already notified by the Commission for its correct operation and achievement of the goal it was established for, should be exempted from the EPS 550 (until 2025 for the new-build capacities) or entitled to derogations (for example until 2030 for the existing capacities), which is in line with the Council proposal in the CEP negotiation process. I also expect respecting the acquired rights for the capacity contracts concluded before the date of entry into force of the Market Regulation” – argued Filip Grzegorczyk, Vice-president of PKEE.

The opinion was echoed during the consecutive event in Brussels by Christof Schoser, representative of the European Commission’s Directorate for General Competition, who also admitted that the strategic reserve should not be favoured. In Madrid, the voice on adapting the energy transition to local circumstances was taken by Dr Frank Umbach, Research Director of the European Centre for Energy and Resource Security (EUCERS) at King’s College, London. “The ultimate compromise should remain technology-neutral. One has to remember that for Poland the capacity market is the most effective solution. This was confirmed by the European Commission’s approval for implementation of this mechanism” – he pointed out.

**PARIS – THE REDUCTION OF THE CO2 EMISSIONS SHOULD BE PERFORMED USING A SINGLE TOOL**

Talks in Paris were focused on the emissions trading scheme and the EPS 550 standard. A very important issue was discussed – the sense of introducing the 550g CO2/kWh emissions standard in the capacity markets when already the EU ETS is in place. “One cannot mix the tools as this only increases the costs to consumers” – argued PKEE’s expert Maciej Burny.

A similar position was taken by Fabien Roques, Vice-president of Compass Lexecon, one of the most experienced consultants analysing the most economically justified measure for assuring the security of supply, whereas the CO2 emissions reduction should be achieved with a single tool, being the EU ETS. Reducing emissions using the EPS 550 emissions standard in the Market Regulation, in his opinion, increases the costs and has no economic justification.

**ROME – SYNERGY IS NEEDED**

During the workshop in Rome, the experts representing the Italian electric power sector stressed the necessity of maintaining a synergy between the different solutions used in the EU Member States. PKEE pointed out that both the Italian and the Polish capacity markets, both approved by the European Commission in February 2018, fully comply with the EU rules on State aid, as proven based on the detailed study conducted by the Commission. “The capacity market in Poland is based on a real need to guarantee the security of supply to the customers. By 2030, energy consumption in Poland will increase by around 24%. We have to guarantee stable supplies to our consumers – households and businesses alike” – said professor Filip Grzegorczyk, President of TAURON Polska Energia. He also assured that the capacity market in Poland is the means to support the growth and integration of the RES in the modernisation process of the electric power sector.

During the European debates, PKEE stressed that the Polish capacity market would be technology-neutral, open to cross-border participation and based on auctions to provide the energy consumers with the lowest prices.