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EU Electricity Market Design Reform

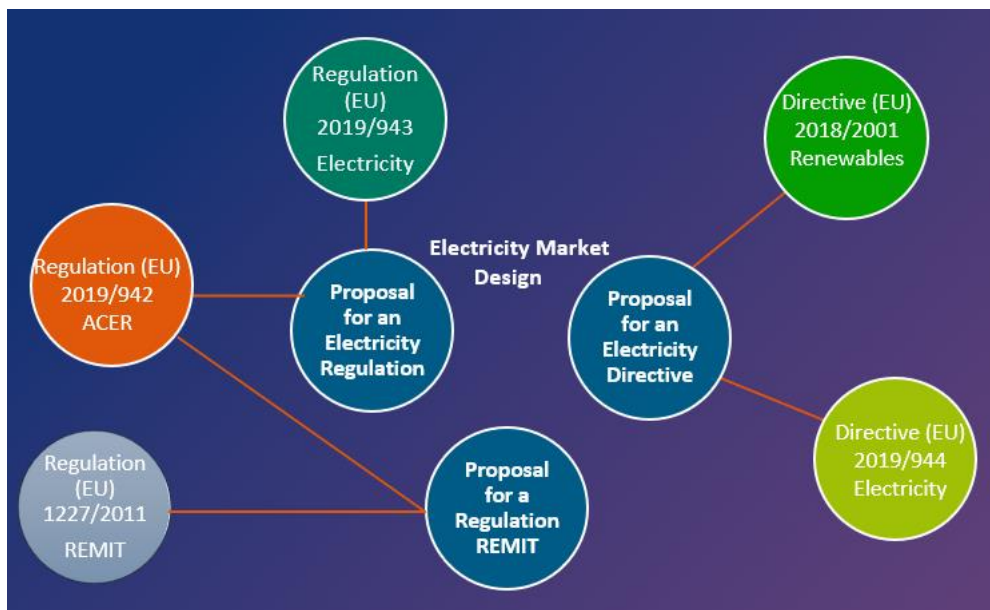
# EU Electricity Market Design Reform

## Introduction

On 14 March 2023, the European Commission proposed a reform of the EU electricity market aiming to increased protection of consumers against soaring energy prices. Besides, the reform aimed to boost renewables for electricity bills to be less dependent on fossil fuel prices and improve the flexibility of the electricity system.

The reform consisted of two legislative proposals:

- The proposal for an amending regulation to improve the Union's electricity market design (**EMD**), which revises the Electricity Regulation, the Electricity Directive, the Renewable Energy Directive Regulations, and the European Union Agency for the Cooperation of Energy Regulators (**ACER**) Regulation (hereafter section 1).
- The proposal for an amending Regulation to improve the Union's protection against market manipulation in the wholesale energy market, which revises the regulation on wholesale energy market integrity and transparency (**REMIT**) and the ACER Regulation (hereafter section 2).



The interinstitutional negotiations between the European Parliament and the Council were concluded on 14 December 2023. The text needs to be endorsed formally by the two institutions. The vote at the European Parliament plenary session is planned for March 2024.

## 1. Proposal to improve the Union's EMD

- Overview

The new proposed rules encompass a range of specific measures aimed at enhancing the energy market and benefiting consumers with a broader array of contracts and transparent information.

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Firstly, to mitigate the risk of supplier failure, the proposed rules introduce new requirements on price risk management and the establishment of suppliers of last resort, aimed at ensuring a more secure energy supply chain. Additionally, a focus is given on promoting the sharing of renewable energy, such as selling excess electricity from rooftop solar installations to neighbours, thereby fostering a more interconnected and sustainable energy community.

Secondly, the proposed rules also advocate for more stable long-term contracts, specifically Power Purchase Agreements (**PPAs**) between companies and suppliers. Furthermore, the introduction of Contracts for Difference (**CfDs**) between electricity generators and public entities adds flexibility and dynamism to the energy market.

Thirdly, an integral aspect of the proposed rules is the obligation to facilitate the integration of renewables into the energy system. This underscores a commitment to transitioning towards cleaner and more sustainable energy sources. As the next step in the process, formal endorsement of the agreement by the Parliament and the Council will be pursued, marking a significant milestone in the implementation of these progressive measures.

In essence and summary, the main provisions of the EMD are the following.

- Power Purchase Agreements

Article 19(a) of the final text encourages the conclusion of PPAs without specifying that the focus should be specifically on nuclear power. It omits the inclusion of "EU guarantees" for PPAs but instead advocates for state guarantees. Member States also retain the flexibility to provide guarantees exclusively for additional investments in renewable energies.

While standard contracts for PPAs will be proposed, their adoption remains voluntary. Furthermore, the Commission is tasked with "assessing the possibility" of organizing European auctions for renewables at the EU level if the target of achieving 45% renewables in the Union's energy consumption by 2030, as outlined in the Renewable Energy Directive (RED), is not met.

- Contract for Differences

CfDs are encouraged for renewables such as wind, solar, geothermal, and hydropower without reservoir, as well as for nuclear power. Existing power stations have the option to employ these guaranteed price contracts when engaging in new investments. Notably, the Member States' mandate experiences a significant shift, as the CfD is no longer the exclusive authorized support scheme for new renewable and nuclear projects launched three years after the reform takes effect. Member States may opt for "*equivalent schemes with the same effects.*"

Several provisions, mirroring those outlined by the Council, govern the execution of these contracts. This includes the requirement for alignment with the rules on State aid and monitoring to prevent any adverse impact on EU competitiveness. The text incorporates Parliament's suggestion of incorporating penalty clauses in the design of CfDs, applicable in the event of early unilateral termination of the contract.

Regarding the revenue generated from CfDs, it has the potential to be redistributed to end consumers, though the text does not specify whether the redistributed amount should be proportional to the level of consumption. Alternatively, the funds could be utilized to finance the cost of the CfDs in instances where the market price falls below the guaranteed price.

- Capacity mechanisms

Articles 64 and 66 of the final text call for the use of capacity mechanisms to be simplified. A Commission report on the subject is expected no later than six months after the entry into force of the reform. This

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report should inspire a Commission proposal to facilitate and rationalise the use of capacity mechanisms, expected nine months after the entry into force of the text.

As proposed by the Council, the limit on CO<sub>2</sub> emissions has been abolished (subject to conditions) for power plants built before June 2019. This will apply until 31 December 2028. To put it plainly, plants with high emissions (gas or coal-fired) will be able to benefit from subsidies thanks to a capacity mechanism already in place when the reform comes into force. The European Commission will "assess the impact of the request in terms of greenhouse gas emissions" before granting the derogation. In addition, the Member State that obtains the derogation will have to provide a plan for phasing out coal and reducing greenhouse gas emissions.

- Crisis mechanisms

The Member States will be in the driving seat when it comes to deciding whether a crisis episode should be triggered. As proposed by the Commission, the Member States will decide by qualified majority to declare crisis status. A crisis is triggered if:

- average prices on the wholesale market are 2.5 times higher than in the previous five years (except 2022 and other periods when a crisis is declared) and at least 180 euros/MWh with an upward trend expected to last at least six months;
- retail prices increase by 70% over a period of at least three months.

In the event of a crisis, Member States must be able to control prices more closely. Measures such as price shields will therefore be authorised. However, the extension of the cap on rents for sub-marginal producers has not been retained.

## 2. Proposal for amending Regulation to improve the Union's protection against market manipulation in the wholesale energy market

- Overview

The amended REMIT aims to broaden data reporting requirements in the electricity market through additional information targeted by the reporting obligation. It also aims to enhance the collection of inside information through third parties.

However, the primary point of contention among Member States revolves around empowering ACER for REMIT enforcement. This debate gains significance considering the recent decision by the French REMIT authority (CORDIS) penalizing Engie for omissions to disclose information specified in REMIT. While this decision showcases the flexibility disposed by national authorities in the sanctions under REMIT, the proposed amendments seek to position ACER as the authority for the effective enforcement of REMIT.

In essence and summary, the main provisions of the amended REMIT are the following.

- Reporting obligations

Initially, REMIT focused on data collection, specifying that reported information should include the identification of wholesale energy products (products bought and sold along with agreed price and quantity), as well as details about the parties and beneficiaries to the transaction.

In its amended form, article 8 introduces new data to be collected by market participants. Specifically, it now targets information concerning the market participants exposures, "*detailed by products, including*

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*the transactions that occur over the counter*". Also, the new version of article 8 includes intermediaries to the transaction as data to be reported.

This new category of intermediate actors is also highlighted in the amended article 15, which addresses the obligations of individuals professionally arranging transactions. Originally introduced for actors not directly subject to REMIT reporting obligations, but involved in electricity market transactions, article 15 mandates the notification of transactions potentially breaching REMIT to national authorities.

The revised version extends this obligation to cover any cancellations or modifications of transactions, as well as transactions not conducted on "*organised market places*" (OMP).

More generally, the amended REMIT extends its focus beyond financial instruments. It also introduces a time limit for notification of potential breaches, that should be made within four weeks from the day the person professionally executing the transactions, becomes aware of the suspicious event.

- ACER's powers

To strengthen transparency and counter fraud in energy markets, the Commission proposed on assigning a more significant role to ACER. Notably, the proposal included the possibility for ACER to initiate investigations into potential fraud cases when three member states are implicated, extending its authority for investigation and enforcement.

During the EU interinstitutional trilogues, the European Parliament went one step further proposing to grant ACER powers to lead investigations, inflict sanctions and carry onsite inspections.

However, the Council curtailed these ambitions safeguarding the Member States' discretion. Indeed, the final text grants ACER the ability to launch investigation, emit information requests to Member States and impose financial penalties. However, the latter will be limited to procedural rules linked to inspections. In that sense, the authority to impose fines for REMIT breaches remains within Member States' hands, as advocated by the Council.

Additionally, the Council maintained the monopoly of national authorities by allowing Member States to oppose ACER's investigation launch. National regulators will have three months from notification of the investigation launch by ACER to oppose any action by the latter. This opposition can be based on two grounds: the regulator has itself launched an investigation into the facts, or it has already concluded an investigation by determining the existence or absence of abuse.

In sum, the amended REMIT enlarges its scope of application, both in terms of data collection by market participants and entities obliged to report potential breach. Despite efforts to strengthen ACER's powers, Member States remain at this stage the central actors in the implementation and enforcement of REMIT.