



The European electricity market: fit for purpose?



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Introduction

The climate crisis and Russia's war in Ukraine together act like a perfect storm for Europe's turbulent energy market. In quick response to last year's dramatic rises in prices, the European Commission earlier this month unveiled a set of proposed reforms to the EU's electricity market that it hopes will be a robust response to both challenges.

The main aims of the proposed reforms are to protect private and corporate consumers from volatile fossil fuel prices, to accelerate the transition to renewable energy, and ultimately, to phase out natural gas, which is a major factor that determines electricity prices.

The Friends of Europe policy insight debate on Monday 27 March brought respected voices from academia, the energy industry and the European Commission together to discuss the proposal. Speakers included Professor **Leonardo Meeus**, Director of the Florence School of Regulation at the European University Institute (EUI); **Marion Labatut**, Deputy Director of European Affairs at Électricité de France (EdF); and **Annamaria Marchi**, Deputy Head of Unit for the Internal Energy Market at the European Commission Directorate-General for Energy (DG ENER).

A common response to the Commission's electricity market reform plans was a sense of relief that the proposals do not amount to widescale overhaul, which many had expected. Meeus remarked: "I am as happy by what is not in there as by what is in it."

Is a break-up of the existing short-term gas and electricity market necessary or desirable?

Ahead of the publication of the Commission's proposal, Meeus said that one of his chief concerns was that the reforms would include a break-up of the short-term market, separating gas prices from electricity prices to allow for the establishment of a clean power market.

“ There is a widespread desire to boost renewables

Annamaria Marchi, Deputy Head of Unit for the Internal Energy Market at the European Commission Directorate-General for Energy (DG ENER)

Some EU member states, including Greece and Spain, had been calling for such a radical reform. Others such as Germany and the Netherlands are calling for less radical reforms, warning about the risks of destabilising the market.

This proposal for market separation was not included and the panel agreed that there was a rich opportunity to build on the EU's clean energy package to ensure that renewables play a greater role.

Marchi played down the perceived divergence in views among member states, remarking that "the press exaggerates the problem... There is a widespread desire to boost renewables and even the most cautious countries made use of the facility set up last year to regulate prices."

The Commission's proposal stops short of making last year's emergency measures permanent, and it does not propose capping the profits of renewable energy producers.

However, it does allow member states to intervene again if another EU-wide crisis is declared and this worries the energy industry.

Will longer-term contracts help?

Also of concern, particularly to industry, is the Commission's proposal to reduce volatility in electricity prices through longer contracts, such as Power Purchase Agreements (PPAs) between energy suppliers and their corporate customers, and contracts for differences (CfDs) between governments and energy suppliers.

PPAs are commercial contracts between an electricity customer and a generator, whereby the generator agrees to sell energy directly to the customer at a certain price. CfDs are contracts concluded by a public entity to encourage investment. They top-up the market price paid for electricity if the price is below a certain level, but they require the generator to pay back amounts where the market price is above a certain level.

Both types of long-term contracts can help reduce the cost of capital to energy firms looking to invest in raising capacity, and this can pass on savings to consumers, Labatut argued.

Under the proposal, member states will be obliged to ensure the availability of market-based guarantees for PPAs. Meanwhile, all government support for new investments in renewable and non-fossil energy generation will have to be in the form of CfDs.

With homes and businesses increasingly generating electricity, can we have a realistic, green and reliable vision for energy generation that has consumers playing a role?

Moderator and Senior Fellow for Health at Friends of Europe, **Tamsin Rose**, asked the panel about their views on the Commission's aim to develop energy sharing.

“ We have to be careful that this proposal does not create a loophole in the ecosystem of supplying electricity

Tamsin Rose, Moderator and Senior Fellow for Health at Friends of Europe

Energy sharing involves homes and businesses that generate electricity from solar panels feeding unused electricity back to the grid or specific users like neighbours and family members. Labatut said she welcomed the fact that the proposal seeks to go a step further in developing a decentralised production.

However, she warned that “we have to be careful that this proposal does not create a loophole in the ecosystem of supplying electricity. Strong suppliers are a very important element of our energy system,” highlighting that last year some players could not live through the crisis and consumers were left without a supplier due to hedging. Labatut reminded participants that energy sharing has network implications and while it is a good idea to develop this, we must also ensure sure that the grid, and its remuneration, are preserved.

With a new EU administration starting next year, what still needs to be done?

Meeus accepted that there is still a lot left to do. He remarked that “we have been discussing the 2030 targets, and we still need to start to discuss the 2040 targets.” He concluded by acknowledging the need to be more ambitious with respect to investment in all kinds of energy infrastructure. This sentiment was shared by the other members of the panel.

“Some people worry that the proposal we currently have won’t be enough to have the infrastructure we need. Can we be more ambitious to make sure we have enough investment in all kinds of energy infrastructure?” he asked.

“ Can we be more ambitious to make sure we have enough investment in all kinds of energy infrastructure?”

Leonardo Meeus, Director of the Florence School of Regulation at the European University Institute (EUI)

Key recommendations

- The EU needs to ensure that the reforms proposed by the Commission are ambitious enough to attract investment in all kinds of energy infrastructure
- The EU needs to avoid creating a loophole in electricity supply through its energy-sharing aims
- The EU should focus more on PPAs and less on CfDs



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