



– Position paper –

Council Regulation on an emergency intervention to address high energy prices

Brussels, 27 September 2022 | In its proposal for a Council Regulation on an emergency intervention to address high energy prices, the European Commission suggests measures relating to demand reduction and a cap on market revenues and distribution of surplus revenues to final customers. Europex fully acknowledges the need to build on previous steps taken at European level to alleviate the burden of high energy prices on consumers and businesses. We would therefore like to take this opportunity to offer additional guidance to ensure that these emergency measures are not adopted without due consideration of their short- and mid-term effects. In particular, we highlight below several key aspects to consider regarding the identification of peak hours and the proposed cap on market revenues from inframarginal technologies.

In addition to these critical considerations, we also include specific amendments to the text in Annex 1 of this document.

Electricity demand reduction

Europex supports the reduction of electricity demand as set out in Articles 3-5 of the draft Council Regulation. Given that the current energy crisis is first and foremost an energy *supply crisis*, demand reduction measures are most effective to mitigate high prices in the short-term and to cope with potential energy shortage concerns in the coming heating season and beyond.

Regarding the reduction of gross electricity consumption during peak hours, **Europex recommends that peak hours are to be identified for the entirety of the period of application of the emergency Council Regulation, instead of on a monthly basis.** This will ensure that relevant characteristics and specific events are accounted for in the demand reduction, such as the winter period, school holidays, as well as country-specific consumption and production patterns, etc.

Cap on market revenues for the generation of electricity from inframarginal technologies

While it is understandable that unexpected short-term financial gains are considered to partly alleviate the costs of high energy prices for consumers, the proposal to cap market revenues for the generation of electricity from inframarginal technologies constitutes a complex undertaking. The measure requires adequate implementation both from a legal and technical

point of view to avoid market distortion and a negative effect on price formation, including the supply and demand equilibrium in spot markets and knock-on effects in forward markets where spot prices are used for trading and settlement purposes. If politically agreed, it is therefore essential that the following nine points are fully taken into consideration:

1. Temporary nature

- It is vital that the cap is implemented in a coordinated manner and on a **temporary emergency basis only, with a clear start and end date.**

2. Harmonisation across Member States

- The current proposal leaves too much discretion to Member States when it comes to the implementation of inframarginal revenue caps. The result could be a patchwork of different cap models across Member States, potentially overlapping with each other and negatively affecting the proper functioning of the EU Internal Energy Market as well as the level playing field between Member States.

3. Coverage for all marketplaces and across all market timeframes

- Importantly, the cap for inframarginal rents must apply homogeneously across all markets and to all timeframes (forward/futures markets, day-ahead, intraday, ancillary services/balancing) to ensure a level playing field and to minimise market distortions.

4. Ex-post application in all Member States

- The current proposal leaves Member States the option to freely decide whether to apply the cap on inframarginal revenues at the exchange's settlement or thereafter. **We strongly urge that the revenue be captured solely ex-post by all Member States, i.e. after the settlement and after the market price has been cleared. Applying the revenue cap at or shortly after the trade execution** would result in a de facto price cap, dangerously affecting the bidding behaviour in the market.

5. Exceptional technology-specific caps

- The suggested threshold of 180 EUR/MWh could lead to a situation where some technologies (e.g., oil, lignite, hard coal) would be unable to recover their marginal costs, posing a serious risk to security of supply. Exemptions for inframarginal production with levelised costs above 180 EUR/MWh shall be made more general and become applicable to any supply source that can show production related costs above the suggested cap, thus not specifically referring to hard coal or other specific fossil fuels.¹

6. Collection of revenues

- The current text does not specify who will collect the revenues. Clear responsibilities and tasks need to be defined. In addition, it should also be made very clear that NEMOs/PXs/derivatives exchanges shall not have a role in the revenue collection since they do not possess the necessary data to do so.

¹ See text proposal on Articles 6.5 and 7.4 in Annex I below.

7. Implementation difficulties related to portfolio-based bidding

- The current proposal does not address how the cap could be applied to portfolio-based bidding and marketing. Clear guidance should be provided for the sake of legal clarity and market integrity.
- In addition, the fact that power is usually sold, purchased and resold several times is not addressed.

8. Operational questions

Many operational questions remain unanswered:

- ***Which authority will operate the cap and who will police the data and correct applicability?***

Clear responsibilities and tasks need to be defined. In addition, it should also be made very clear that NEMOs/PXs/derivatives exchanges shall not have a role in the revenue collection since they do not possess the necessary data to do so.

- ***How will the cap be calculated?***

We note that Article 6 currently includes little detail on how the inframarginal revenue cap should be calculated and applied. Specifically, the current draft is silent on the data which should be used to make the relevant calculations. We recommend that the revenues subject to the cap be calculated based on well-defined criteria founded on hard data (e.g. output, metering, proof of realised revenues through forward/derivatives contracts, PPAs, OTC or sale on the SDAC, SIDC or ancillary services/balancing markets and other relevant support instruments that affect the calculation of the amounts to be clawed back), rather than on broad and imprecise assumptions, to ensure a fair, correct and consistent capture of all relevant inframarginal profits.

- ***Who will extract the revenues?***

The proposal should not only consider producers, but all the sellers along the value-chain.

- ***What is the relationship to existing caps and measures?***

Further clarity should be provided on the overlap between existing caps and the new measures.

- ***How will a level-playing field between different markets be ensured?***

A patchwork of different caps across Member States will create an unlevel playing field and must be avoided.

9. Further market considerations

- It must be noted that the proposed cap on inframarginal revenues could **render several markets less liquid. Market participants will not have incentives to hedge future electricity production, hence drying out forward markets.** In addition, market players could lose incentives to bid in the intraday and balancing markets, given revenues are uniformly capped at a same threshold across all markets.

Based on the above, please see our concrete text amendments below:

ANNEX I

N.	Article	Europex proposal	Considerations
Demand Reduction			
1	Article 4.1	<p>1. Each Member State shall identify peak price hours corresponding in total to a minimum of 10 % of all hours of <u>the period between 1 December 2022 and 31 March 2023</u> month.</p>	<p>The peak hours must be identified for the entirety of the period of application of the emergency Council Regulation, instead of on a monthly basis. This will ensure that relevant characteristics and events are accounted for, such as the winter period, holidays, as well as country-specific consumption and production patterns, etc.</p>
Cap on revenues from inframarginal technologies			
2	Article 6.2	<p>2. Member States shall ensure that the cap targets all the market revenues of producers, regardless of the market timeframe (forward/futures markets, day-ahead, intraday and ancillary services/balancing) in which the transaction takes place and independent of whether the electricity is traded bilaterally or in a centralised marketplace.</p>	<p>All markets and all market timeframes need to be included to ensure a level playing field and avoid undue arbitrage opportunities between markets. We urge Member States to clarify that balancing markets are included as well.</p>
3	Article 6.3	<p>3. Member States shall decide whether to apply the cap on revenues at after the settlement of the exchange of energy or thereafter.</p>	<p>The alternative “at the settlement of the exchange” should be deleted, among others, because of the risk of a severe distortion of the price formation mechanism. The latter may lead to a situation where suppliers with inframarginal production units may not be able to sell at the prevailing market price that might be far above the inframarginal revenue cap at any given point in time. And this would of course have strong negative effects on security of supply and affordability.</p>

4	Article 6.5	<p>5. Subject to the requirements under Article 6(4), Member States may allow the regulatory authority to maintain or set a specific cap on the market revenues obtained from the sale of electricity produced from hard coal for producers who demonstrate to the regulatory authority their current levelised costs of energy exceed the maximum set in Article 6(1). The specific revenue cap shall allow for those costs and a reasonable profit margin to be covered. Such measures shall be designed so as not to affect the merit order and the price formation on the wholesale market.</p>	<p>Exemptions for possible inframarginal production that has levelised costs above the 180 EUR/MWh shall be kept general and become applicable to any supply source that can show production related costs above the general cap, thus not specifically referring to hard coal or other fossil fuel-specific production.</p> <p>We propose to merge Articles 6.5 and 7.4 by deleting 6.5 and amending 7.4 to become general in nature (i.e. not tailored for hard coal). See below</p>
5	Article 7.1	<p>1. The obligation in Article 6 shall apply to the market revenues obtained from the sale of electricity produced from the following sources:</p> <p>(a) wind energy;</p> <p>(b) solar energy (solar thermal and solar photovoltaic);</p> <p>(c) geothermal energy;</p> <p>(d) hydropower without reservoir;</p> <p>(e) biomass fuel (solid or gaseous biomass fuels), excluding bio-methane;</p> <p>(f) waste;</p> <p>(g) nuclear energy;</p> <p>(h) lignite;</p> <p>(i) crude oil and other oil products;.</p> <p>(j) peat;</p> <p><u>(k) hard coal.</u></p>	<p>All relevant fossil inframarginal production sources (e.g. all fossil sources except natural gas) should be listed in Article 7.1 list, thus also hard coal.</p>
6	Article 7a ²	<p>1. Complementary to the mandatory cap on market revenues:</p> <p>(a) Member States may maintain or introduce measures that further limit the market revenues of producers listed in Article 7(1);</p>	<p>We propose to merge Articles 6.5 and 7.4 by deleting 6.5 and amending 7.4 to become general in nature (i.e. not tailored for hard coal).</p>

² This amendment is based on REV2 made available on 22 September while other amendments refer to the original proposal by the European Commission as tabled on 14 September.

		<p>(b) Member States may maintain national measures to limit the market revenues of producers generating electricity from sources not referred to in Article 7(1);</p> <p>(c) Member States shall set a higher revenue cap for producers producing from the sources listed in Article 7(1) provided that they prove that their investments and operating costs of the distinct assets exceed the maximum set in Article 6(1);</p> <p>2. Measures referred to in paragraph 1 shall:</p> <p>(a) be proportionate and non-discriminatory;</p> <p>(b) not jeopardise investment signals;</p> <p>(c) ensure that the investments and operating costs are covered;</p> <p>(d) not distort the functioning of electricity wholesale markets, and in particular, not affect the merit order and the price formation on the wholesale market;</p> <p>(e) be compatible with Union law.</p>	<p>In addition, we are convinced that in order to achieve the goals in accordance with Article 7a.2, any higher cap needs to be based and shall be only granted for distinct assets. Granting a cap for an entire technology class would yield discriminatory results and would have an impact on the merit order curve as it would incentivise more efficient assets to bid at higher prices. An average cap would also still force less efficient assets out of the market, which would result in a reduction of supply.</p> <p>Moreover, we highly advocate to render the higher caps for these assets mandatory to ensure that single national measures do not result in a shortage of supply and a further distortion of the wholesale market.</p>
7	Article 7.5	<p>5. Producers and relevant market participants (excluding NEMOs/PXs/Derivatives Exchanges) shall provide to Members States all necessary data for the application of Article 6, including on the electricity produced and the related market revenues, regardless of the market timeframe in which the transaction takes place (forward/futures markets, day-ahead, intraday, ancillary services/balancing) and of whether the electricity is traded bilaterally, within the same undertaking or in a centralised marketplace.</p>	<p>All markets and all market timeframes need to be included to establish a level playing field and avoid undue arbitrage opportunities between markets. We urge to clarify that balancing markets are included as well.</p> <p>It should be made clear that NEMOs/PXs/Derivatives Exchanges shall have not role in the data provision task, since they do not possess the necessary data.</p>

Review			
	Article 19.1	<p>1. By 28 February 2023, the Commission shall carry out a review of Chapter II in view of the general situation of electricity supply and electricity prices in the Union and present a report on the main findings of that review to the Council. Based on that report, the Commission may in particular propose, in case this is justified by the economic circumstances or the functioning of the electricity market in the Union and individual Member States, to prolong the period of application of this Regulation, to amend the level of the revenue cap in Article 6 (1) and its application to the sources of electricity generation referred to in Article 7(1) to which it applies producers in Article 7, or otherwise amend Chapter II.</p>	<p>It must be ensured that the production sources subject to the revenue cap shall not be amendable in case there would still be a prolongation of the measures beyond 31 March 2023.</p>

About

Europex is a not-for-profit association of European energy exchanges with 30 members. It represents the interests of exchange-based wholesale electricity, gas and environmental markets, focuses on developments of the European regulatory framework for wholesale energy trading and provides a discussion platform at European level.

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