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## Nordenergi's position on the upcoming electricity market design reform

A severe imbalance between the supply and demand for power has led to soaring and volatile electricity prices, predominantly driven by high gas prices caused by Russia's energy war. Together with low availability of nuclear, drought and low levels of precipitation, this has put the wholesale electricity market under pressure not experienced before. The situation has led to periods with power prices that are not affordable for many customers, and households, businesses and industries all over Europe are suffering.

Nordenergi, the joint collaboration between the Nordic energy organizations, strongly emphasizes the importance of separating the current supply crisis from the long-term challenge of facilitating the investments necessary to achieve ambitious climate targets. The Nordic electricity market works very well and is characterized by numerous retail companies offering a variety of different products to benefit the customer with a lot of choices. Nordenergi notes with concern the recent non-papers on electricity market design which suggest more centralized solutions and disregard the market's role as an enabler for efficient use of our resources. Although the current market model can be improved, the introduction of far-reaching governmental participation can at worst damage a market which, according to ACER, delivers benefits of 34 billion Euros per year.

Nordenergi recognizes the economic hardship electricity customers suffers due to high energy prices, but we believe it is vital to make a distinction between price and cost. Rather than destroying the price signal, which safeguards a cost-minimizing use of resources, measures should be directed towards the customers to lessen their burden. As circumstances vary between Member States, such measures should to a large degree be subject to national adaptation. However, measures that might influence cross-border competition should to a larger degree be harmonized.

Nordenergi welcomes the Commission's work and efforts to manage the current energy crisis. The Nordic associations will respond to the Commission's consultation on a revised market design but would in addition like to convey our key messages and concerns in this position paper.

### 1. The long-term market design should not be designed to solve a short-term extraordinary crisis

It is important to distinguish between problems to be solved in the short and long term respectively. We see it as essential to clearly separate the response to the short-term gas crisis from the longer-term solutions needed to develop the electricity market to enable sufficient investments and an efficient operation of a power system fit for net zero. The extremely volatile and soaring electricity prices reflect a severe imbalance between supply and demand for electricity, caused by Russia's disruption of gas supplies in combination with other unfortunate circumstances mentioned above. The crisis requires us to move, but the short-term gas crisis is a matter of urgency that should be addressed by short-term measures that are proportionate, reversible and designed to solve the problem in question. New market arrangements will not solve the structural imbalance in the short run.

Future-proofing the electricity market to enable secure and efficient operation of a power system with more intermittent power production and enable investments in stable production requires thorough assessment, and a clear description of the problems to be solved as well as the potential shortcomings of the current market design. A future-proof electricity market design should enable electrification and green transition, while also ensuring security of supply and competitive prices through sufficient investment signals for new fossil-free electricity generation and system need. Long term changes should be assessed against these overall goals.

Against this backdrop, Nordenergi is concerned about the pace of the work with the reform for long-term market design. A hasty process can result in a regulatory framework with unforeseen and harmful consequences.

## **2. The short-term solution is to alleviate the burden on costumers**

The current volatile and high price level is unsustainable for many households, enterprises and industry. In the short term, compensation to customers in need is the only possible relief. As circumstances vary between Member States, the implementation and financing of such measures must be a national prerogative.

Support schemes to relief customers should as far as possible be designed not to lead to increasing electricity consumption and preserve the incentives for consumers to reduce their demand in periods of high prices. We therefore support that such support schemes have been accompanied by schemes to reduce consumption.

Of great importance is that all possible measures are implemented in a way that does not distort neither the internal market, cross-border trade nor investment incentives.

## **3. The long-term solution is to restore the balance between power supply and demand**

The long-term solution is to restore the balance between supply and demand. Nordenergi highly welcomes EU's efforts to reduce electricity demand, enable efficient use of energy and accelerate and incentivize the deployment of fossil free energy. In this, the short-term market has had a crucial role in delivering scarcity prices which are indispensable to provide correct incentives for flexibility and energy savings.

## **4. The short-term markets have worked well during the crisis and will be increasingly important with more renewables**

Electricity is a unique commodity since it cannot be stored, hence supply and demand must be balanced at all times, without exceeding power grid capacity. The current market design, which has evolved through continuous improvements since its introduction in the Nordics in the early 90s, is an excellent planning tool and enables us to balance the power system in a cost-efficient way.

The short-term market has worked just as expected through the current crisis: through higher prices, they have conveyed the message that energy is scarce. As also highlighted by ACER, the market rules in place have helped mitigate the current crisis, thus avoiding electricity curtailment or even blackouts in certain quarters.<sup>1</sup>

While a persistently high level of power prices might not be politically and socially acceptable, allowing for short term price variation is important to enable the development and operation of a power system fit for net zero. With increasing share of renewables, the role of flexible production and flexible demand will be more important. Efficient short-term price signals are key to enable this segment to develop efficiently, and to trigger the necessary responsiveness in periods of low production of renewables.

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<sup>1</sup> ACERs Final Assessment of the EU Wholesale Electricity Market Design, April 2022 ([link](#))

Nordenergi appreciates the Commission's recognition of the role of these markets and their increasing importance with rising shares of intermittent renewable generation. We welcome initiatives to enable flexibility solutions such as demand response and energy storage to participate in these markets, as these will be key solutions in our future power system.

#### **5. Access to voluntary long-term hedging opportunities must be improved for all market actors, but bilateral contract should not be favoured at the expense of transparent, financial marketplaces**

The forward market offers a transparent and organized marketplace with a wide range of hedging instruments. Since the financial crisis in 2009, there has been a gradual reduction in the liquidity in the Nordic financial market, further exacerbated by the introduction of EMIR and MIFID II.

A transparent and liquid market for long-term hedging is important for investment signals for electricity production, but also a prerequisite for an efficient and competitive retail market. It must be recognized that the financial forward market on regulated marketplaces is in competition with the bilateral market, and that favouring the bilateral market will drain liquidity from transparent and organized marketplaces even more. It should also be recognized that liquid marketplaces for financial hedging is necessary for market participants to correctly price PPA-agreements. Further exploration into the possible improvements of PPA-agreements is welcomed.

Bilateral agreements can play an important role both to enable producers and customers to share risk, and regulatory barriers for such contracts should be removed. At the same time, these contracts should not be favoured compared to other instruments in the financial market. On the contrary, measures to increase the liquidity in this market should be considered (for example market making, integration of forward markets, collateral requirements). Hence, the regulatory burden for companies who are active on regulated marketplaces should be reduced through revision of the relevant financial legislation (EMIR, MIFID II).

Nordenergi welcomes the ACER/CEER report on possible ways to develop the forward market and encourages EU policy makers to explore these options further.

#### **6. The potential trade-off between a large extent of long-term contracts and liquidity in the short term markets should be investigated**

The Commission has pointed to long-term contracts using different remuneration structures as one possible way to give consumers better access to lower cost renewables with less volatile prices. Power Purchase Agreements (PPAs), Contracts for Difference (CfDs) and strengthening the liquidity of forward markets more generally are mentioned as possible solutions.

The Commission's non-paper emphasizes the importance of the short-term markets in balancing the system, but it lacks a description of how the short-term markets actually will work with a large extent of long-term contracts. How a large extent of long-term contracts could influence bidding behaviour and the short-term markets should be carefully investigated. In general, contracts with a fixed price and no volume restrictions risk deteriorating the role of short-term price signals.

PPAs and CfDs should be designed in a way that preserves the markets' participants incentives to participate in the short-term market.

## 7. Market-based solutions prior to centralized solutions and public intervention

Nordenergi recognizes the role of the European Union and the national states with regards to providing energy security for citizens. For example, the current gas crisis shows that geopolitical risks needs to be taken into account when planning the energy system.

The current market is founded on voluntary agreements between market participants. It is the result of more than twenty years of improved regulations, which have worked well in securing a high degree of competition, cost-efficient solutions and affordable energy prices. Nordenergi advice against a development where the state is given a role in the power market at the expense of commercial relationships. Commercial relationship and competition are key to maintaining cost-efficient solutions and innovation for a capital-intensive, uncertain future.

When possible, investments should take place on markets conditions. Government-backed CfDs should be reserved to realize investments that need public support for its realization, and the design must be carefully considered. A key role for governments should be to provide possibilities for commercial agents to develop projects, by providing sites, speed up development for grid and speed up the different approval processes.

## 8. Consumers should be offered a wide range of retail offers and engagement opportunities

The Clean Energy Package aimed at putting consumers at the heart of the energy transition by enabling them to participate more actively in the market by smart meters, price comparison tools, dynamic price contracts and citizens' energy communities. At the same time, a strong framework for consumer protection was put in place to ensure that energypoor and vulnerable consumers would have better protection. Nordenergi welcomes the full and effective implementation of the package.

The current crisis has led to a political demand for low and stable prices for consumers, and the price volatility in the power system is perceived as a problem. For most customers, electricity is a necessity good, and affordable and sustainable prices is a sound overall goal. There is however a trade-off between stable prices, and short-term price variation that can trigger demand reductions and flexibility. The incentives for consumers to react on short term price signals will be increasingly important in a system with more intermittent power production and where changes in demand will be important to balance the system.

Retail contracts should reflect the great diversity of consumers' needs, and consumers should get information, options and freedom to choose. Consumers should be able to choose a contract which protects them from price variation. At the same time, consumers should also be able to choose exposure to price variation and short-term price signals. Retail companies should compete when it comes to guidance and developing tools on how consumers can use electricity efficiently, and the legislation should not restrict their business models.

In the Nordics almost all consumers have hourly meters and thus have the opportunity to monitor and react to hourly price volatility. This has resulted in clear examples of how high prices and raised awareness have triggered demand reductions among consumers. This awareness is important and can be beneficial on our way to net zero.

Nordenergi would also like to remind that the current market design is compatible with a well-developed retail market as seen in the Nordics, characterized by a multitude of suppliers and great variety of contracts, including long-term fixed price contracts, for the customers to choose from. Many of the retailers also sell flexibility enablers (for instance smart EV charging) and customers also choose hourly priced contracts to an increasing degree.

*Nordenergi is the joint collaboration between the Nordic associations for electricity producers, suppliers and distributors. Members are Swedenergy, Green Power Denmark, Renewable Norway, Finnish Energy and Samorka. Overall, Nordenergi represents more than 2,000 market actors (member companies), most of them active in the electricity sector, but also in other areas such as district heating, gas and services. For more information regarding Nordenergi please visit [www.nordenergi.eu](http://www.nordenergi.eu)*