



Fostering energy markets, empowering **consumers**.

**CEER Response to
European Commission Consultation on
Community Guidelines on Environmental
and Energy State Aid for 2014-2020
(Ref: HT 359)**

**14 February 2014
Register number: 65470797015-89**

1 Introduction

Historically, EU State Aid rules evolved to support countries balance strategic interests with the principles of free and fair competition between Member States. This balance is well illustrated in the energy sector where, for environmental and other (mainly energy mix reasons), European governments have found it necessary to adopt a range of policy measures to drive the necessary transition and structural changes towards a low carbon energy sector.

Given the importance of energy to domestic interests and the wider European Community, it is important that State Aid rules, in the first place prevent abuse, and secondly give clear guidance for the measures required in terms of national support schemes, infrastructure investments, and associated measures by relevant national agencies.

As the representative body for Europe's energy regulators, CEER welcomes the opportunity to comment on the Commission's draft Guidelines on Environmental and Energy State Aid for 2014-2020¹. As a collective of National Regulatory Authorities (NRAs), CEER's competences extend to matters of energy security, market development, cost-effectiveness, regulatory certainty and financing arrangements as these areas directly affect the future development of the Internal Energy Market (IEM).

Commentary and observations are offered on this basis. These guidelines are of particular relevance for energy regulators, as they will be the basis for investigations of existing arrangements and will most likely affect any plans by Governments / NRAs e.g. for new support schemes for generation capacities and renewable energy sources (RES).

2 Structure and high level reaction of the CEER response

The Draft Guidelines on Environmental and Energy Aid for 2014-2020 set out the proposed conditions under which the Commission may consider requests for state aid for energy and environment projects to be compatible with the wider aims of the internal market (according to the relevant articles of the Treaty of the Functioning of the European Union).

CEER understands that the principal aims of the State Aid Modernisation (SAM) programme are to contribute to the achievement of sustainable, smart and inclusive growth in a well-functioning, competitive internal market². The secondary aims are to assist the Commission's *ex ante* scrutiny of those cases with the greatest potential impact on the functioning of the internal market, and to help streamline rulings and accelerate the decision-making process.

¹ http://ec.europa.eu/competition/consultations/2013_state_aid_environment/index_en.html

² [Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions EU State Aid Modernisation \(SAM\) /* COM/2012/0209 final */](#)

Overall, CEER welcomes the introduction of revised Guidelines on environmental and energy aid. Ambitious, decadal guidelines contribute to long-term regulatory and investment planning certainty, and help ensure aid is well-justified and in the interests of consumers.

CEER further appreciates the coherence of the proposed Guidelines with the principles of the Commission's recent Communication: *Delivering the Internal energy market and making the most of public intervention*.³

We support in particular the implicit steer within the Guidelines towards greater integration of RES within the market, and the importance of minimising market distortion in the design of capacity mechanisms.

More detailed commentary / the remainder of the CEER response is structured around the three main elements of the draft Guidelines which are also of most relevance to NRA interests / competences:

1. **Support schemes for RES**
2. **Reduction in funding support for RES**
3. **Capacity Mechanisms**

3 Detailed commentary

3.1 Support schemes for RES

CEER wishes to respond to specific provisions of the draft Guidelines linked to the design of support schemes for RES. These being:

3.1(a) Allowed aid intensity of 45-65% for RES

Further clarification would be helpful in understanding the implications of the provision. For example:

- How should this intensity apply to operational aid for RES installations as it is linked to the size of the enterprise (small, medium, large), and how should it then be linked to the support level determined?
- On what basis were the aid intensities of 45%, 55% and 65% derived?

The Guidance also suggests that aid intensity can be increased for medium-sized (10%) and small enterprises (20%). CEER supports the intention of this provision (adjusting the proportionately higher costs for SMEs in delivering environmental or energy objectives) but

³ Cf. also CEER response to the Public Intervention package, http://www.ceer.eu/portal/page/portal/EER_HOME/EER_PUBLICATIONS/CEER_PAPERS/Cross-Sectoral/Tab/C13-EWG-95-05_Public%20Interventions%20Package%20views_12-Dec-2013.pdf

notes that many RES investments are usually realised through small project companies (e.g. Special Purpose Vehicles) which are subsidiaries of large commercial interests.

3.1(b) Aid schemes authorised for a maximum of 10 years, with the possibility of re-notification

A clarification regarding this provision would be useful as it is unclear whether it affects existing contracts, and / or schemes to cover investment rather than operating costs, e.g. FiTs. It would also be useful for the Guidelines to set out a definition of investment vs operating aid (particularly in the context of RES)⁴, and to clarify what incentives might be necessary to encourage existing plants to switch to the new regime.

This decadal limitation is appropriate on the basis that the market situation for RES will have evolved over such a period. However, for investment security it is crucial to clarify that changes to the system resulting from future changes to state aid (e.g. post-2020) should not affect ongoing contracts (e.g. 'grandfathering' arrangements). An investment decision for a RES installation is based on its full lifetime (generally 20 years). Having to take possible changes into account after 10 years increases the risk for the investor, which in turn increases the costs of the RES installation.

3.1(c) Operating aid schemes should in principle be open to other EEA countries and contracting parties of the energy community

CEER supports the provision that national aid schemes should be open to any investor in RES installations within the EEA. The draft acknowledges that Member States may require that a cooperation mechanism be in place before allowing cross-border support. However, any subsequent cooperation mechanisms between countries should reflect the contribution of consumers to the refinancing of support schemes (at the national level). In addition, although outside of regulatory competences, CEER wishes to highlight that wider benefits (such as biomass plants supporting Member States' agricultural sectors) may not (or only partially) occur if the investment is realised in a different country.

3.1(d) Operating aid for the production of renewable energy and/or combined production of renewable heat

The Guidelines propose that aid is notifiable if the resulting renewable energy capacity exceeds 125MW. This condition raises the question of whether state aid is notifiable in the case of coal-biomass co-firing plants. For example, how should the "resulting renewable energy electricity generation capacity" be calculated for co-firing plant - the full capacity of the plant or the RES share multiplied by the full capacity?

⁴ It would also be useful to clarify whether there can be other forms of compliant aid (e.g. tax reduction) or whether these would constitute operational aid. There is also a mismatch between two sentences of the Guidelines: in one sentence it mentions the share in production and in another share in consumption.

The Commission's proposed aid thresholds (p37) suggest that FiT aid may be granted to RES installations of less than 1MW (apart from wind, where a threshold of 5MW applies). These thresholds may interact with Member State capacity limits, leading to consequential changes to scheme designs (negatively impacting take-up and consumer confidence). Certain Member States have in place (or are considering introducing) higher thresholds (for example 10MW) to encourage the emergence of community-based RES, which again would be affected by this provision.

A clarification regarding what constitutes "projects of first commercial scale" (para 131) would also be useful, particularly in relation to Member States to offering higher rates to help offset "test and demonstration" costs for advanced technologies (e.g. floating turbines).

3.1(e) Differentiation between deployed and less-deployed RES technologies

According to the parameters set by DG COMP (1-3% share of electricity production at EU level⁵) the following RES technologies would be considered as deployed technologies (based on 2011 Eurostat figures): hydro (10.2%), wind (5.5%), biomass & renewable waste (4%) and solar (1.4%). Less-deployed would include geothermal and "tide / wave / ocean".

This definition does not take into account the level of deployment within a specific technology, nor the size (installed capacity) of the RES installation. In the case of wind, for example, there is still a significant difference between the costs for producing electricity from offshore (fixed or floating) and onshore wind turbines, and CEER recommends greater definition (granularity) of technology in the Guidelines.

Applying the guidelines' classification for RES technologies ("deployed" and "less deployed") would have a direct impact on the method for determining the support level. According to the provisions set out in the guidelines, the support level for deployed technologies must be determined through a competitive bidding process.

Whilst CEER generally supports such an approach, it should be noted that the outcome of a bidding process may lead to only the most cost-effective (in terms of production costs) technology and sites being supported without taking into account other system parameters. Any bidding process should also be closely monitored to ensure it leads to the most efficient outcome in all cases.

⁵ It would be useful to understand how the 1-3% range was calculated (e.g. does the range refer to gross or net production?).

CEER supports aid schemes which also consider the positive system balancing benefits of certain RES (e.g. biomass and biogas) which can help mitigate the effects of more intermittent sources (e.g. wind and solar)⁶.

CEER recommends that more research is necessary to assess whether a classification based on EU-wide deployment levels is more (or less) suitable than a more comprehensive assessment of technological maturity. For example, the current level of EU RES deployment could be the result of significant subsidies rather than the commercial maturity of technologies.

On a separate note, CEER also queries the provision relating to the “regular update of production costs of at least each [1 GW] of installed new capacity” – it is not clear whether the 1GW threshold would apply on an EU-scale or nationally?

3.1(f) Mandatory bidding process for determining the support level for deployed technologies

CEER generally supports the provision for well-designed, competitive bidding processes (recognising the suitability of the method in determining efficient prices), but suggests that a mandatory approach may not (in all situations) acknowledge the wider benefits of certain renewable energy sources and also not reflect particular circumstances. Additionally, the design of a bidding process may prove to be complex as it would need to reflect multiple parameters (including number and type of installations, volume of electricity to be generated, time horizons etc.).

Similarly, the provision relating to technological neutrality (whilst theoretically attractive) may require careful application in practice, for the following reasons:

- It does not take into account national RES objectives, i.e. reaching them in time would be only possible by supporting different RES technologies.
- Supporting only the most cost-effective technology might impact on the grid stability, e.g. when wind turbines are concentrated in the areas with good wind conditions, as the electricity would still have to be transported to remote consumption areas.
- The guidelines already foresee exceptions to ensure a certain RES mix, for grid stability issues in certain regions and for biomass.
- Importantly, excluding biomass from the competitive bidding process would mean that it cannot be supported otherwise. The importance of RES electricity produced from biomass lies in its ability to provide the system with a constant base load⁷,

⁶ However, application of aid schemes for biomass and biogas should be assessed carefully against their specific costs and benefits with regard to balancing and the possible (negative) market effects of subsidies.

⁷ Moreover, this provision does not take into account Member State specific conditions that would favour production from biomass and would bring environmental benefits and added value to the overall economy (e.g. biogas from industrial/agricultural waste).

which is important for the national energy mix and should be taken into account in the design of aid schemes.

To this end, the Commission may consider reformulating this provision to allow for alternative methods for determining the support level for deployed technologies.

3.1(g) Feed-in premium or equivalent measures involving the direct marketing of the electricity produced

CEER supports the principle of greater market integration for all RES technologies (deployed and less-deployed), with a preference for FiPs (where these reflect national and economic circumstances) and strong justifications for the continued use of FITs – e.g. to support immature technologies.

However, the provision as described in the guidelines remains unclear, as it does not define what would be an “equivalent measure to feed-in premiums (FiP) involving the direct marketing of electricity produced”. Therefore the guidelines should clearly stipulate that both fixed and variable (floating) premiums paid on top of the market price are within the scope of compatible national support schemes.⁸

3.1(h) Beneficiaries are subject to standard balancing responsibilities where competitive intra-day balancing markets exist.

CEER agrees that it is very important to ensure that RES beneficiaries have the same balancing responsibilities as all market participants when selling their electricity into the market. In order to place RES producers on an equal footing with other producers in the market, it seems appropriate that these responsibilities go beyond standard balancing responsibilities to also cover the imbalance settlement.

Indeed, forecasting errors do lead to deviations between demand and supply and create imbalances in the network, which need to be technically compensated and financially settled. The financial settlement, i.e. the procurement of (positive / negative) reserve electricity, is linked to additional costs for the market participants. These costs for the financial settlement of imbalances should be borne by all market participants, including RES beneficiaries.

To this end, the Commission may consider re-wording the provision “where competitive intra-day balancing markets exist” as this may imply RES balancing responsibilities are conditional.

3.1(i) Bring existing schemes into line with these guidelines within 12 months after their publication

⁸ As it is described in the Commission guidance document for the design of RES support schemes (SWD(2013) 439 final, p. 9): “Best practice for feed in premium schemes: (...) Determine the form of premium – floating (with or without cap) or fixed – as function of desirable exposure of producers to price risk.”

Bringing existing schemes into line with the new guidelines requires time and resources to modify the schemes, and may create investor uncertainty. Some new elements such as bidding processes and legislative reform are very complex issues, which may be challenging to implement within 12 months. From a regulatory scheme / administration perspective, adequate time should be allowed for Member States to bring their existing scheme in line with the new requirements for state aid.

However, application of the new guidelines should respect current support levels for existing RES installations so as to preserve investor certainty and avoid preventable increases to the cost of RES installation. New schemes should also consider ways of integrating existing renewable installations which were previously granted support without market integration.

3.1(j) Aid granted by way of a feed-in-premium or feed-in-tariff (aid for biomass plant after depreciation)

The draft Guidance states that the Commission will consider operating aid for biomass after plant depreciation compatible if a Member State demonstrates that the variable operating costs borne by the beneficiary after plant depreciation are still higher than the market price of the energy concerned and provided further conditions are met. CEER recommends taking into account fixed operating costs (for the more efficient plants), not only variable costs. If market prices are enough to cover variable operating costs (e.g. fuel costs) but not fixed operating costs like staff costs, this may affect operator decisions regarding plant lifetimes.

3.2 Aid in the form of reductions in funding support for electricity from RES

CEER supports the general principle that all national electricity consumers should bear the costs of financing their national RES support scheme (commercial, industrial and domestic).

In order to avoid the situation of companies being placed in a difficult competitive situation, Member States should, according to the guidelines, be allowed to grant partial compensation for additional costs so as to facilitate the overall funding of RES support and avoid carbon leakage. This approach should imply that the criteria for identifying the concerned companies are to be clearly defined and should not be based on technical or contractual aspects of their electricity consumption (e.g. in the case of self-consumption / consumption behind- the-meter).

CEER considers the proposals regarding the aid in the form of reductions in exemptions from environmental taxes and in funding support for electricity from RES a positive step forward in clarifying general provisions at present contained in the Council Directive 2003/96/EC referring to the Community framework for taxation of energy and electricity products.

CEER however notes that the criteria referred to in (176) a) and (184), clearly limits exemptions to sectors exposed to significant carbon leakage due to environmental taxation and/or funding support to RES and calls for a coherent development of the Community framework for taxation of energy product currently under revision.

3.3. Aid for generation adequacy

It is important to note that the existing electricity systems can present different reasons for security of supply challenges, and that Member States and NRAs typically tailor policy considerations to address these particular challenges. Such differences go some way to explaining the reasons why various capacity mechanisms are envisaged or being implemented. From a high level appraisal of these interventions, it can be claimed that not all these measures have been designed to address purely generation adequacy problems, but also challenges linked to system stability and lack of financial investment.

When considering any public intervention, it is essential that the pursued objective is clearly defined to avoid any overlap with other mechanisms in place which may result in suboptimal economic efficiency and undue additional costs to be paid by consumers. In this respect, the implementation of the draft Guidelines will also need to be carefully planned vis-à-vis existing capacity mechanism arrangements already in place in certain Member States, and to ensure that all relevant and related issues are addressed in a coherent way.

CEER supports the approach in the guidelines where the need for capacity mechanisms should be clearly demonstrated⁹ according to a defined set of criteria before being introduced by a Member State.

⁹ The choice of instrument should also be justified by an analysis that provides robust evidence that one capacity support instrument is more adequate than another to address identified adequacy gaps in one Member State or possibly at regional level.

CEER shares the Commission's concern that incompatible or poorly designed capacity measures may **risk distorting electricity trading, generation and investment decisions**. Coordination between neighbouring system operators, NRAs and Member States in defining cross-border rules of such mechanisms would clearly **need to be considered and enhanced to ensure full compatibility** with the objectives pursued by the Internal Energy Market (IEM)¹⁰.

Moreover, CEER is of the opinion that the framework for aid for generation adequacy should reflect key design principles for effective capacity measures, such as: **technological neutrality (including the participation of demand-side response, interconnection and storage on an equivalent basis to generation), cross-border participation where it is physically possible, limited interference with cross-border energy markets, fair allocation of costs to consumers and the potential to phase out capacity measures** after the underlying issue has been solved.

3.4. State Aid and Green 'offer' interactions

In considering possible negative effects / market distortions arising from aid measures, the Commission proposes to consider the 'consumer preference' effect associated with green credentials (e.g. increased sales associated with preference for environmental protection).

CEER would like to highlight to the Commission the possible distortions between (State Aid supported) RES-backed green energy retail 'offers' and the 'consumer preference' effect for green energy. As increased consumer demand for 'green' tariffs is arguably a positive development, further consideration of this provision may be required.

3.5 Proportionality / eligibility of aid

The draft guidance on eligible costs (para 77, p29) suggests that costs not directly linked to the achievement of the environmental or energy objective shall not be eligible for support. CEER suggests this may require further clarification in the case of coal-biomass co-firing, as typically investment costs are partially related to renewable production and some to fossil fuel based production. For example, the installation or refurbishment of the plant furnace serves both biomass and coal firing purposes, raising the prospect that at

¹⁰ Please see on this issue CEER views on the European Commission's Public Interventions Package: Delivering the internal electricity market and making the most of public intervention 12 December 2013, see http://www.ceer.eu/portal/page/portal/EER_HOME/EER_PUBLICATIONS/CEER_PAPERS/Cross-Sectoral/Tab/C13-EWG-95-05_Public%20Interventions%20Package%20views_12-Dec-2013.pdf and ACER Opinion 05-2013 on Capacity Markets 15 February 2013, see http://www.acer.europa.eu/Official_documents/Acts_of_the_Agency/Opinions/Opinions/ACER%20Opinion%2005-2013.pdf

least some costs should be considered eligible (e.g. according to the ratio of renewable sources in total fuel usage).

3.6 Compatibility between State Aid and EU R&D Framework provisions

The Guidance sets out criteria for aid to energy infrastructure if investments are not funded through tariffs (p52-54). CEER notes that certain schemes overseen by energy regulators (e.g. offshore bidding rounds and interconnector regimes) may be affected by this provision and may require further consideration before the Guidelines are finalised.

In addition, many regulators support innovation schemes (to encourage collaborative partnerships between network operators, suppliers, generators, technology providers and / or other parties to support the transition to a low carbon, affordable energy system). There is a possibility these schemes may be perceived as 'aid to infrastructure' and CEER requests that the Commission consider the compatibility of criteria / eligibility between the State Aid Guidelines and various EU Frameworks for Research, Development and Innovation.

3.7 Specific technologies

CEER notes the specific criteria in relation to CHP (p41) and renewable heat (p41). These aid measures have the potential to incentivise and increase deployment of community-scale heat and power schemes, which will in turn have knock-on implications (depending on scale) for networks and ultimately consumers.

3.8 Energy efficiency measures, including cogeneration and district heating and district cooling

In terms of State Aid scheme performance indicators, CEER notes that efficiency improvement is not always accompanied by declining consumption and recommends a measure reflecting gains in consumption per unit (energy intensity).

3.9 Energy infrastructure financing

In reference to aid to energy infrastructure, CEER shares the general view of the Commission that tariffs are the appropriate primary means to fund energy infrastructure.

In line with this reasoning, CEER strongly questions the Commission's position on the need to allow state aid measures for Projects of Common Interests (PCIs)¹¹. Arguably, there is sufficient financial support set out in the provisions of EU Regulation 347/2013, particularly through the means of cost allocation of PCIs (Art. 12), incentives (Art.13) for projects with higher risks as well as eligibility of PCIs for union financial assistance (Art.14).

Additionally, whilst understanding that partial exemptions from IEM regulatory framework might require case-by case assessment by the Commission, CEER would appreciate if the Commission could better justify why a case-by-case assessment is also needed in the case of gas storage (para 193).

¹¹ EU Regulation 347/2013

About CEER

The Council of European Energy Regulators (CEER) is the voice of Europe's national regulators of electricity and gas at EU and international level. Through CEER, a not-for-profit association, the national regulators cooperate and exchange best practice.

A key objective of CEER is to facilitate the creation of a single, competitive, efficient and sustainable EU internal energy market that works in the public interest.

CEER works closely with (and supports) the Agency for the Cooperation of Energy Regulators (ACER). ACER, which has its seat in Ljubljana, is an EU Agency with its own staff and resources. CEER, based in Brussels, deals with many complementary (and not overlapping) issues to ACER's work such as international issues, smart grids, sustainability and customer issues.

The work of CEER is structured according to a number of working groups and task forces, composed of staff members of the national energy regulatory authorities, and supported by the CEER Secretariat.