WindEurope's response to the European Commission's legislative proposals for Electricity Market Design reform

May 2023

The European wind industry welcomes the targeted revision of the EU's Electricity Market Design proposed by the European Commission. And calls on the European Parliament and the EU-27 to keep the balance of the Commission's proposal when defining negotiating mandates.

The co-legislators must urgently restore certainty for renewables in Europe. Europe is in a fierce global race for renewable energy investments while all the EU wind energy indicators are flashing red in 2022:

- Europe only invested €17bn in new wind, the lowest since 2009.
- Final Investment Decisions were taken for only 10 GW last year.
- Turbine orders were down 47% year on year.
- There was not a single Final Investment Decision in commercial scale offshore wind.

This is mainly due to fragmented and uncoordinated interventions of Governments in power markets as a means to tame down energy prices. This undermined the very fundamentals of the internal energy market leading to uncertainty on revenues and very significant negative impacts on renewable investments at the expense of the global competitiveness of the European economy.

In fact Europe's market design has worked as it should in the last two years: it has put a high price tag to reflect the mismatch between power supply and demand, notably for gas. Yet the policy responses to the crisis have mixed up how Europe delivers on the long-term goal of a carbon-neutral power sector and the short-term policy response to high power prices.

Critical to both objectives is deploying renewables at scale. Europe lacks a sufficient home-grown renewable energy base that can counteract our reliance on external supplies of energy vulnerable to geopolitical shocks. And it lacks the regulatory framework making renewables-based electrification the natural choice for industry and households.

Therefore, the targeted Electricity Market Design reform must address these as a matter of priority and restore the investment signals in renewables. And the European Parliament and the Council must:

Retain from the European Commission's proposals:

- The availability of all contractual forms for power supply generation: Contracts-for-Difference, Power Purchase Agreements, merchant investments.
- The removal of national revenue caps for inframarginal generators.
- The grandfathering of support to existing projects.
- The additional measures promoting Power Purchase Agreements.
- The inclusion of a Transmission Access Guarantee for offshore wind.

Improve from the European Commission's proposals:

- Harmonisation of Capacity Remuneration Mechanisms fully aligned with climate neutrality.

Investment Certainty & Public interventions on power markets

Retain from the European Commission's proposals:

- Grandfathering of support to existing projects.
- Revenue caps for inframarginal generators come to an end with the expiration of the EU emergency rules on power market interventions, and do not become a structural part of Europe's Electricity Market Design. This will restore certainty in wholesale market price formation.
- Public interventions on electricity retail price formation respect pre-defined criteria, in line with EU Electricity Market Design acquis.

The co-legislators must ensure the grandfathering of support to existing projects as mandated by the EU Renewable Energy legislation. Investment certainty and stable regulatory frameworks remain the bedrock for renewables deployment in Europe. Market scale sets in those countries where Governments respect the stability of already existing and awarded support schemes, and where Governments plan ahead and provide regulatory visibility for the wind industry and its supply chain with concrete wind deployment objectives. Industry best practices points that at least five-years forward-looking auction schedules (timeline, budget, capacity) and technology-specific auction designs are critical to attracting investments in wind energy. The 2018 Renewable Energy Directive lays down the key principles in its Articles 4 and 6.

The co-legislators must ensure revenue caps on infra-marginal generators remain out of the targeted Electricity Market Design reform. Revenue caps are temporary measures introduced with the EU emergency power market intervention rules that will expire on 30 June 2023.

Their implementation has been extremely messy and uncoordinated. Governments have largely deviated from the Commission's proposed uniform cap of €180/MWh and several of them have also failed to factor in hedging or virtual power purchase agreements meaning that they are in breach of the rule whereby the revenue caps must apply to realised profits only. Renewables investors in those markets expect significant losses. And the emergency measures have not stopped additional measures from being applied, such as new taxes coming on top of revenue caps. All of this has already resulted in uncertainty on revenues and to very significant negative impacts on renewable investments and deployment in 2022.

Instead of revenue caps, the transposition of the EU energy acquis at national level by the EU-set deadlines e.g. Clean Energy Package is far more critical for addressing the energy price crisis than embedding short-term emergency rules into the targeted reform of the Electricity Market Design.

The co-legislators must ensure any public interventions on electricity retail price formation respect the existing EU Electricity Market Design legislation and are based on a clear set of pre-defined criteria. The European wind industry welcomes the balanced approach the European Commission has taken to guarantee any public interventions in electricity retail price formation are fit-for-purpose. The Commission builds on an EU-wide approach on the back of the EU Electricity Directive to clarify the rules under which National Governments could intervene, as last resort, on power retail markets to support end-consumers without undermining investor confidence. Notably, the clear rule book of cumulative pre-defined conditions under which the Commission could declare a regional EU-wide price crisis, the limited duration of such crisis which ensures measures are not perpetuated beyond their meaningful use, and the preservation of suppliers' legitimate contractual rights in the event of a crisis are all good.

Revenue stabilisation mechanisms

Retain from the European Commission's proposals:

- Member States offer a mix of long-term contract options for investors to incentivise renewable deployment at scale e.g. Contracts-for-Difference, Power Purchase Agreements, merchant investments.

- Investors may, on voluntary basis, combine Contracts-for-Difference and Power Purchase Agreements for the same project where it makes business sense.

Remove from the European Commission's proposals:

- Article 19a (4): Power Purchase Agreements should not be treated as a non-price criteria in the allocation of public support to renewables.

The central response to the current crisis is ensuring more energy supply, in particular with more home-grown renewable electricity generation. Europe's Market Design must therefore send the right investment signals to doubling the wind energy deployment at scale. **The targeted EU Electricity Market Design reform should enable the development of long-term contracts (2-sided Contracts for Difference, Power Purchase Agreements, "10 year plus" futures traded on stock exchanges) to unlock the investments needed to accelerate new power capacity buildout**. Long-term contracts provide energy consumers, asset developers and investors certainty and reduce the impact of short-term fluctuations in prices.

The co-legislators must guarantee a mix of long-term contract options is available to investors. This is key to Europe's energy transition as it a) incentivises the scale of investments in renewables needed and b) guarantees investors' decision-making when managing large energy portfolios across multiple national jurisdictions.

Government-backed Contracts for Difference (CfDs) have proven very effective in de-risking wind investments and building at scale by keeping finance costs low. Crucially, they protect consumers from extraordinary price spikes. To ensure the most cost-efficient scheme for the society, the level of support shall be based on competitive market prices and not on administratively set prices.

The industry welcomes the proposals for further facilitation of corporate renewable Power Purchase Agreements (PPAs). PPAs have an important role to play in the energy transition in particular for the renewables-based decarbonisation of energy-intensive industries. The targeted Market Design reform must remove all remaining regulatory barriers to the conclusion of PPAs[1] and the lack of a standardised contact template for PPAs[2]. And should also aim to maximise the number of players active and able to sign PPAs on the demand side also towards SMEs. Government and/or public banks (notably the European Investment Bank) can play a role in underwriting PPAs and addressing challenges related to off-taker credit worthiness.

[1] The RE-Source Platform, regrouping corporate renewable electricity buyers and developers from across Europa, has mapped out all existing barriers to corporate renewable Power Purchase Agreement per European country in the European Corporate Sourcing Directory.
[2] The RE-Source Platform, together with the European Federation of the Energy Traders (EFET), a standard contract template for corporate Power Purchase Agreements which is today available in 6 European languages.

The co-legislators should retain the option for investors to combine, on voluntary basis, support mechanisms if it makes business sense e.g. combining Government-backed Contracts for Difference and market driven revenue stabilisation mechanisms such as renewable PPAs.

The explicit recognition in the Commission proposals for this combination to be enshrined in EU legislation explicitly is good. Investors could opt to combine CfDs and PPAs for the same project in view of their complementarity: CfDs guarantee price stability while PPAs secure off-takers for a renewable energy generator's output. However, the industry disagrees with the treatment of PPAs as a non-price criteria for the allocation of public support. PPAs are a financing instrument critical to building the business case of a project. Non-price criteria on the contrary aim to achieve wider societal benefits from the deployment of a renewable project e.g. environmental protection. The two have different end-goals and should not be treated under the same heading when defining competitive advantage for the allocation of support mechanisms.

Alongside CfDs and PPAs, purely merchant investments will be needed too. This is essential for electricity producers to meet their obligations under PPAs. Generators often need to buy electricity on the spot market to meet their obligations to deliver power to the off-taker under a PPA. This means they also need to sell some of their production on the spot market to have matching revenue.

Forward hedging will play a role to complement other long-term instruments (e.g. CfDs, PPAs) in the market to support investments in new generation capacity. Increased use of long-term future markets will enable off takers to hedge partial or full exposure undesired price changes.

Liquidity in the forward markets is currently insufficient. To increase it, the European Agency for the Cooperation of Energy Regulators (ACER) and the European Commission should prioritise the finalisation of forward markets' integration as per the EU market coupling regulatory acquis.

Electricity Grids

Retain from the European Commission's proposals:

- TSOs and DSOs providing information to project developers on available capacity for new grid connections, and status of connection requests.
- Transmission Access Guarantee for offshore wind.

Improve from the European Commission's proposals:

- Clarify rules on grid connections for renewables in the revised Electricity Regulation.

The targeted Electricity Market Design reform should serve as an opportunity to improve existing rules and remove bottleneck to help accelerate renewables deployment.

The accelerated deployment of electricity grids is an absolute priority for renewables deployment going forward. Europe has underinvested in its electricity grids in the last decade. System operators, renewable asset developers, technology suppliers and end-users need deeper cooperation since the early design stages to accelerate development of the power grid and, where appropriate, renewable

hydrogen infrastructure. Permitting rules for power grids should be clarified and aligned between EU, national, local authorities so that the required infrastructure can be unlocked. And National Regulatory Authorities should create targeted mechanisms to minimise grid built-out delays in line with national electrification and decarbonisation targets.

The co-legislators must retain the proposed requirements for TSOs and DSOs to inform on available capacities for new grid connections, and to inform investors on the status of their connection requests.

The co-legislators should also aim to further clarify grid connection regimes under the Clean Energy Package. These are currently very unclear on the conditions under which TSOs and DSOs can refuse grid connection access – this should be improved. In particular, TSOs and DSOs should be asked to provide enough adequate information on why they refuse grid connections for renewable energy projects. And they should grant temporary access and flexible contracts to renewable energy projects while TSOs/DSOs are in the process of developing or building lacking grid infrastructure.

The Market Design reform should ensure the expandability of the offshore grid. Offshore wind could meet 17% of Europe's power needs by 2050. But this cannot happen with today's approach to grid development and Market Design.

The co-legislators should enable investment in offshore hybrid assets by appropriately sharing risks, costs, and benefits between developers, grid operators, and society. Empowering developers and TSOs to connect offshore wind farms to two or more markets will be saving space, resources and helping the balance the energy system. These offshore hybrid assets could be up to one third of all offshore wind capacity by 2050.

The co-legislators should retain the proposals for using congestion income from TSOs for a Transmission Access Guarantee (TAG) for offshore wind. And aim to clarify its implementation. The TAG ensures that offshore wind farms are compensated when congestions occur in the electrical systems which the offshore hybrid is connect to and TSOs reduce interconnection capacity to solve such congestions.

The co-legislators should then clarify what would trigger the compensation mechanism of the TAG. It should be when the total interconnector capacity is lower than the installed Offshore wind farm capacity to ensure that all the derating induced risk is compensated and that it works for different hybrid configurations. In certain cases, a price drop in the offshore bidding zone may be induced by an operational derating.

Furthermore, the reliability of the TAG compensation is key for offshore wind investors. If the TAG compensation is paid from congestion income alone, it is essential that it is classified as priority use of congestion income.

Even with all these changes, TAG will not be enough to incentivise the first offshore hybrid projects. Offshore hybrid projects today are riskier than connecting wind farms to individual countries and building separate interconnectors, although they bring significant socio-economic welfare benefits such as increase in market integration and decrease in system costs. To unlock the potential of offshore hybrids it is key to hedge both volume and price risks.

Wholesale markets, flexibility & Capacity Remuneration Mechanisms

Retain from the European Commission proposal:

- Short-term wholesale markets are based on marginal pricing and the merit order.
- Dedicated provisions for flexibility.

Improve from the European Commission proposal:

- Designing climate-compatible Capacity Renumeration Mechanisms allowing domestic and cross-border demand side response, storage and renewable generators' participation.

The co-legislators should preserve short-term wholesale markets (based on the marginal cost approach). They remain very efficient in reflecting the real value of electricity at a given time. Short-term wholesale markets should remain the main mechanism for ensuring cost efficient power plant dispatch and settlement of electricity market contracts. The EU Market Design reform should safeguard the functioning of liquid and efficient short-term markets. The reform should ensure the functioning of short-term markets is not distorted by revenue caps and other uncoordinated market interventions from National Governments.

The co-legislators should preserve the new flexibility provisions unlocking flexibility products in the market. They will help navigate investment decisions in these solutions and will help incentivise flexible behaviour by the consumers.

The co-legislators should align rules on long-term adequacy mechanisms (Capacity Remuneration Mechanisms) with climate action. CRMs will be needed, notably to unlock the potential of electricity storage. They should be limited to providing the required adequacy based on a system adequacy assessment and designed to minimise distortive impacts on energy markets. Capacity Remuneration Mechanisms design should allow for cross-border solutions and should be fully consistent with the delivery of climate neutrality.

Capacity Remuneration Mechanisms should be technology-neutral, based on a system adequacy assessment, and allow domestic and cross-border demand side response, storage, zero-carbon and renewable generators' participation. And they should meet an emissions performance standard starting from the European Investment Bank (EIB) lending policy standard and decreasing over time so that Europe manages to decarbonise its energy system already by 2035.