

EFET commentary on the Clean Energy Package for All Europeans



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TABLE OF CONTENTS

I. <u>INTRODUCTION</u>	2
II. <u>LEGISLATIVE FRAMEWORK FOR THE WHOLESALE POWER MARKET</u>	3
III. <u>NEW LEGISLATIVE DISTINCTIONS BETWEEN CATEGORIES OF MARKET PARTICIPANTS</u>	10
IV. <u>SYSTEM OPERATOR UNBUNDLING AND STORAGE OPERATION</u>	13
V. <u>RETAIL MARKET</u>	15
VI. <u>TREATMENT OF RES-E</u>	15
VII. <u>GOVERNANCE OF THE INTERNAL ELECTRICITY MARKET</u>	17
VIII. <u>CAPACITY MECHANISMS</u>	19

I. INTRODUCTION

The European Federation of Energy Traders (EFET) generally welcomes the Commission's legislative proposals bundled together as a Clean Energy Package for All Europeans. Since 1999, EFET has accompanied legislative and regulatory developments contributing to establishment of a European single market in electricity. We believe that the proposal of the European Commission puts the European Union in a capacity to fulfil the 2015 mandate of the European Council to strengthen the Energy Union, and ensure security, sustainability and competitiveness in the supply of electricity in the EU.

Overall our evaluation of the Clean Energy Package is positive. **We welcome the emphasis on the use of market-based mechanism and on improving the quality of price signals in the electricity market. We also welcome the European Commission's intention, by putting the consumer at the centre of the legislative package, to ensure that the benefits from liberalisation that we already see at European level trickle down all the way to the final end-users.** In the main body of this paper, we underline some of the key principles that have appropriately been maintained from the Third Package, and a few key novelties we deem significant steps forward for the proper functioning of integrated electricity markets.

Our general satisfaction, however, is tempered by a few surprising omissions and inconsistencies in the draft package. **Indeed, the draft legislation creates confusion in terms of the roles, rights and responsibilities of the various actors in the electricity market. While it strives to remedy some of the distortions introduced by previous legislation by way of differential rights as between renewable energy producers and other market participants, it opens the door for the creation of new privileges for alternative business models. Finally, it sometimes goes into a level of detail that we are surprised to see in primary European legislation of this kind, or which we doubt is compatible with the subsidiarity principle of the European Treaties.** We elaborate below on the most troublesome of these issues, which require immediate action from the parties involved in the adoption of the Package.

With our detailed recommendations in the main body of this document, we aim to pursue our work of the past decade and a half: the promotion and facilitation of a thorough liberalisation of the power sector and the harmonisation of national frameworks. Our proposals target **the establishment of a truly open, transparent, sustainable and liquid wholesale market in electricity, unhindered by national borders, secular commercial interests or distortive industrial policies.**

II. LEGISLATIVE FRAMEWORK FOR THE WHOLESALE POWER MARKET

1. Imports and exports of electricity within the IEM

A true Europe-wide wholesale market free of distortive national interventions and national variations in market design is not yet a reality. Increasing volumes of renewable electricity output, the generators of which enjoy national financial support, are dispatched without regard to market price signals, except in times of extreme negative prices, and irrespective of the incidence of cross-border congestion in too many EU Member States, still. Additionally, in respect of cross-border trade in those power volumes not enjoying priority access and dispatch, market participants continue to experience disruptions in the form of export bans, export related transmission fees, and opaque restrictions on the availability of cross-border transmission capacity imposed by TSOs.

With these current distortions and disruptions in mind, we are worried about the disappearance of the **former Annex 1 to the EU Regulation on the internal electricity market, the so-called Congestion Management Guidelines**. These Guidelines have enshrined the basic principles for the conduct of cross-border electricity trading since 2003 in a dedicated instrument that aggregated these principles while being part of the Regulation. Some of the basic rights and obligations which were set out in the Guidelines seem to have been reformulated in the text of the draft, recast Regulation for the electricity market; others have been dealt with already in the FCA, CACM and EB Guidelines. Given the importance of the Congestion Management Guidelines as a concise instruments that summarises all the basic principles for the conduct of cross-border electricity trading in Europe, we request that the European Commission publishes a comprehensive mapping of where the original articles of the original Guidelines have moved to, and a justification for any relegation of certain provisions to subordinate legislation (network codes and binding guidelines).

On a more fundamental note, in **Article. 3.1 of the draft recast Directive**, the emphasis at the outset of the recast piece of primary legislation should not be on facilitating cross-border *flows*, rather on facilitating cross-border **transactions in electricity**. The blocking of interconnection capacity, by supposedly embedded loop flows and flows induced by generation assets exempt at national level from the discipline of market forces, lies at the heart of what has gone wrong in recent years with cross-border transmission capacity calculation and allocation.

2. Use of cross-border transmission capacity and congestion management

We welcome the conservation of the principle that TSOs must maximise the availability of cross-border transmission capacity in **article 14.3 of the draft recast Regulation**, with explicit wording on the need for TSOs to use counter-trading and redispatch, including cross-border redispatch, to maximise available capacities unless it is demonstrated that it is not beneficial to economic efficiency at Union level.

This principle is reinforced by **Article 14.7 of the draft recast Regulation** that states that TSOs shall not limit the volume of interconnection capacity to be made available to market participants in order to solve congestion within their own control area or to manage loop flows unless this is just by system security concerns or where it is beneficial to economic efficiency at Union level, and agreed at Capacity Calculation Region level. This article generally reflects the elements of the ACER Recommendation of November 2016¹, save for one important detail: in its Recommendation, ACER insists that the derogations to the principles should only be approved if it is necessary to maintain system security *and* if it is economically more efficient. This is a critical difference, where we expect the ACER wording to ensure that any TSO decision pertaining to capacity calculation, which by definition would have an impact on system security, should be taken on the basis of a transparent cost-and-benefit analysis. Finally, the ACER Recommendation proposes a review of the inter-TSO agreement on cost sharing to ensure that expenditures linked to the management of loop flows is allocated to the control areas that are at the origin of these (so-called “polluter pays” principle). We understand **Articles 46 and 57 of the draft recast Regulation** as an obligation for Member States to push TSOs to perform an appropriate review of their cost-sharing agreement. A review of the inter-TSO agreement on cost sharing is key for the success of the new capacity allocation rules of Article 14, as it will ensure that the avoidance of redispatching costs is not the only guide for TSO decisions on capacity allocation and remedial actions. The Member States and the European Commission should proactively see to the effective implementation of the combination of Articles 14, 46 and 57 of the draft recast Regulation.

We also welcome the strengthening of the rules regarding the transparency in the use of congestion income by the TSOs in **Article 17.2 of the draft recast Regulation**. The new provision builds on the principle of the existing article 16.6 that requires TSOs to use revenues resulting from the allocation of interconnection to guarantee the actual availability of the allocated capacity and/or maintain or increase interconnection capacities through network investments, in particular in new interconnectors. The new article 17.2 restricts the use of congestion income by the TSOs for other purposes by requiring TSOs to place congestion income that exceeds

¹ ACER Recommendation 02/2016 on the common capacity calculation and redispatching and countertrading cost sharing methodologies, published on 11 November 2016, available at: http://www.acer.europa.eu/Official_documents/Acts_of_the_Agency/Recommendations/ACER%20Recommendation%2002-2016.pdf.

² As an example, the Danish regulator cancelled a 100 MW reservation of cross-border transmission capacity for exchange of aFRR between Norway and Denmark in April 2017 due lack of demonstrated socio-economic return.

³ According to the CEER Status Review on the Implementation of Distribution System Operators' Unbundling Provisions of the 3rd Energy Package, “If compared with the unbundling rules for TSOs, which were thoroughly revised under the 3rd Package, resulting in new, more far reaching unbundling requirements, the unbundling requirements for DSOs have only been slightly reinforced in the 3rd Package. Another difference between DSO

the need of the above-mentioned purposes (congestion management actions and network investments) on a dedicated account line for future use on these purposes. We understand the intentions of the European Commission, i.e. to avoid that congestion income that is at one point in time in excess of congestion management or investment needs is directly reallocated to reduce network tariffs, without regard for longer-term consequences. Indeed, this reallocation of congestion income to network tariffs is currently allowed by article 16.6 and has been used repeatedly, if not constantly, by certain TSOs. The consequence of this is that when investment funds are needed, instead of tapping into (by then depleted) congestion income revenues, TSOs finance themselves through state-backed or tax-privileged loans, at the expense of the taxpayer.

However, the proposal of the draft recast regulation seems quite drastic, as it could have the consequence of TSOs holding sums of money for unlimited periods of time even if the financial needs for congestion management and investment are consistently below the TSOs' congestion income. This money would then sit with TSOs, or be invested by TSOs, rather than being used productively in the unregulated economy. Instead, we would advocate a clear hierarchy. Congestion income should be used:

- first to ensure firmness of already allocated cross-border transmission capacity;
- second to fund operational measures enabling a higher allocation, consistent with the maintenance of security standards and of an economically efficient nature;
- third, to fund investments that have been deemed to be economic according to a cost-benefit analysis.

If congestion income remains and (i) firmness of already allocated cross-border transmission capacity is ensured, (ii) no efficient redispatching/countertrading operation can be done to increase the availability of cross-border capacity, and (iii) no investment activity is planned, then the congestion income could be used to reduce transmission tariffs after a period of two to five years. We also expected that this set of rules would help guarantee that TSOs take all necessary, possibly costly remedial actions to ensure the availability of cross-border capacity at all times, take investment decisions when economically warranted, and do not unnecessarily hold capital when it can be returned to end-consumers if it is not needed for the proper functioning of the electricity market and system.

3. Re-dispatch of generating plant by TSOs: relationship to the market and economic impact

We are concerned by the provisions of **Article 12 of the draft recast Regulation** on redispatching and curtailment. We generally support the key principle of using market-based mechanisms to determine the incidence of and payment for curtailment or redispatch. We however also recognise that due to the local necessity to adjust the generation schedule affecting specific facilities, the establishment of actual markets for redispatch may be complex, and in some cases neither possible nor desirable. For this purpose, sub-article Article 12.2 also foresees the possibility of regulated compensation for redispatch. However, one need to ensure that the circumstances allowing the regulated compensation for redispatch instead of market-based mechanisms are not too broadly described and defined.

In particular, we are concerned that the proposed wording of sub-article Article 12.6 envisages compensation which may end up under-valuing the loss of output: **Article 12.6(b) of the draft recast Regulation** foresees as an option that non-market based curtailment or redispatch could be compensated taking 90% of the net revenues from the sale of electricity in the day-ahead market that the generation of demand facility would have earned without curtailment or redispatch. We consider this proposal not acceptable as it constitutes an arbitrary measure, with no explanation of the European Commission where the 90% figure stems from. In fact this would certainly result in compensation below the actual costs incurred by the owner or operator of the asset as a result of the redispatch measure. Such an arbitrarily set formulae cannot reflect the complexity of redispatch measures and their related costs.

We therefore urge that draft recast Regulation should only determine the general principle for the design of redispatch compensation rules, i.e. that asset owners that are subject to curtailment or redispatch measures must be compensated in such a way that they are left financially indifferent, taking account of opportunity costs as well as actually incurred costs. This principle ensures the equal treatment of all market participants and avoids that individual market participants are discriminated as a result of local congestions.

4. Bidding zones delineation

EFET is an active and constructive contributor to the review of bidding zones initiated by ACER and currently carried out by ENTSO-E according to the CACM GL. We acknowledge that the current delineation of bidding zones is rather a heritage from the past, with bidding zone borders often following Member States borders, and that a regular review of bidding zones is a relevant exercise. However, we have also repeatedly insisted that changes to bidding zones should only be carried out following careful consideration of not only of network congestion, but also of long-term economic efficiency. Any proposal to re-delineate bidding zones following a review should be carefully handled, take into account the likely evolution of market fundamentals (changing fuel mix, prices etc.), and allow for planned future generation, demand response and storage investments and future grid

reinforcement. Also, the stability of bidding zones over time is of particular importance to ensure the relevance of price signals and the existence of true hedging opportunities on the forward market.

We are therefore concerned about the new **Article 13 of the draft recast Regulation** that seeks to simplify and bring about a quicker implementation of bidding zone reviews. **Article 13.6 of the draft recast Regulation** takes the final decision on the delineation of bidding zones away from Member States and makes it a decision of the European Commission. It is not clear why it is deemed necessary to reform this process already as even the first bidding zone review initiated according to the CACM GL has not yet been finalised.

The risk of repeated bidding zone changes in the short or medium term (even without these changes actually taking place) undermines the functioning of the forward power market and impairs the scope for that market to give locational generation investment signals. Ultimately the frustration, due to the unforeseen imposition of basis changes, of forward hedges entered into on a cross-border basis will be to the detriment of consumers of electricity. Furthermore, decisions about investment in, refurbishment of and divestment of generation, demand response and storage assets, become more difficult in an environment where bidding zone boundaries might change at short notice.

We believe that the existing process in Article 32.4(c) of the CACM GL is an adequate instrument to ensure that Member States effectively performs their duties as guarantors of security of supply according to Article 194 of the Treaty on the Functioning of the EU. It also ensures that Member States play a role in balancing the interests of system security, market efficiency and consumer protection when changes to bidding zones delineation are being discussed. Therefore, we suggest the removal of **Articles 13.6 to 13.8 of the draft recast Regulation**.

5. Forward and future transactions in electricity

We are concerned by the lack of attention throughout the Clean Energy Package to the forward market: forward and future contracts still represent over two thirds of wholesale power transaction volume on the electricity market in Europe. Indeed in the countries and regions most open to competition and benefiting from multiple interconnections the proportion is over 85 %. We share the assessment of the European Commission that the growing penetration of intermittent power generation leads to a greater need for the deployment of flexible capacity. We also agree that, as aging large-scale traditional power generation plants are decommissioned, and the total generation capacity surplus correspondingly diminishes, the potential flexibility of new generation and storage technologies will increase in importance. Greater use of demand response is to be welcomed in addition. The liquidity of short-term markets should be able to benefit from inclusion of each of these sources of flexibility.

However, the basic facts of the intermittency of an ever larger proportion of baseload generation capacity, the reluctance or inability of many consumers to adjust their demand and the high cost of newer technologies points to increasing volatility of wholesale electricity prices close to real time. Exposure to volatile short run prices reinforces the importance to market participants of long-term hedging opportunities. Both OTC markets and organised trading venues already witness the development of short period activation products on a forward basis to help generators, retail suppliers and larger consumers cope with greater uncertainty in final price outcomes for marginal volumes closer to real time.

Therefore **Article 8 of the draft recast Regulation** should at the start clearly recognise the value of forward and future markets, not only for their price hedging function, but also as guarantors of competition and providers of pools of liquidity. Such explicit recognition can help policymakers, legislators and regulators re-assert their confidence in the ability of the energy-only market to provide longer term price signals, to help underpin investment decisions in all technologies of power generation, demand response and storage. In addition, Article 8 ought to include a similar provision to that which can be found in **Article 6.2(h) of the recast Regulation**, ensuring that also forward markets shall “*make no distinction between trades made within a bidding zone and across bidding zones*”.

6. Balancing and ancillary services market

Only a few weeks after the adoption of the Electricity Balancing guideline, it is useful to reiterate the fundamental principles that govern the balancing market and the procurement of ancillary services. Therefore, we welcome the wording of **Article 5 of the draft recast Electricity Regulation**, and notably the principles of open and non-discriminatory access of all market participants, as well as the principle of separate procurement of balancing energy and capacity. The provision of Article 5.10 is also a welcome addition to ensure the transparency of the balancing market, the price signal of which all markets in previous timeframes rely for dispatch and investment decisions.

Though we welcome the provision of **Article 5.4 of the draft recast Regulation** insisting on the need for “*maximum use and efficient allocation of cross-zonal capacity*” within the boundaries of system security, we insist that along the lines of Article 6.2(h), this paragraph also ensures that no distinction be made between trades made within a bidding zones and across bidding zones.

We reserve our comments on the question of the cross-border dimensioning and procurement of balancing capacity in **Articles 5.7 and 5.8 of the draft recast Regulation**, which pose the question of how to achieve these goals without the TSOs reserving cross-border transmission capacity for the balancing timeframe, which we strongly oppose. Indeed, reservation by the TSOs of cross-border transmission capacity for balancing purposes takes away trading opportunities from

the market in the intraday, day-ahead and forward timeframes, and relies on ex-ante TSO analyses that have proven very hard to get right².

We are in favour of markets for reserves being increasingly opened for cross-border competition. The market should remain the primary driver when evaluating at which point in time cross-border transmission capacity has the highest value. A very high value close to real time may indicate that a small fraction of cross-border transmission capacity could be set aside before the opening of the day-ahead and intraday markets for bidders for a balancing service. In this case, we could imagine a model where market participants can create bundled reserve products (reserve plus transmission) to meet the technical requirements for the reserve product requested by a TSO and offer the service also to TSOs on the other side of a bidding zone border. This would require the possibility to procure PTRs not subject to a use-it-or-sell-it condition in day-ahead, and the recognition on both sides of the relevant border of a BSP-TSO balancing market model, which we recognise is not the current target model. Such a model could have the benefit of revealing more accurately both the value of cross-border transmission capacity across timeframes (a limited volume of PTRs for intraday trade might in due course be included in a scheme, subject to the same type of assessment of market value) and the value of the reserve products for which various TSOs tender.

We have concerns regarding the proposal to shorten the timeframe for the procurement of reserves in **Article 5.9 of the draft recast Regulation**. This provision specifies that balancing capacity procurement must be performed on a day-ahead or intraday basis. We understand the goal of the legislator to facilitate shorter-term procurement in order to enable a greater participation of intermittent generation and demand in the ancillary services market. However, we believe there is still a rationale to maintain at least part of the procurement of reserve capacity with a longer time horizon, both to ensure an easier management of the system by TSOs and to reduce the cost of reserves procurement, which is borne by the end-consumer through network tariffs. As a consequence, we would recommend amending the paragraph to ensure that part, but not all of the balancing capacity procurement is performed on a day-ahead or intraday basis and shall have a maximum contracting period of one day.

² As an example, the Danish regulator cancelled a 100 MW reservation of cross-border transmission capacity for exchange of aFRR between Norway and Denmark in April 2017 due lack of demonstrated socio-economic return.

III. NEW LEGISLATIVE DISTINCTIONS BETWEEN CATEGORIES OF MARKET PARTICIPANTS

1. Use of terms and definitions in the new legislation

We welcome the greater focus the Clean Energy Package puts on consumers. However, we believe the extra attention to end-consumers, which the European Commission proposes to devote within the EU internal electricity market legislative framework, should result in a widening of the scope of the legislation, not a shift in emphasis. The level of detail that the European Commission intends the recast Directive on common rules for the internal market to reach on the subject warrants very clear definitions to ensure that the widening of the scope of European legislation leads to effective protection and empowerment of energy consumers.

Therefore, we believe that greater attention is needed **throughout the draft recast Directive, and in particular in Article 2 and the entire Chapter III**, to the use of terms denoting various market actors. As an example, different categories of “customers” are defined in Article 2 of the draft recast Directive, but the terms “consumers” or “end users” are still used in the text. Likewise, “market participants” are sometimes labelled as “system users”, sometimes as “customers”, the latter term being muddled up at certain points with the term “final customer”. Finally, the terms “suppliers” and “aggregators” appear as mutually exclusive in some articles, in others not.

Also, the Commission is pursuing the improvement of flexibility as a goal. Flexibility is often defined as “the capability of a system to balance rapid changes, for example caused by intermittent renewable generation.” Such a definition would not be sufficiently precise. Flexibility is not just the capability to respond to *rapid* changes. The system must be able to respond to situations of scarcity for several days in a row (e.g. caused by low wind, low reservoirs, high demand, etc.). Flexibility should therefore be defined as *the capability to use capacity with few or insignificant limitations, and capacity is the option to take (consumer) or deliver (generate) electricity*. Where there is a need for flexible capacity, it will be rewarded in a well-functioning electricity market. Flexibility (or better put: flexible capacity) can be of specific value in each of these segments. This also means that flexibility is not a separate commodity that needs to be traded on a separate market. Therefore, we warn the legislators against the promotion of specific actors which would be supposed to represent a certain form of flexibility. Ensuring that the market is fully functioning is the best way to achieve the desired level of flexibility needed by the system, and to adapt to changing conditions.

2. Balancing responsibility and aggregation

We welcome the clear statement of **Article 4 of the draft recast Regulation** that all market participants shall be financially responsible for imbalances they cause in the system, either directly or indirectly. **Article 5.2 of the draft recast Regulation** reinforces this provision by insisting that “*balancing markets must be organised in such a way as not to discriminate between market participants*”. These obligations ought to apply to all: no participant in the market shall be immune from the basic discipline of balancing responsibility, either directly for Balancing Responsible Parties (BRPs), or indirectly for market participants that do not have a direct balancing contract with the TSO.

Therefore, we believe that provisions such as **Article 17.4 of the draft recast Directive** that foresees that “*Member States may exceptionally allow compensation payments between aggregators and balancing responsible parties in order to ensure that balancing costs and benefits induced by aggregators are fairly assigned to market participants*” are not coherent with the principles of the recast Regulation. Proposing that balancing responsibility, either direct or indirect, can only be applied exceptionally to a certain category of market participants falls short of providing the level-playing field that the Clean Energy Package intends to set out in terms of the roles and responsibilities of market participants, as laid out in the Explanatory Memorandum of the recast Directive: “[The Directive] ...addresses rules that discriminate between resources and which limit or favour the access of certain technologies to the electricity grid. In addition, all market participants would bear financial responsibility for imbalances caused on the grid and all resources would be remunerated in the market on equal terms.”

3. Contractual rights and obligations in the supply and consumption of electricity: aggregation and communities

We fully support the objective, embedded in various provisions of the Clean Energy Package, that generation, storage and demand response should compete on a level-playing field. We applaud the overall emphasis of the proposals on the use of market-based mechanisms and on the efficiency of price signals that should facilitate development of both implicit and explicit demand response. However, in its commendable encouragement of demand response, we fear that the proposals of the European Commission could lead to misapprehensions in the implementation of the Directive, and possible distortions of the basic principles of the law of contract.

a. Demand response, including aggregation

To start with, we insist on the freedom of end-users when it comes to opting or not to commercialise their demand response potential, as well as to choosing how and with whom they wish to do so. In order to ensure the right of demand response providers, including demand response aggregators, to propose their services to any consumer, their right to freely enter in and exit from the market should be more clearly set in stone. Hence, we recommend reinforcing **Article 3.2 of the draft recast Directive** by

including these market participants in the list of actors whose freedom to enter in and exit from the market should be guaranteed, alongside electricity generators and suppliers.

Second, we believe that the principle of free negotiation between participants in the market should be upheld. When a third-party aggregator is involved, EFET strongly supports the negotiation of bilateral arrangements between the parties involved – consumer, supplier and third-party aggregator – to establish the elements that rule this trilateral relationship, including the exchange of information regarding demand response activation, and possible payments between the parties. Such free negotiations are the best assurance that the energy is valued correctly, that the various actors of the trilateral relationship are not adversely impacted by the actions of the others, and that market prices are not distorted by a regulated price. Should commercial negotiations not be handled in good faith, then Member States ought to act on the basis of our proposed redrafting of Article 3.2 of the draft recast Directive (see above) or competition law to ensure a true level-playing field between market participants. We believe that the Clean Energy Package, as market design legislation, is the place to ensure that all possible business models have an equal access to the market, but not the place to introduce provisions aimed at overcoming the inappropriate implementation of Third Energy Package rules or to tackle anti-competitive behaviour.

As a consequence, we also challenge **Article 17.3(d) of the draft recast Directive**, which deems aggregators immune from claims for compensation from suppliers or generators following the activation of load shedding from their portfolio of clients. Normal and legally accepted commercial practice dictates that market participants willing to sell a product must bear the costs related to producing or procuring this product. This rule is valid for the electricity sector: for instance, when generators are selling electricity, they must produce it; when traders are selling electricity, they must buy it from another market participant. When an aggregator not acting as supplier to a final customer diverts energy through a demand response activation to make it available to the TSO, this energy is still sourced and injected onto the grid by the supplier or generator of the activated customers and will be used somewhere else in the system.

We insist thus that, as with any other transaction in the market, the supplier or generator should – in this specific case – be allowed to request from the third-party aggregator remuneration for the energy that has already been produced by the generator or sourced by the supplier using a market-based valuation. Hence, we would recommend a clarification of **Article 17.3(d) of the draft recast Directive** that aggregators must remunerate generators for the electricity they produced or suppliers for the electricity they sourced and that is being used by the aggregator when activating its clients, but that the aggregators shall not be required to pay any additional indemnification to suppliers or generators. This clarification would avoid that the implementation of the recast Directive at national level creates a hidden subsidy to a particular type of demand response provider category.

b. Local energy communities

On a parallel note, we fully support the aim that the electricity market design shall not hamper the development of other innovative business models and initiatives, such as renewable energy communities (**Article 22 of the draft recast Renewable Energy Directive**) and local energy communities (**Article 16 of the draft recast Electricity Directive**). The key objective of European legislation should be to ensure no Member State forbids the establishment of local or renewable energy communities throughout the Union. For this reason, we recommend again a reinforcement of **Article 3.2 of the draft recast Directive** to include the establishment of local energy communities.

However, the level-playing field between all types of business models should be maintained. The proposed wording of **Article 16.2 of the draft recast Electricity Directive** (“Member States shall provide an *enabling* regulatory framework”) makes us fear that the European Commission seeks to promote this particular model in preference to other business models. If a regulatory framework elaborated in a Member State would reflect such a preference, which might well lead to discrimination against other market participants. An enabling framework must in no event jeopardise third-party access to networks, decentralised dispatch decisions nor the right to bid into markets on a portfolio basis. Furthermore it should not undermine consumer protection measures. Residential consumers of power and gas deserve the continued benefit of such measures, whether they receive their energy as part of a local energy community or a RES community, or from a traditional supplier.

Moreover, the promotion of local or renewable energy communities would favour a specific business model, which largely relies on the avoidance of sales related taxes, renewable energy levies and network charges. The implication of the development of this model regarding the financial burden on a shrinking pool of “standard” electricity consumers should be seriously considered.

The focus of legislation affecting the electricity market design, as the Clean Energy Package clearly does, should be to remove unduly restrictive regulation where the need arises, as opposed to privileging a specific type of initiative, business model or category of commercial activity.

IV. SYSTEM OPERATOR UNBUNDLING AND STORAGE OPERATION

1. General principles of unbundling for TSOs and DSOs

Strict unbundling rules are the corner stone of a sustainable liberalisation process in a network-backed industry like electricity. The separation of regulated monopoly system operation from all the other competitive activities in the sector ensures that Transmission System Operators (TSOs) in Distribution System Operators (DSOs) act as neutral facilitators of the market. In that sense, we very much welcome the insistence of the European Commission on this principle in the Clean Energy

Package in **Article 35 (for DSOs) and Article 45 (for TSOs) of the draft recast Directive.**

We believe, however, that the application of unbundling requirements on DSOs should be reinforced. Indeed, these requirements have generally been loosely applied³ given the perceived lesser risk of DSOs stepping out of their market facilitator role and acting as market participants until now. With the expansion of intermittent renewable power generation at distribution level, as well as the development perspectives for demand-side response and electricity storage, the question of the strict separation of competitive commercial activities from monopolistic system operation activities at a distribution level becomes of high relevance to maintain DSOs in their sole role of market facilitator. In this respect, we believe that the review of the Directive would be a good occasion to ensure that regulators have the tools to properly enforce DSOs' unbundling requirements.

2. Ownership and operation of storage assets by system operators

On the specific subject of electricity storage, we once again welcome the principle enshrined in **Article 36 (for DSOs) and Article 54 (for TSOs) of the draft recast Directive** that system operators shall not be allowed to own, manage and operate electricity storage facilities. Storage assets – in the same manner as generation assets or demand-response capacities – should never be considered as part of a network since they can be used for purposes other than system operation (in contrast to, e.g., transmission lines, phase-shifters or transformers). Hence system operators who see the need to rely on storage capacity to perform their duties should procure this capacity from market participants. We believe that market participants are best placed to provide cost-efficient storage solutions. The probability of system operator procurement of storage happening would improve the business case for investments in storage capacity, when considered from the point of view of market participants.

The same rationale should also apply to e-mobility charging points. As the electrification of the transport sector proceeds, the capacity of charging points and car batteries will become very significant and eventually also they will act as flexibility providers. Maximising the value of this such flexible capacity on the market would be at odds with the DSOs' role to facilitate the market and raise serious questions about their neutrality.

However, the principle of non-ownership and non-operation by system operators is stated to be subject to exemptions in **Article 36.2 and Article 54.2 of the draft**

³ According to the CEER Status Review on the Implementation of Distribution System Operators' Unbundling Provisions of the 3rd Energy Package, "If compared with the unbundling rules for TSOs, which were thoroughly revised under the 3rd Package, resulting in new, more far reaching unbundling requirements, the unbundling requirements for DSOs have only been slightly reinforced in the 3rd Package. Another difference between DSO unbundling and TSO unbundling lies in the new requirement for TSOs, which now have to be certified by the competent National Regulatory Authorities (NRAs) as being compliant with the unbundling requirements and to be designated by the Member States. Such a certification and designation requirement does not exist for DSOs." More information at: http://www.ceer.eu/portal/page/portal/EER_HOME/EER_PUBLICATIONS/CEER_PAPERS/Cross-Sectoral/2016/C15-LTF-43-03_DSO-Unbundling_Status_Review-1-Apr-2016.pdf.

recast Directive. In our view, these exemptions should not exist. If they are maintained, the limitations on the exemptions should be significantly strengthened: cost-efficiency analyses should be performed by the system operators to look at all alternative ways (not only storage) to solve the identified problem; tenders should be open to different types of technologies (not only storage) to respond to their needs; tenders should be established in such a way that the system operators are not the only ones that can fulfil their requirement; and tendering should last long enough to reduce costs for asset operators.

Legislators ought to keep in mind that should storage assets be operated by system operators, these assets would in most likelihood be structurally under-used, resulting in higher costs overall. On the one hand, this would diminish the value of the system operator-owned assets: unlike market participants, system operators would not be able to pool the capacity and output of different storage assets to sell them both on the market and use them for system operation, thereby increasing the price of storage capacity use for all users, including themselves. On the other hand, under-used system operator-owned storage assets would weaken the business case for private investments in storage assets, as it would suppress signals of the value of storage capacity on the market.

V. Retail market

We welcome the effort of the Commission to tackle the issue of energy poverty and to protect vulnerable consumers by other measures than price setting, in **Articles 28 and 29 of the draft recast Directive**. It is important to deal with these issues by social rather than energy policy measures.

Given this context, we also fully support the proposals aiming at making sure that retail pricing is market-based in **Article 5 of the draft recast Directive**. We particularly welcome the proposals related to putting an end to retail price regulation as such measures run counter to establishing a competitive and customer-oriented retail market. However, we believe that the five-year transitional period foreseen in **Article 5.3 of the draft recast Directive** is unnecessarily long, given the fact that abolition of price regulation had already been foreseen by the Third Energy Package. The market distortion caused by price regulation of electricity supply shall be removed as soon as possible. We also believe that there is a need to properly define cases of “*extreme urgency*” in **Article 5.4 of the draft recast Directive**, to ensure it is not used for continuation of regulation of electricity supply.

VI. TREATMENT OF RES-E

The Clean Energy Package provides a first step forward when it comes to both integrating renewable energy sources in the market, and making the market fit for renewables. In combination with the reform of the Renewable Energy Directive (RED II) which foresees the partial opening of RES financial support schemes to cross-border participation, **Articles 4 and 11 of the draft recast Electricity Regulation**

establish the principles of universal balancing responsibility, and the phase-out of priority dispatch for new installations, respectively. These rules combined will help speed up the integration of renewable energy sources into the market, while the reform of, inter alia, balancing markets launched with the Electricity Balancing Guideline will ensure that the market also accommodates all forms of power generation, demand response and storage.

However, **Article 4.2 and Article 11.2 of the draft recast Regulation** still open the possibility for exemptions of balancing responsibility and standard dispatch rules for installations of less than 500 kW. We believe that the legislation should go further and phase out network-related privileges for all renewables installations, or at the very least set a much lower threshold or limit the exemption to pilot projects in new renewable technologies. The current wording of the recast Directive would de facto exclude the vast majority of solar power installations from common market rules. It is also a counter-incentive to the aggregation of power generation from renewable energy sources, which the European Commission appears to promote to facilitate the integration of renewables in the market and asserts “*could help consumers save significant amounts of money*”.

We also observe that very few Member States have put measures in place to ensure that renewable energy generators have no incentive to generate electricity in times of negative prices, as laid out in point 3.3.2.1.b of the 2014 Guidelines on State aid for environmental protection and energy. We encourage the legislators to include provisions in this sense in the draft recast Regulation and the draft recast Renewable Energy Directive in order to enshrine this principle in primary legislation.

Article 12.5 of the draft recast Regulation also enshrines in EU legislation priority access for RES generators (and CHP operators): in case of non-market based redispatch, RES and CHP units would be the last ones to be curtailed or redispatched. We believe non-market based curtailment and redispatching should be a last resort option for TSOs (who should always use market measures first), and in this case system security should prevail as the main criterion for curtailment or redispatch decisions. Therefore, we recommend the deletion of the subarticle.

Finally, **Article 11.4 of draft recast Regulation** enshrines in European legislation the continuation of priority dispatch for RES generation units commissioned prior to the entry into force of the new Regulation. We believe the obligatory grandfathering of nationally created rights through EU legislation is unnecessarily generous and may not be entirely consistent with the current State Aid Guidelines for energy and environment. The indefinite continuation of a right to priority dispatch mandated by EU law, barring a need for renegotiation of the relevant units’ connection agreement, also jars with the clear cessation of immunity from balance responsibility provided for in Article 4 of the draft recast Regulation. We urge reconsideration of the terms of this sub-article.

VII. GOVERNANCE OF THE INTERNAL ELECTRICITY MARKET

1. Roles and responsibilities of ACER

At large, we have a positive impression of the institutional reform that has been proposed in the new legislative package. We see as a positive step forward the adaptation of the powers of ACER as laid out in the **draft recast ACER Regulation**, especially as far as the drafting, review proposals and implementation of network codes/binding guidelines and related methodologies is concerned – **Articles 4 and 5**. Our position on the role of ACER on those articles is notwithstanding our opposition to the adoption of network codes and guidelines by the European Commission as delegated acts (see point VII.3 below).

We also insist on the need for the European Commission to review the budget and staffing of the Agency to ensure it is able to appropriately discharge its tasks.

2. Functioning and governance of ENTSO-E and the future European DSO representative organisation

We highly support the initiative of founding a Drafting Committee at ENTSO-E that will include market participants in the drafting of the network codes and binding guidelines, as foreseen in **Article 55.9 of the draft recast Electricity Regulation**.

Considering the growing role that DSOs are expected to gain in the coming years, we also welcome the creation of a DSO entity as laid out in **Article 50 of the draft recast Electricity Regulation** in order to ensure that a better coordination and facilitate the dialogue with stakeholders and regulators. We nonetheless warn the European Commission, which will be in charge of overseeing the entity, against some of the governance issues we have already faced with ENTSO-E: in our view the structure of ENTSO-E and its decision-making process prevented the organisation to fully discharge its regulated mandate in a satisfactory manner on the one hand, and muddled the line between that mandate and the defence of individual TSO interests on the other hand. While its rules should ensure a proportional geographical representation of DSOs, the future DSO entity should be governed in such a way that the organisation does not represent the interest of individual DSOs to avoid decisions based on the smallest common denominator, as we have sometimes experienced with ENTSO-E in the past. Instead, there should be clear statutory duties related to the energy policy objectives of the European Union.

The tasks of the EU DSO entity should be as clear as possible. It should not be responsible for market design. In that respect, the word “integration” (in **Article 51.1.b of the draft recast Regulation**) is too broad and imprecise. DSOs are not responsible for the integration of (renewable) generation in the market. It would be better to rephrase this into “providing access to the grid”. DSOs are also not responsible for the development of demand side response. Therefore Article 51.1.c of the draft recast Regulation should be removed.

3. Adoption of network codes and guidelines

We are worried by the proposed change in the procedure for adopting network codes – from adoption by implementing acts towards use of delegated acts, according to **Article 66 of the draft recast Directive and Article 54 of the draft recast Regulation**. Covering quite a number of politically sensitive areas by delegated acts may be problematic, as the procedure of adopting delegated acts can never ensure the same transparency and Member States' involvement in the legislative process as the ordinary legislative procedure. Therefore we believe that these areas shall be tackled either directly in the text of the regulation / directive, or that network codes shall be adopted as implementing acts.

Further, we challenge the intention to dedicate specific network codes or guidelines to some of the subject matter laid out in **Article 55.1 of the draft recast Regulation**. Indeed, sub-paragraph (n) foresees the adoption of a network code or guideline on demand-response, including aggregation, energy storage, and demand curtailment rules. As highlighted in Section III of this paper, we believe that guaranteeing a level-playing field between all market participants is essential to ensure that consumers have a real choice of how they wish to organise their supply and storage of electricity, and the commercialisation of their demand response potential. As a consequence, the same rules for the organisation of the market should apply to all market participants, be they generators, demand-response providers (including aggregators) and storage operators. Should the current network codes or guidelines be considered discriminatory vis-à-vis certain categories of market participants in terms of market architecture, then they should be reviewed. But creating a separate set of rules for these categories of market participants is bound to distort the level-playing field in the market.

4. Regional Operational Centres

Since the early days of market liberalisation, EFET has been a strong advocate of improved cooperation between the European TSOs. We have observed the development of regional coordination centres such as Coreso, TSC and SCC in the past decade and appreciate the commendable efforts of TSOs to improve regional coordination in system operation. However, we still observe uncoordinated TSO actions (such as unilateral curtailment of cross-border transmission capacities), significant differences in the definition of margins or the use of remedial actions, inconsistent transparency on network management. These uncoordinated TSO actions lead to inefficiencies in system operation at a regional level, loss of time, and ultimately alters the efficiency of the market.

EFET believes that TSO cooperation goes beyond mere coordination: uncoordinated TSO actions and inefficiencies may only be overcome by strict enforcement of relevant EU rules.

Therefore, EFET generally supports the establishment of regional operational centres (ROCs) as laid out in **Articles 32 to 44 of the draft recast Electricity Regulation**. It could help accompany the strict implementation of EU rules and provide market participants with a clearer understanding of system operation thanks to harmonised operational standards. However, we remain convinced that harmonised standards at EU level are the way forward. As a consequence, we understand the regionalisation of operation standards through ROCs as a first step. ROCs could also improve the understanding of TSOs of grid management throughout a region, just like TSOs have built up their understanding of grid management by the DSOs comprised in their control area.

In any case, we believe that ROCs can only bring added value to the internal energy market if they are independently funded, staffed and governed. Other coordination efforts such as the establishment of the Joint Allocation Office (JAO) have not been a success so far, with an implementation phase that has created chaos on the market at a number of occasions, and significant losses to certain market participants. We would therefore welcome amendments and clarification in the Electricity Regulation in that regard.

Finally, ROCs should only be entrusted with functions for which they can be effectively liable. The establishment of ROCs would require clear chains of liability and responsibility, notably for the oversight performed by regulators: progress on TSO cooperation should not be held up by a lack of cooperation at regulatory level that prevents the adoption of the necessary decisions for the functioning of the ROCs. **Articles 38, 40 and 43 of the draft recast Regulation** should be reviewed in that regard.

VIII. CAPACITY MECHANISMS

We welcome the intention of the European Commission to establish rules in European legislation on capacity mechanisms. We support the provisions of **Article 18 and 19 of the draft recast Regulation** mandating Member States to perform a coordinated resource adequacy assessment at European level that should be the basis of any possible establishment of a capacity mechanism according to **Article 23.5 of the draft recast Regulation**. We also support **Article 23.3 of the draft recast Regulation**, which foresees that capacity mechanisms shall not create unnecessary market distortions and not limit cross-border trade and that the amount of capacity committed in the mechanism shall not go beyond what is necessary to address the capacity adequacy concern.

However, we believe that the **final report of the sector inquiry on capacity mechanisms** and the draft recast Electricity Regulation are quite a disappointment in terms of how capacity mechanism should or should not be designed, where they are deemed needed. We see no significant addition compared to the earlier publications of the European Commission on the subject since 2012. We were notably expecting a real “blue print” guidance for Member States in **Article 23 of the draft recast Regulation** to avoid the patchwork situation we are in at the moment with capacity

mechanisms. This “blue print” guidance should include at least the following elements: all capacity mechanisms shall be open to cross-border participation; all capacities – all types of generation, demand or storage, existing or new – should be treated equally; mechanisms shall be designed to phase-out in case they are no longer necessary; the regulation should clearly state a deadline for compliance of existing mechanisms with the new rules.

A major novelty, and the only binding design criterion for capacity mechanisms that the European Commission has seen fit to include in the Clean Energy Package is a on greenhouse gas (GHG) emission standard in **Article 23.4 of the draft recast Regulation**. EFET rejects this concept as it contradicts the core principles of non-discrimination, effective competition and the efficient functioning of the market. A capacity mechanism needs to ensure security of supply – it is not a tool for promoting decarbonisation. The most efficient way to bring about decarbonisation is to internalise the externality of carbon emissions by putting a price on carbon. This is what the EU ETS seeks to do. Picking winners and losers through emissions limits is likely to introduce inefficient market distortions. To exclude specific technologies in this way may result in these technologies exiting the market and hence creating a requirement for costly new investment in (other) conventional power plants. Hence this measure is likely to bring no additional benefit in terms of emissions reductions while imposing higher costs on consumers. The measure will have the detrimental effect of weakening the carbon price in the EU ETS, which in itself undermines GHG reduction targets in the long-term. It will not reduce GHG emissions in the traded sector, since these are set by the EU ETS cap.

Somehow worrisome in the whole discussion on capacity adequacy is the lack of importance given to the relation between scarcity pricing and competition. Energy prices should be allowed to reflect the true value of scarcity during times of system stress and high demand for power; similarly, when energy is in abundance prices should be allowed to reflect the value of displacing that generation and even go negative. To this end we believe there should be no price caps or floors imposed on the market unless they are set at the value of lost load, as foreseen in **Article 9.1 of the draft recast Regulation**, without exception⁴. Making the market more efficient will result in a more efficient use of capacities and therefore translate into lower prices overall, which better reflect the match between supply and demand. We reiterate that assessments of capacity adequacy – to be performed at pan-European, or at least regional level – will remain inaccurate if the market framework in a specific country or region does not allow the free formation of prices.

⁴ For details on the subject, please refer to our statement on the danger of technical price limits suppressing price signals in the day-ahead, intraday and balancing markets, dated March 2017, available at: http://www.efet.org/Cms_Data/Contents/EFET/Folders/Documents/EnergyMarkets/ElectPosPapers/~contents/MS_HJKDBFL6NB6LRX/EFET-statement_price-limits_23032017.pdf. See also our Discussion Paper on the importance of the free formation of prices in the European wholesale electricity market, dated June 2016, available at: http://www.efet.org/Cms_Data/Contents/EFET/Folders/Documents/EnergyMarkets/ElectPosPapers/~contents/GGH299HP5MPZQ5T5/EFET_Free-formation-of-prices-power-market.pdf.