State intervention and the future of the European internal energy market- will it survive?

Leigh Hancher

The European Green Deal

Mobilising research and fostering innovation

Transforming the EU's economy for a sustainable future

Increasing the EU's Climate ambition for 2030 and 2050

A zero pollution ambition for a toxic-free environment

Supplying clean, affordable and secure energy

The European Green Deal

Preserving and restoring ecosystems and biodiversity

Mobilising industry for a clean and circular economy

From 'Farm to Fork': a fair, healthy and environmentally friendly food system

Building and renovating in an energy and resource efficient way

And leave No one behind

Accelerating the shift to sustainable and smart mobility

Financing the transition

Leave no one behind (Just Transition)

The EU as a global leader

A European Climate Pact

Upgrading climate, energy, transport and tax measures to reduce GHG emissions by at least **55% by 2030** vs 1990

"The more interdependent we become in Europe, the more independent we become from Russia. The ultimate aim is: an interconnected European market for clean energy. That is the foundation of a true Union of Clean Energy. And this is how we REPower the EU."

Ursula von der Leyen
President of the European Commission

REPower EU

- A roadmap to reduce the dependence on Russian fossil fuels and fast forward the energy transition
- Based on **3 pillars**:

Energy saving and energy efficiency

Massive acceleration of investment in renewables

Diversification of our energy supplies

De facto: 4th Pillar: Fighting high prices –
Gas & electricity price caps – market design reforms

EU chief announces electricity market overhaul amid 'skyrocketing' prices

By Frédéric Simon and Nikolaus J. Kurmayer | EURACTIV Jun 10, 2022 (updated: Jun 13, 2022)

A two-speed focus to mitigate the crisis•

Short term : Demand reduction! (energy efficiency, savings)

Increased LNG imports (+5% more worldwide, now19 exporting countries and 44 importing)
Infrastructure investments
Ad hoc provisions for vulnerable consumers/specific categories•

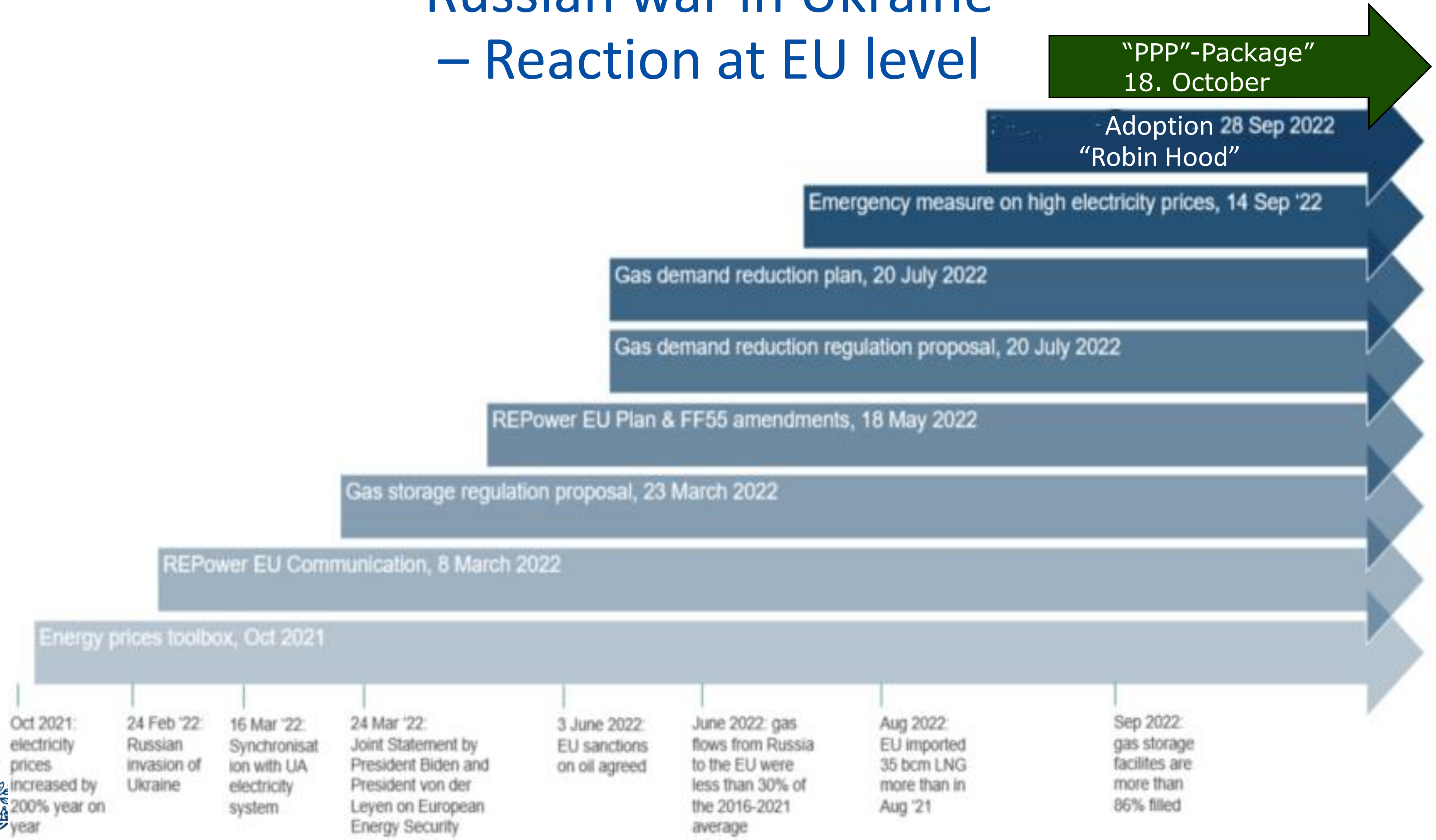
Diversification! Solidarity measures

Renewable electricity and renewable and low-carbon gases(biomethane, hydrogen) acceleration

(Renewable) Hydrogen?

Market design review?

Russian war in Ukraine – Reaction at EU level



TILBURG

24 February 2022
Russia's invasion of Ukraine

1. **13 October 2021**
Communication **"Tackling rising energy prices: a toolbox for action and support"**

2. **8 March 2022**
Outline of **"REPowerEU": joint EU action for more affordable, secure and sustainable energy"**

3. **23 March 2022**
Commission proposal to amend the **Security of Gas Supply Regulation** and a **Communication "Security of supply and affordable energy prices: Options for immediate measures and preparing for next winter"**

4. **21 April 2022**
Campaign by IEA and EC "Playing my part" with **energy saving tips to help cutting the EU's reliance on Russian fuel**

5. **18 May 2022**
The Commission REPowerEU Plan to rapidly reduce dependence on Russian fossil fuels

6. **27 June 2022**
Adoption of the **Gas Storage Regulation** (EU 2022/1369)

7. **20 July 2022**
Commission proposal for **a Regulation on coordinated demand reduction measures for gas** and **communication "Save gas for a safe winter"**

8. **26 July 2022**
Energy Ministers agreement on the Regulation on coordinated demand reduction measures for gas

9. **14 September 2022**
Commission proposal for a new **Regulation on an emergency intervention to address high energy prices and reduce energy bills for EU citizens**

10. **30 September 2022**
Energy Ministers agreement on the Regulation on an emergency intervention to address high energy prices

11. **18 October 2022**
The Commission's additional proposals to fight high energy prices and ensure security of supply

European Commission

Communication of 18 October 2022 ‘**Energy Emergency - preparing, purchasing and protecting the EU together'.**

The Current Crisis – are the legislative responses adequate?

What criteria do we assess these ‘temporary’ mechanisms by?

What price is solidarity?

Is the process transparent and legitimate?
What is the end game?
Can history help? Can the Euratom Treaty provide a precedent?

Article 122 (1) TFEU

- (ex Article 100 TEC)
- "1. Without prejudice to any other procedures provided for in the Treaties, the Council, on a proposal from the Commission, may decide, in **a spirit of solidarity** between Member States, upon the measures appropriate to the economic situation, in particular if severe difficulties arise in the supply of certain products, notably in the area of energy".

- Little used until current crisis:

- No consultation/impact assessment/EU Clilmate Law check/political control

- Judicial challenge?

- **Ordinary legislation:** Art. 194 TFEU, Parliament and Council (see: Storage Regulation Regulation (EU) 2022/1032, June 2022)
  - (+) Full legislative process, Parliament involvement; qual. majority voting
  - (-) Negotiations more time-consuming; highly technical issues
- **Temporary crisis instrument under Art. 122 TEFU**
  - 122: only possible if
    - (1) needed to **address crisis**
    - **(2) time-limited**
    - (3) reflects **solidarity**
  - (-) Specific conditions, no lasting solution

Strategic gas storage – creeping intervenitonism

- ‘Decarb package’ – recast Gas Directive and Regualtion, Dec 2021

► Joint risk assessment

► 4 options in case of identified supply risk:

strategic reserve (shipper), incentives for booking storage capacities,
strategic stocks (TSO), integration of storage into TSO network; MS to agree on financing of the measure, and on common procedures for withdrawal of the gas
in case of declaration of emergency

- **Joint procurement for reserve stocks:**

► Member States may set up a mechanism for the joint procurement of strategic stocks by transmission system operators as part of the preventive measures to ensure security of supply, subject to conditions

- **Measures on cybersecurity**
- **Solidarity** - Calculation of compensation payment to be controlled ex-post by NRA or competition authority

Storage Regulation 2022:

Full fledged act under Art. 194 (Council and EP)

- Filling targets/trajectories; MS “shall ensure” [new targets/trajectories adopted by delegated legislaton]
- Burden sharing – cross-border filling
- Commission can “order measures”
- Storage certification

Implementation issues

- Filling of non-storage countries: how to enforce?
- Certification of SO: template?

Demand Reduction Regulation:

Temporary crisis measure, Art 122(Council; no EP)

- Reduction during “reduction period” (until 3/2023)
- MS “may” reduce by 15%
- MS “shall” reduce by 15% if alert (Council decision)

Implementation issues

- Demand reduction measures: which?
- NRA decisions in demand reduction

Electricity emergency measures (Reg.2022/1854) *("Robin Hood" Regulation)*

Temporary crisis measure, Art 122(Council; no EP)

- Mandatory peak demand reduction
- Surplus profit cap
- Redistribution to "customers"

Implementation issues

- Calculation of "surplus profits" – e.g. how to treat hedging
- Taxation vs energy regulation

1 Coordinated electricity demand reduction

- 5 % — Peak hours

- Mandatory
- 10% of hours per month identified as peak hours

- 10 % — Overall consumption

- Non- mandatory
- Taking account of consumers without smart meters

2 Revenue cap for low-cost power generation

180 EUR/MWh

- Same level for all inframarginal generators
- Level above LCOE - does not deter investment
- All timeframes and all markets

EUR 117 billion/y

- Targeted support to households and (aid) businesses
- Demand reduction measures
- Support the energy transformation

3 Solidarity contribution from fossil fuel companies

- Collected on excess profits in 2022
- Covers profits which are above a 20% increase on the average profits of the previous three years
- Member State governments will collect these revenues Estimated to generate around €25 billion to help bring down energy bills

Gas emergency measures (proposal of 18.10.22) => gas sharing, energy platform, price measures

Temporary crisis measure, Art 122(Council; no EP)

- Demand aggregation platform: *mandatory*; joint purchasing: *voluntary*
- Default conditions absent solidarity agreements; clarifications on protected customer/essential generators; arbitration in C/B disputes
- ‘Price correction’ mechanisms

Implementation issues

- Meant to incentivise solidarity agreements between MS
- Key elements (related to prices -Art 23 & to gas allocation -Art. 25) still to be developed

EU energy

+ Add to myFT

Energy crunch threatens to shatter European unity, warns IEA boss

Fatih Birol says a continental scramble for winter fuel supplies would unleash a ‘wild west scenario’

Fatih Birol, head of the Paris-based International Energy Agency, said that ‘Russia has lost a good client, and forever’ as Europe seeks alternative gas sources © Ritzau Scanpix/Claus Fisker/Reuters

Comments on the EU Gas Storage Regulation and Joint Gas From Storage to Purchasing Mechanisms

- **The Storage Regulation amendment of July 2022 [**Reg 2022/1032] **was it a good idea?**

Will the EU have sufficient gas for winter 2022. Probably yes

For 2023? And beyond? Probably not

What criteria do we assess the mechanism by?

Targets, sources and subsidies

- By October 2022, the average gas storage filling level among member states **was over 92%**
- Germany, hardest-hit by Russia's reduced gas flows - set a higher goal for itself and aimed to be at 95% full by November.
- The EU imported 21.36 million tonnes of LNG in the first half of 2022, up from 8.21 million tonnes in the same period a year ago
- Private firms are primarily responsible for storage injections. European governments offered range of incentives such as credit lines, loans and subsidies to buy gas as prices hit record highs
- So EU on track to reach a gas storage filling target by the start of 2022 winter, at a cost of replenishing stocks estimated at over 50 billion euros ($51 billion), <u>10 times more than the historical average of filling up tanks for winter.</u>

Record profits for the lucky few! Robin Hood rules?

- ‘Gargantuan profits continue to roll in at Europe’s energy giants’.

- Nov 1: BP – doubles third- quarter profits on back of gas trading

- Nov 1: Saudi Aramco joins oil results bonanza with 39% jump in net income

- London-based Shell reported adjusted earnings of $9.45 billion for the third quarter, its second-highest profit on record. On the same day, Paris-based TotalEnergies reported a profit of $9.9 billion.
- For both companies, the profits were more than double what they earned in the same period a year ago.

- TTF prices record high and then fall: TTF month ahead price has collapsed from a peak of 339 €/MWh on Aug 26th to 113 €/MWh on Oct 18th. ‘A mild start to winter and continued strength in LNG deliveries has helped further build already healthy European stock levels, reducing expectations around the scale of the required demand response this winter’

For 2023 and after…. Flexibility or Rigidity?

- ACER and CEER recommended determining the EU filling target and filling trajectories according to **the level of expected demand**; **regional vulnerability assessments** should be carried out to calculate the appropriate volumes of gas to be stored on 1 November….
- This ratio could serve as a basis for setting the EU filling target starting from 2023.
- A proper monitoring system, covering both volumes (filling levels) and prices, must be in place as of day 1 **in order to control the level of cost for EU taxpayers.**

2023 – 90% target

- The magnitude of Russia's gas supply cuts in 2023 will be a key determining factor both for the European and global gas balance [Ukraine and Turkstream transit routes still operational?]

- Only limited LNG liquefaction capacity coming online next year-> LNG supply would not be enough to offset the shortfall in Russian gas deliveries.
- Additional pressure on the 2023 summer market, when injections will need to speed up to fill up storages at least to 90% capacity, and above that in certain markets (e.g. 95% in Germany).

Gas Price Caps? – opening the pandora’s box ?

Wholesale Gas Price Cap

Initial steps of the Commission were cautious, leading to ever stronger calls by Member States for effective action to constrain the effect of high gas prices:

Communication 13 October 2021: Toolbox, subsidies to vulnerable customers

Communication 8 March 2022: Guidance on regulated prices to retail customers and ‘clawbacks’ under strict conditions

Communication 23 March 2022: outlining options, underlining importance of maintaining marginalist electricity system

Subsequent measures address the effects of high gas prices on electricity markets, but do not deal with gas prices per se:

May 2022: Introduction and approval under the State aid rules of the Iberian model

Regulation 30 September 2022: Regulation on energy prices agreed by the Council, requires mandatory claw-backs, electricity infra-marginal price cap

oil and gas profit claw-back

The next regulation: the proposed aggregation process and the Joint Platform – next Council meeting on13 Dec

- New measures - should first and foremost coordinate the filling of gas storage facilities, in line with targets.
- **For the next winters until 2025, including the 2023-2024, a gap of uncontracted demand of up to 100 bcm per year is estimated in case of a full interruption of Russian supplies.**
- "… this mechanism to jointly purchase gas would benefit from market leverage from joint purchasing and help ease the uncertainties and abnormally high prices seen in the last filling season this year"
- To enable joint purchasing, especially for the filling of gas storages, the EC proposes:

• **First step**: Demand aggregation at EU and Energy Community partners level, grouping together gas import needs and seeking offers on the market on that basis;

• A mandatory participation by Member States in the EU demand aggregation for at least 15% of their storage filling obligations;

• **Second step**: A voluntary purchasing system, allowing companies to form a European gas purchasing consortium

**private undertakings will remain parties to the contracts for gas supply established under the joint purchasing.

The Council President and 15 Member States have repeatedly called on the Commission to propose an ‘ambitious’ wholesale gas price cap.•
Various Commission Non-papers outline options, but identify problems rather than solutions:

How to cover LNG (high enough cap? simply exclude?)

How to deal with OTC and other non-EU exchanges?
How to allocate scarce capacity faced with a supply shortage?

Likely reaction of pipeline (and LNG) suppliers?

"Gas cap" – what do we mean?

1. Wholesale or *retail "cap"* ? (Gaspreisbremse, "Wumms")

2. Gas cap or Gas subsidy? (Iberian model)

Lower prices by eliminating barriers to internal market?
Export bans (RO & Co); "political" bidding Zones; odo-urisation etc.

7. <u>Joint purchasing</u> (<u>non-binding tendering</u>? Or also Purchasing? Mandatory?)

8. Price cap <u>*after emergency*</u> (not if markets still working?)

9. "Hard" price CAP at hubs (Impact: LTCs?)

Activate Demand Reduction?
Declare EU Alert ?

3. Price cap via import ban? (RU? Others? LNG? only)

5. Import price cap (RU? All?)

10. "Soft"/dynamic hub CAP (FSR) (LTCs? SOS?)

11. <u>'Circuit Breakers' at hubs</u> (<u>Short-term? Mid term?</u>)

4. Price cap via tariffs /levy? (RU? Others? LNG?)

6. <u>Cap through Diplomacy</u> (Who?)

12. <u>Better Benchmarks for gas prices</u> (Possible/Imposed?)

* underlined: Included in COM proposal of 18.10.22

Market Correction Mechanism

Would set a price ceiling of €275 on month-ahead Dutch TTF derivatives. This ceiling would be triggered if two cumulative conditions are met:

- the front-month TTF derivate settlement price exceeds €275 for two weeks;
- TTFprices are €58 higher than the LNG reference price for 10 consecutive trading days within the two weeks.

Temporary instrument to intervene in the case of excessive gas price spikes -“super peaks”

Once these conditions are activated, ACER will immediately publish a “market correction notice”.

Orders exceeding the price ceiling will not be accepted.

Notable elements: Not aimed at structurally decreasing prices; temporary, targeted & exceptional instrument
OTC and LNG trades unaffected
Effects on security of supply remain uncertain
A number of Member States have requested the Commission to re-propose the market correction mechanism before adopting the entire gas package –continued push for a structural wholesale gas price cap

Mechanism may be activated from 1 January 2023.
Two ways to deactivate:
▪Automatic deactivation if the difference between the TTF price and the LNG price reference) is no longer met for 10 consecutive trading days.▪
Suspension decision which can be taken by the Commission

State Aid Control

- Large scale national intervention but light touch EC control?

State Aid Section 4.1 CEEAG – Aid for renewable energy

- Scope: Aid for all types of renewable energy
- Incentive effect
- No breach of any relevant provisions of EU law
- Necessity of the aid: project would not be carried out without the aid
- Appropriateness: presumption of achievement of decarbonisation goals
- Eligibility, e.g. compatibility with sectoral targets
- Public consultation
- Proportionality: in general competitive bidding process, exceptions for tax measures/SMEs/award of concessions
- Avoidance of undue effects on competition and trade: maximum 10 year duration
- Weighing the positive effects of the aid against the negative effects on competition and trade

TCF Section 2.5 – Aid for accelerating the rollout of renewable energy, storage, and renewable heat relevant for REPowerEU

- Aid for generation of renewable electricity/energy: key conditions
  - Technology-neutrality, no limitation by size of projects, locations or regional aspects
  - Direct grants, repayable advances, loans, guarantees, tax advantages
  - Aid scheme with an estimated volume and budget
  - Aid granted by 31 December 2023 at the latest; obligation to go into operation within a given timeframe; reimbursement in case of delays
  - Maximum duration of 20 years
  - In general: competitive bidding process; exception for tax advantages/smaller projects
  - Maintaining operating incentives and price signals (e.g. Contract for Difference)
  - Projects may have started before 20 July 2022
- *New:* Aid for increasing maximum capacity for existing installations without further investments

THE TEMPORARY FRAMEWORK

	CEEAG	TCF
Legal basis	Art. 107(3)(c) TFEU	Art. 107(3)(c) TFEU
Purpose	Guidance on how COM will assess energy measures subject to notification	Further simplification for the implementation of support measures on a temporary basis
Incentive effect, necessity of the aid	Identification of the factual and counterfactual scenario	Presumption that beneficiaries would continue their activities without changes
Public consultation	Section 4.1.3.4 applies from 1 July 2023	Not required
Competitive bidding process	Extensive list of requirements - avoid carbon lock in and stranded assets	Simplified requirements, thresholds for SMEs similar to CEEAG
Miscellaneous	[no equivalent]	Reimbursement obligation in case of delays

Euratom – ESA as precedent?

- Euratom Treaty - Articles 52 -72
  - » [*https://euratom-supply.ec.europa.eu*]
  - » ESA focuses on enhancing the security of supply of users located in the European Union and shares responsibility for the viability of the EU nuclear industry. In particular, it recommends that EU utilities operating nuclear power plants maintain stocks of nuclear materials and cover their needs by entering into long-term contracts with diversification of their sources of supply.
- ESA can work (in the centralized procedure) as a clearinghouse (with veto powers) as opposed to lead EU negotiator to increase buyer power. NB compulsory character of the ESA mechanism which, together with the legal obligation to ensure equal access, would certainly protect smaller buyers in periods of scarcity

  (and reduce admin costs).
- RULES of the Supply Agency of the European Atomic Energy Community determining the manner in which demand is to be balanced against the supply of ores, source materials and special fissile materials. (OJ 2021 L218)