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Nordenergi position on short term interventions in the power market

Russia's effort to weaponize energy has led to soaring gas and electricity prices in Europe. Together with a series of other unfortunate and coinciding events, such as low availability of nuclear, heat and drought, the wholesale electricity markets are under pressure not experienced before. Several suggestions to make the price of electricity more independent from the price of gas have been proposed, with the overall aim to ease the burden of high energy prices on consumers.

The current situation calls for action and strong European cooperation is more important than ever. Nordenergi welcomes a rapid and coordinated EU-wide response to the emergency situation, and we welcome the work done to address the issues by the Commission and Council in the run up to the extraordinary Council meeting 9 September.

We would like to emphasize that the current market design is not the root of the soaring energy prices. The same market mechanism generated record low electricity prices in 2020. Our market-based solutions have served us well for decades, and it ensures that the demand for electricity is covered at the lowest possible cost to society. The electricity prices work as information carriers, and the soaring level is an expression of the underlying resource situation, extraordinary circumstances, and fear of even more severe disruption in Russian gas supplies. We encourage policy-makers to keep this in mind when assessing the various measures. It is crucial that short-term measures do not lead to an increase in gas or electricity demand and as a consequence worsens security of supply. We strongly advise against measures that could have this effect, such as a cap on the price of electricity or gas and proposals to decouple the gas and electricity price in the wholesale markets, as also pointed out by the Commission in its non-paper on emergency electricity market interventions. On the contrary, the economic incentives to reduce the demand for gas and electricity should be maintained.

Furthermore, the fight against climate change must be fought in parallel, and both short and long term measures must maintain incentives for the green transition.

This being said, we understand and agree that current situation requires extraordinary measures. We would therefore like to highlight some key messages to EU policy makers on their way forward:

- Comprehensive efforts to reduce the demand for electricity are needed
- Support for customers should be strengthened through support systems adapted to national circumstances
- Safeguard that current electricity production is not reduced and if possible, make necessary changes to increase climate-friendly power production.
- The liquidity situation must be addressed immediately
- We strongly advise against interfering with EU ETS
- Measures should be implemented in a timely and smooth manner
- Emergency measures should be temporary, and we welcome a thorough process with broad stakeholder involvement on the long term review of market design

Comprehensive efforts to reduce the demand for electricity are needed

Nordenergi agrees that it is important to introduce measures to lower electricity consumption. A reduction in the demand for electricity could have positive effects on security of supply as well as a dampening effect on power prices under the right circumstances. A further strengthening of the call for energy savings at an EU level could be an option. We believe that such savings schemes should be subject to national considerations, as to finding the best solutions. Strengthening financing schemes for better insulation, heat pumps, district heating and other measures which would lower demand for electricity would be welcomed. We also support measures to increase the public awareness of electricity saving. A union wide campaign stressing the need for energy savings would be very welcome.

We are also positive to the idea of introducing tenders for demand reduction, and we already have experience with this measure in the Nordic countries in severe situations. This could be a step away from equal competition, given that some industrial customers are not aware of how their demand response could be of use to the electricity market.

Support for customers should be strengthened

The soaring energy prices have severe effect on households and businesses, and support to vulnerable customers should be strengthened. Support schemes for consumers exist in a number of EU countries, and this is vital to limit energy poverty as much as possible.

There are several ways to support consumers, and when assessing them it is necessary to recognize that the high energy prices reflect scarcity and uncertainty in the market. Support schemes should not have the indirect effect of increasing electricity consumption. On the opposite, it would be welcome with support schemes that give consumers incentives to reduce their demand. In our view, a direct income support is an example of the latter. As a consequence, we consider this a better option than regulated tariffs and reductions related to the electricity bill. We believe that such schemes must be national and non-binding, and that there would be different approaches that are suitable for different countries.

We understand the will for redistribution of unintended profits, but financing of emergency measures should be a national decision

In the current situation, there is a big gap between the marginal cost for inframarginal production technologies and the whole sale market price, since gas is the marginal price setting technology. Due to this and the need for public revenues to finance support to customers, the Commission has proposed to redistribute some of the unintended profits generated by these producers through a cap on their income.

Nordenergi supports emergency measures targeting final customers and understands that to redistributing some of the extraordinary income generated in the current situation, may seem appealing to decision makers and it might even work under some specific circumstances. We however see several shortcomings with the proposal put forward by the Commission, such as it could actually decrease supply of production and that it presupposes extraordinary unintended profits regardless of the degree of hedging in MS.

Given the varying national circumstances, financing of these compensating measures should allow for national solutions. For example, the Swedish transmission system operator has amassed a large sum of

congestion rents. The existing EU legislation specifies in some detail how that could be used as for example re-payment to the customers. Consequently, we propose that leniency regarding the use of these congestion rents could be an equally permissible source of financing, alongside of VAT and other sources of income that follow the increases of electricity price. The Commission proposal also seem to boarder to EU-taxation, and Nordenergi questions the EUFT compatibility of introducing EU-wide taxing through the back door.

As stated above, proposal to introduction a tax on part of the power production has several shortcomings. Just to mention some is that it will not lead to a lower price per definition. A tax reduces the incentive to increase production and could in fact lead to less production and not the least available flexibility. The introduction of a tax on trade via the DA-market will lead to less liquidity as it will lead to more bilateral trading, and it is difficult to foresee the consequences for the intra-day- and balancing market respectively and could have repercussions on system operation and security of supply.

The proposed tax will strike at the power production we want to be profitable, i.e. non-fossil power production, and will be unfair to countries with large shares of non-fossil power production. The proposal also not take into account geographical differences like countries with large shares of hydro power or Member States with national bidding zones.

Furthermore, we would like to highlight that most generators are hedged for multiple years, and most market-based renewable projects have signed power purchasing agreements (PPAs) running even longer. This means that some of the extraordinary profits that are being generated is already distributed in society. The leaked documents lack does not describe the relationship between an income cap and such hedging. If an income cap is chosen, this is something that must be thoroughly addressed and an income cap needs to be carefully designed in order to not affect existing hedging contracts, PPAs and CfDs which were entered before the crisis.

The liquidity situation must be addressed immediately

High and volatile electricity prices on energy exchanges create pressure on the collateral and margin requirements and thus effects on the cash liquidity of energy market participants. The current situation is leading to situation where market participants are closing their positions on exchanges and moving to OTC-markets, which will decrease transparency of the markets and hinder the functioning of EU energy markets. In addition, last spring's communication 'Short-Term Energy Market Interventions and Long-Term Improvements to the Electricity Market Design' from DG ENER recognizes the need for liquidity support.

Recent measures of loan and guarantee schemes of the Finnish and Swedish governments calm and secure functioning of the market in extreme situations. However, accepting CCP's to receive non-fully backed bank guarantees would cover partially the margin requirements and relieve pressure on cash liquidity challenges. To accept fully backed bank guarantees would require amendments to EMIR and actions to change the legislation should begin immediately.

We strongly advise against interfering with EU ETS

We strongly advise against interfering with the EU ETS market. Currently, the effect of EU-ETS on electricity prices are relatively marginal and any interference in the market might bring more harm than good in the long run.

Measures should be implemented in a timely and smooth manner

Recommendations and guidance on the EU level is necessary, but in order to ensure a timely and smooth implementation we believe that members states should have the possibility to introduce national measures, taking national circumstances into account.

Emergency measures should be temporary, and we welcome a thorough process with broad stakeholder involvement on the long term review of market design

In our view the measures introduced to address the immediate emergency should be temporary with a clear end date.

In the communication of May 18, the Commission proposed to launch the process for an impact assessment on the long term electricity market reform. We recognise this ongoing work and agree that the impact assessment of any potential reforms to the functioning of the internal market should be thoroughly conducted. Any structural changes will need thorough analysis and broad stakeholder involvement. We look forward to cooperating with the Commission on the long-term impact assessment of energy markets.

Nordenergi is the joint collaboration between the Nordic associations for electricity producers, suppliers and distributors. Members are Swedenergy, Green Power Denmark, Energy Norway, Finnish Energy and Samorka. Overall, Nordenergi represents more than 1000 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

