

# EU Renewable Energy Financing Mechanism – A step closer towards an Energy Union?

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# Introduction



On 15 September 2020, the European Commission adopted an implementing regulation (the "**Regulation**") establishing the legal framework for the Union Renewable Energy Financing Mechanism (the "**Financing Mechanism**") provided in Article 33 of the Regulation 2018/1999 on the Governance of the Energy Union and Climate Action (the "**Governance Regulation**"). The Financing Mechanism aims to tender cross-border support for new renewable energy projects in the Union, allowing Member States to work together more easily in financing and deploying renewable energy projects, either as host or contributing countries.

The Financing Mechanism has both a **gap-filling function**, as it may help a Member State covering a gap in its indicative trajectory pursuant to Article 32 of the Governance Regulation, and an **enabling function**, as it should enhance renewable energy deployment across the Union, irrespective of a gap to the indicative Union trajectory.

This paper specifies the functions and functioning of the Financing Mechanism (**1.**), its potential benefits (**2.**) and the possible contribution to the achievement of the Energy Union (**3.**).

Although it is still too early to predict the extent to which this mechanism will be used, it can be argued that it constitutes a step closer towards an Energy Union. Indeed, the Financing Mechanism provides a tool to the European Commission to enforce non-binding targets for the deployment of renewables and allows for a certain Europeanisation of the support schemes, which remain until now largely national.

<sup>1</sup> Implementing Regulation (EU) 2020/1294 of the Commission of 15 September 2020 on the Union renewable energy financing mechanism, Publ. L 303/1.

<sup>2</sup> Regulation (EU) 2018/1999 of 11 December 2018 on the Governance of the Energy Union and Climate Action, amending Regulations (EC) No 663/2009 and (EC) No 715/2009 of the European Parliament and of the Council, Directives 94/22/EC, 98/70/EC, 2009/31/EC, 2009/73/EC, 2010/31/EU, 2012/27/EU and 2013/30/EU of the European Parliament and of the Council, Council Directives 2009/119/EC and (EU) 2015/652 and repealing Regulation (EU) No 525/2013 of the European Parliament and of the Council, Publ. L 328/1.

<sup>3</sup> The provisions and parameters used by the European Commission to determine the respective national indicative trajectories are included in article 5 of the Governance Regulation and in Annex II thereof.

<sup>4</sup> For the relationship between the EU target and the national trajectories, see also article 3 of Directive (EU) 2018/2001 of the European Parliament and of the Council of 11 December 2018 on the promotion of the use of energy from renewable sources, Publ. L 328/82.



# The legal framework (I)



## 1. The legal framework

### 1.1 Functions of the Financing Mechanism

According to Article 33 of Governance Regulation, the purpose of the Financing Mechanism is twofold.

On the one hand, in order to collectively achieve the Union binding target of 32% of renewable energy consumption by 2030<sup>5</sup>, Member States must contribute to this objective by increasing the share of renewables in their respective energy mix. In 2022, 2025 and 2027, the Member States will have to reach a reference point of at least respectively 18%, 43% and 65% of the total increase in the share of renewable energy compared to the 2020 binding target of that Member State<sup>6</sup>, and its contribution to the 2030 target, as set out in their integrated national energy and climate plans.<sup>7</sup> The European Commission can take corrective actions when a Member State is

not on track to achieve its target. One of these actions can consist in a voluntary payment to the Financing Mechanism – the so-called "gap filling function".

On the other hand, the European Commission has to support the ambitions of Member States in the deployment of renewable energy sources through an enabling framework that aims to reduce costs and enhance regional cooperation – the so-called "enabling function".

Different rules apply per function, for example in relation to the relevant award criteria (see 1.2).

### 1.2 Functioning of the Financing Mechanism

The Financing Mechanism enables the contributing Member States to pay financial contributions into the scheme, which will be used for renewable energy projects in host Member States. A third (non-Union) country can also be a host country.<sup>8</sup> In addition, the Union itself and private entities can make a contribution to a specific project.

<sup>5</sup> Article 3 Directive (EU) 2018/2001 of the European Parliament and of the Council of 11 December 2018 on the promotion of the use of energy from renewable sources, Publ. L 328/82.

<sup>6</sup> See Annex I of the Governance Regulation for the 2020 targets. These binding national 2020 targets remain the respective baseline shares for each Member State. In other words, the share of renewable energy in their mix cannot go below this threshold. See Article 3, paragraph 4 of Directive (EU) 2018/2001 of the European Parliament and of the Council of 11 December 2018 on the promotion of the use of energy from renewable sources, Publ. L 328/82.

<sup>7</sup> Article 4(a)(2) of the Governance Regulation.

<sup>8</sup> See 3.1.

# The legal framework (II)



In terms of functioning, the European Commission will call each year on the Member States to express their interest in participating as contributing and/or host Member State in grant award procedures. Interested Member States shall provide relevant information, such as preferred technology, environmental specifications or the maximum amount of capacity (step 1).<sup>9</sup> For example, Spain, as a host country, might need to install 100-150 MW of new offshore wind capacities and wishes to attract foreign investments while retaining 30% of the statistical benefits for its renewable energy objectives. Germany, as a contributing country, might need to install either 1.000 MW PV or 500 MW wind onshore, or a mix of the two, depending on available capacities in host countries.

Upon this information submitted by the host and contributing countries, the European Commission drafts a timetable and tender documents, states which preferences of

the Member States it is going to take into account during the first round, and pre-calculates the division of the statistics for renewable energy (step 2).<sup>10</sup> These draft calls are notified to the Member States. The host countries may then confirm their interest through an *irrevocable* commitment (step 3). Afterwards, the European Commission communicates on the ceiling prices<sup>11</sup> and the maximum budget available for each call for proposal (step 4).<sup>12</sup> Next, the contributing Member States commit to pay a contribution to the Financing Mechanism in relation to one or several calls and provide relevant information, including an indication on which one of the two functions (see 1.1) the payment is based (step 5).<sup>13</sup> Following these commitments, the European Commission launches the call(s) for proposals to project developers (step 6). Afterwards, the proposals will be appraised by the European Commission (step 7) and the grants can be awarded (step 8).

<sup>9</sup> Article 7 of the Regulation.

<sup>10</sup> For example, 30% of the statistics for the host country and 70% for the contributing country.

<sup>11</sup> The maximum price per kWh or kW that can be awarded within a specific call and above which applications are excluded from the grant award procedure.

<sup>12</sup> Article 9 of the Regulation.

<sup>13</sup> Article 10 of the Regulation.



# The legal framework (III)

In case where a Member State contributes to the Financing Mechanism by making a "voluntary"<sup>14</sup> payment in light of the gap-filling function in their respective national trajectories, this tender may only be allocated based on the lowest price as sole award criterion. After receiving the bids, per host country, the European Commission ranks the different bids from competitive to least competitive into a list. If Germany for example committed to host maximum 500 MW of renewable projects, the most competitive projects will be accepted up to a maximum cumulated amount of 500 MW, ranked based on the lowest bid.

On the other hand, where a Member State contributes in the context of the enabling function, this contribution may be allocated to joint projects, joint support schemes,

small-scale or innovative technology projects, or any other project that contributes to the enabling framework.<sup>15</sup> The award criteria in this respect shall reflect the preferences of the Member States, for instance the environmental criteria.

The Regulation sets apart different principles for the award procedures to comply with, as to for example what kind of technologies could be used.<sup>16</sup> In addition, the Financing Mechanism awards subsidies for investment support granted to increase the capacity for renewable energy production or operating support to incentivise the operation of renewable energy installations, by providing premiums in addition to market revenues<sup>17</sup> for example. The European Commission decides on the form of the support, taking into account the preferences of the host Member State.<sup>18</sup>

<sup>14</sup> The Regulation states "voluntary" in article 3(8), but in essence it is a payment in reaction to the recommendations of the European Commission, as referred to in article 5 and 32 Governance Regulation. Therefore, it is to be seen whether this payment is genuinely "voluntary", depending on how strict the European Commission will enforce the indicative trajectories.

<sup>15</sup> Article 15 of the Regulation.

<sup>16</sup> Article 16 of the Regulation.

<sup>17</sup> Market premiums. See also Article 4, paragraph 3 of Directive (EU) 2018/2001 of the European Parliament and of the Council of 11 December 2018 on the promotion of the use of energy from renewable sources, *Publ. L 328/82*.

<sup>18</sup> Article 17 of the Regulation.



# Potential benefits (I)

## 2. Potential benefits

The division of the allocation of grants will depend on who is investing, what is the function of the investment, and the specific features thereof.

The renewable energy produced generates statistical benefits for contributing Member States based on the expected lifetime of the installation. All statistical benefits after this period remain with the host Member State.<sup>19</sup> By default, 80% of the renewable energy shall be allocated among the contributing Member State(s), 20% to the host Member State. The European Commission can decide otherwise and allocate 0% up to 50% of the benefits to the host Member State, based on the potential costs or the likelihood that the call will attract any support. This division will be communicated by the European Commission together with its intention to launch a call for proposal. Contributions by the Union or private investors are taken into account for the Union's binding overall

target. Whenever a third country is hosting a project, 100% of the statistical transfers will be allocated to the contributing country.<sup>20</sup>

Beside the allocation of statistical benefits, this Financing Mechanism brings about benefits for any participant thereof. For contributing countries, some of the benefits are lower direct and indirect costs than deployment of an installation<sup>21</sup> on its own territory and lower transaction costs.<sup>22</sup> These countries will also have access to potentially cheaper renewable energy sources or to renewable energy sources that would otherwise be unavailable, albeit in a statistical, or "virtual" so to say, manner since they could receive statistical benefits only. The host Member States would have to depend less on import and could modernise their national energy system, in addition to the improved air quality, environmental security and greenhouse gas emission reductions.

<sup>19</sup> Article 27.3 of the Regulation.

<sup>20</sup> Article 27 of the Regulation.

<sup>21</sup> Compared to only a clearly-defined cost contributed to the Financing Mechanism.

<sup>22</sup> The Member States can contribute to the Financing Mechanism and do not need to, for example, establish political contacts for the deployment of installations in another Member State.





# Potential benefits (II)

Project developers can benefit from the Financing Mechanism that will identify suitable renewable energy installation projects to be developed and receive support based on an EU-wide tender system. Several questions could arise, however, for these project developers, such as for example the auction design in a cross-border auction implemented by the European Commission. Usually, tender volumes in terms of capacity (in MW) are the most commonly used form. The most common tender formats for renewable energy projects are static, where all bidders simultaneously submit their bids and prices are unknown to the other. Generally, the same practices apply for renewable energy projects. In addition, private stakeholders, such as the project developers, may be consulted to state their opinion on the proposed tender design.<sup>23</sup> It is important to stress that, although the rules of the national regulatory framework, as well as the national market conditions will remain largely unchanged in the context of tenders under this mechanism, these rules relate to the country where the installation is built. One could think of corporate taxation, conditions for grid connection, environmental requirements and so on. For this

reason, bidders from different countries inevitably face differing circumstances, even though they are competing on the basis of a common support scheme design. Therefore, preparation is key.

Furthermore, private investors are encouraged to invest in the Financing Mechanism in order to broaden their sustainable energy portfolio and benefit from the Union-wide green labelling via guarantees of origin. The entity is free to indicate a preference for tender procedure or a type of technology for which its support is intended. The European Commission has published a survey for private investors on this matter, which seeks to collect replies to several questions, such as the objective that a contributing entity seeks to obtain, the amount of energy supported, the maximum financial contribution, the technological focus of the auction and whether or not the entity would request the guarantees of origin.<sup>24</sup> By means of this survey, the European Commission is preparing for the first call for proposal. Nonetheless, for these private investors, issues such as permitting, but also an array of other practicalities, could determine the feasibility of their investments.

<sup>23</sup> AURES II, The new renewable energy financing mechanism of the EU in practice, [http://aures2project.eu/wp-content/uploads/2020/11/AURES\\_II\\_D6\\_3\\_EU.pdf](http://aures2project.eu/wp-content/uploads/2020/11/AURES_II_D6_3_EU.pdf)

<sup>24</sup> Press release European Commission, EU renewable energy financing mechanism: opening the way for private investment, 11 January 2021, [https://ec.europa.eu/info/news/eu-renewable-energy-financing-mechanism-opening-way-private-investment-2021-jan-11\\_en](https://ec.europa.eu/info/news/eu-renewable-energy-financing-mechanism-opening-way-private-investment-2021-jan-11_en). The survey runs until 15 February 2021.



# A step closer towards an Energy Union? (I)



## 3. A step closer towards an Energy Union

### 3.1 An alternative to a harmonised European support framework

The European Commission had been advocating for market-based support and cross-border cooperation with the ultimate ambition of creating a harmonised quota system. Already in the late 1990s, the European Commission intended to harmonise the support of renewable electricity based on tradable green certificates (TGC) system<sup>25</sup>, which was blocked by the European Parliament and several Member States. When drafting the Third Energy Package, the European Commission endeavoured again to introduce an EU-wide tradable certificate scheme,

based on guarantees of origin (GO).<sup>26</sup>

Virtual cross-border trade was necessary to give Member States sufficient flexibility to meet their targets and allowed for imports of renewable energy from third countries, such as Norway. However, in the legislative process of the Renewable Energy Directive of 2009, the provisions for a tradable GO were removed, since it was opposed by the European Parliament. Therefore, the European Commission never succeeded at establishing a harmonised European support framework.

The Financing Mechanism is not a harmonised European support framework, although it offers to all Member States the possibility to meet its renewable energy targets, not (necessarily) by closing bilateral agreements, but by creating the opportunity to invest in renewable energy (of its choice) spread over the whole Union. This allows governments to compensate for the lack of domestic deployment by investing and still comply with the national indicative renewable energy trajectory, without effectively implementing a harmonised European support framework.

<sup>25</sup> David Jacobs, 'Designing Financing Mechanisms for Electricity from Renewable Energy Sources: The Role of the European Commission as an Agenda Shaper', in Jale Tosun, Sophie Biesenbender, Kai Schulze (eds.), *Energy Policy Making in the EU. Building the Agenda*, London, Springer, 2015, p 117.

<sup>26</sup> COM(2008) 30 final, Proposal for a Directive of the European Parliament and of the Council on the promotion of the use of energy from renewable sources.



# A step closer towards an Energy Union? (II)

In addition, with the adoption of this system, the Union effectively opens up borders for the achievement of the renewable energy target, by confirming and stressing that meeting the target is not about meeting the reference points in their respective trajectories on the own territory of the Member State, but about financing its relevant share in energy, wherever the project may be located in the Union.

## 3.2 An alternative to the Cooperation Mechanisms

In the context of the Green Deal, this Financing Mechanism adds a third possibility for Member States to meet the 2030 target for renewable energy. Currently, Member States primarily pursue this target through national support schemes, such as for example feed-in tariffs/feed-in premiums and green certificates mechanisms. The renewables deployment targets may also be pursued through cooperation mechanisms introduced by the Renewable Energy Directive 2009 ("**Cooperation Mecha-**

**nisms**"), such as statistical transfer agreements<sup>27</sup>, joint projects between Member States (and third countries)<sup>28</sup> or joint support schemes.<sup>29</sup>

In a statistical transfer agreement, an amount of renewable energy is deducted from one country's progress towards its target and added to another. For example, in October 2020, Belgium decided to conclude such statistical transfer agreement with Denmark, for an amount of 22,5 million EUR, to achieve its renewable energy target for 2020. These statistical transfer agreements are considered as a cost-efficient instrument to fulfil the renewable energy targets.<sup>30</sup> Joint support schemes relate to two or more EU countries that co-fund a joint support scheme for renewable energy production. It can involve measures such as common feed-in tariff, feed-in premium and certificate trading regimes.<sup>31</sup> The joint projects (possibly with third countries) relate to the co-funding of a renewable energy project and share the renewable energy for the purpose of meeting the targets. These projects are suitable to jointly develop technologies, save costs of renewable energy target fulfilment and prepare long-term electricity imports/exports.<sup>32</sup>

<sup>27</sup> Article 8 of the Renewable Energy Directive

<sup>28</sup> *Ibid.*, articles 9 and 11.

<sup>29</sup> *Ibid.*, article 13.

<sup>30</sup> Flemish Parliament, Commission of Energy, Request for explanation on the Flemish renewable targets 2020 of 14 October 2020.

<sup>31</sup> ECOFYS, Cooperation between EU Member States under the RES Directive, 29 January 2014, p 4.

<sup>32</sup> ECOFYS, Cooperation between EU Member States under the RES Directive, 29 January 2014, p 6.



# A step closer towards an Energy Union? (III)

One of the differences between these Cooperation Mechanisms and the Financing Mechanism relates to the fact that no bilateral or multilateral agreements are required for the Financing Mechanism. Joint support schemes require a deep cooperation between Member States who share similar technology preferences (such as for example the Joint Support Scheme for offshore wind energy between Belgium, Denmark, France, Germany, Ireland, Luxembourg, the Netherlands, Norway, Sweden and the United Kingdom), and/or have well integrated markets (*i.e.* Joint Quota System for Sweden, Norway, Denmark and Finland). The joint projects are raising interest, but are however considered as rather complex.<sup>33</sup> Other downsides of these Cooperation Mechanisms relate to a certain level of efficiency that is required in order to bring about a successful Cooperation Mechanism, efficiency can be gained when one of the Member States already has experience in the design, monitoring and implementation of a similar support scheme.<sup>34</sup>

The Financing Mechanism therefore differentiates from Cooperation Mechanisms by being centrally operated by the European Commission itself, although it can also facilitate joint support schemes and joint projects pursuant to its enabling function to achieve the overall Union target. The European Commission has to take the initiative under the Financing Mechanism to introduce a project, where the contributing State can decide how much it seeks to invest in what kind of renewable energy. Not only Member States benefit from this Financing Mechanism, but also third countries, private investors, and energy project contractors. In addition, this Financing Mechanism also benefits to the Cooperation Mechanisms as the Financing Mechanism can be allocated, within its enabling function, towards a joint product or a joint support scheme.

<sup>33</sup> ECOFYS, Cooperation between EU Member States under the RES Directive, 29 January 2014, p 6.

<sup>34</sup> European Environment Agency (European Topic Centre on Climate change mitigation and energy), "Cross-border regional cooperation for deployment of renewable energy sources", <http://www.eionet.europa.eu/etcs/etc-cme>, p. 19.





# A step closer towards an Energy Union? (IV)

## 3.3 Implementation of the Financing Mechanism

As indicated, the European Commission can prompt a Member State to make a voluntary payment into the Financing Mechanism as a corrective action when the Member State is not on track with its indicative trajectory. Such payment is said to be voluntary, and the reference points of the indicative trajectory are considered as indicative. In this respect, it seems that the era in which this Financing Mechanism has been adopted is different from the era in which the 2020 targets had to be met. These 2020 targets for renewable energy were binding targets for each Member State separately, where the failure to meet the targets could lead to fines, while today the objective is imposed on the Union.

One could ask whether it would not have been (more) opportune for this Financing Mechanism to had already been in place in order to achieve the 2020 targets. The Financing Mechanism would have made a good alternative to a statistical transfer agreement, for example. In addition, this may turn out as a rather beneficial scheme for countries such as Poland, Spain or Greece as host Member States, which have potential but lack funds to invest in renewable energy. It is not said that, for example, Belgium would have been willing to invest sooner in projects in other Member States, considering that could be prone to (political) criticism since it is not benefitting its own national employment or industry. On the other hand, it has been proven that it is difficult for some Member States to comply with their respective targets for

2020.<sup>35</sup> Although the Member States do not individually have to meet binding targets for 2030, Member States still have to comply with specific reference points. In addition, one could argue that this Financing Mechanism was adopted precisely because national targets are not binding anymore.

In conclusion, even if the Financing Mechanism cannot have the same effect as a genuinely harmonised system, it does create the opportunity to invest in renewable energy over the whole Union. It can be emphasised that, because of its double goal, this system opens the Member States' borders for the achievement of the renewable energy target, and the non-complex system brings about benefits for a lot of different parties, not only for the Member States, but also for private investors and developers. This Financing Mechanism also seeks to achieve an economic optimum, where Member States are able to decide what is the most cost-effective way to decarbonise their electricity consumption, by sponsoring renewables at home or abroad, since it both leads to the same quantity of GHG reductions at EU level. In this respect, the Financing Mechanism could be considered as one step closer towards an Energy Union. Nonetheless, considering its political angle, it remains to be seen whether the Financing Mechanism will be effectively used and whether its promising effects on the Energy Union will be implemented in practice, including in the practicalities of its tender procedure.

<sup>35</sup> The state of play is indicated in the latest Renewable Energy Progress Report of the European Commission, (COM/2020/952), 14 October 2020, p. 6: "There are now twelve Member States (Bulgaria, the Czech Republic, Denmark, Estonia, (Greece estimated), Finland, Croatia, Italy, Cyprus, Latvia, Lithuania and Sweden) that have already achieved a share equal to, or higher than, their 2020 target. At the same time, during 2018, six Member States Spain, Italy, Lithuania, Hungary, Portugal and Romania have reduced their renewable energy share compared to 2017."

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