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## **Reply of the CEZ Group to the public consultation on Generation adequacy, capacity mechanisms and the internal market in electricity**

CEZ Group welcomes the opportunity to express its opinion on the different capacity mechanisms existing in the EU. Before answering the concrete questions asked in the consultation paper, CEZ Group would like to make some general remarks on capacity mechanisms.

Firstly, CEZ Group believes that fundamentally the internal market is a self-correcting mechanism that enables energy markets to function under normal conditions without any support mechanisms. However, the functioning of the internal market is being currently hampered by a wide range of support schemes for renewables, which as such make the system more expensive and lead to decreasing returns from conventional resources. Existing feed in tariffs (FITs) for renewables should be abolished as the renewables technologies are already mature enough, those investments which need stabilization of revenues should be integrated into the market as much as possible. Moreover, any new FITs should be technologically neutral.

In order for the internal market to fulfill its expected function, it is essential that the EU restores the proper functioning of the Emissions Trading Scheme (EU ETS). For the time being with prices around 5 EUR, EU ETS does not motivate any investments into modernization of energy portfolio towards decarbonisation of the power sector by 2050. The existing investments are realized only in the field of guaranteed renewables. In the current highly uncertain market context support mechanisms reducing uncertainty to a tolerable level may well be required for new investments to be made. However, as stated in the consultation paper, it is important that such mechanisms be properly designed such that they do not distort the functioning of the internal market.

CEZ Group considers that there should be no capacity payments available for existing power plants. The current capacity schemes should be abolished when consistent with maintaining security of supply. The EU should coordinate this process. The internal market should not be distorted by any unjustified subventions; however in order to be able to deal with their consequences, the Member States should be allowed to temporarily as a short term solution establish capacity mechanisms to ensure security of supply. Electricity produced under such schemes should not be allowed to be exported



from the given Member State. Otherwise distortions are exported. All capacity mechanisms should be discontinued once EU ETS is fully functional and FITs are removed. Capacity mechanisms should be available only for technologies complying with emission limits set by the relevant legislation.

CEZ Group's answers to the concrete consultation's questions follow.

**1) Do you consider that the current market prices prevent investments in needed generation capacity?**

Yes, prices are mainly distorted by different forms of subvention of renewable sources and the ongoing market failure of the EU ETS system, which at its historically forecasted (and desired) level would have promoted naturally new construction and refurbishment of generation capacity.

**2) Do you consider that support (e.g. direct financial support, priority dispatch or special network fees) for specific energy sources (renewables, coal, nuclear) undermines investments needed to ensure generation adequacy? If yes, how and to what extent? It depends on specific energy source:**

Existing support schemes are not technologically neutral and have a number of negative secondary effects. Support schemes are meant to be temporary, operating only until the given technologies are mature enough to be competitive in the market. As this situation of maturity has already happened, such support schemes should be discontinued. The other key issue, already mentioned above, is the need to restore the proper functioning of the EU ETS system.

Low or no market integration of certain technologies, such as renewables, undermines the stability of investment signals for market based investments. Priority dispatch of renewables also adversely affects the stability of grids and cross-border trade due to intermittent and loop flows.

**3) Do you consider that work on the establishment of cross-border day ahead, intraday and balancing markets will contribute to ensuring security of supply? Within what timeframe do you see this happening?**

Improved cross-border trading is a necessary measure which will optimize the use of existing capacities and lower the costs for consumers. It will contribute to ensuring security of supply only if sufficient cross-border capacities are available for trading purposes. However, by itself it will not promote new investment which would ensure security of supply, especially if the markets do not offer long-term stable outlook on available cross-border capacities, which are necessary for investors to trust the long-term viability of markets.

The timeframe is influenced by the different issues of neighboring TSOs. The framework guidelines and network codes should motivate TSOs to increase cross-border trading in a predefined time plan.



- 4) What additional steps, if any, should be taken at European level to ensure that internal market rules fully contribute to ensuring generation adequacy and security of supply?**

EU ETS should be reinvigorated in order to promote investment in new generation capacity and refurbishment of existing capacity. Support schemes should not hamper the functioning of the internal market and must be consistent with competition rules.

- 5) What additional steps could Member States take to support the effectiveness of the internal market in delivering generation adequacy?**

CEZ Group shares the Commission's view that the 3<sup>rd</sup> liberalization package should be fully implemented and respected by all MS in order to create a comparable business and market environment across the EU.

All support schemes established by Member States aiming at creating the conditions necessary for new investments in generation capacity should fulfill the collective goals of competitiveness, sustainability and security of supply.

- 6) How should public authorities reflect the preferences of consumers in relation to security of supply? How can they reflect preferences for lower standards on the part of some consumers?**

The essence of security of supply is that there is sufficient generation capacity to keep the lights on at all times. This standard of security of supply cannot be contested and questioned.

- 7) Do you consider that there is a need for review of how generation adequacy assessments are carried out in the internal market? In particular, is there a need for more in depth generation adequacy reviews at:**

- a) National level**
- b) Regional Level**
- c) European Level**

CEZ Group considers there is no need for review of how generation adequacy assessments are carried out in the internal market.

- 8) Looking forward, is the generation adequacy outlook produced by ENTSO-E sufficiently detailed? In particular,**

- a) Is there a need for a regional or European assessment of the availability of flexible capacity?**

There is certainly need for a regional assessment mostly of the availability of intermittent capacity and its balancing.

- b) Are there other areas where this generation adequacy assessment should be made more detailed?**

CEZ Group does not believe that other areas should become a subject of more detailed generation adequacy assessment.

- 9) Do you consider the Electricity Security of Supply Directive to be adequate? If it should be revised, on which points?**

CEZ Group is of the view that the ESS Directive is adequate and does not require further revisions.



**10) Would you support the introduction of mandatory risk assessments or generation adequacy plans at national and regional level similar to those required under the Gas Security of Supply Regulation?**

A possible risk assessment at regional level could only highlight problems already known, however it will not contribute much to their resolution. More efforts should be made to eliminate already identified barriers to the internal energy market.

**11) Should generation adequacy standards be harmonised across the EU? What should be that standard or how could it be developed taking into account potentially diverging preference regarding security of supply?**

No – generation adequacy standards should not be harmonized before all elements of the 3<sup>rd</sup> liberalization package have been fairly and properly implemented in all member states. Even then it is questionable whether such standards could properly reflect national specificities and compliance with Lisbon treaty provisions.

**12) Do you consider that capacity mechanisms should be introduced only if and when steps to improve market functioning are clearly insufficient?**

Yes – the current market uncertainties combined with the malfunctioning of EU ETS create a context in which there is often no sound business case for investing in the capacity needed to guarantee security of supply. In these circumstances capacity mechanisms may be necessary. While CEZ Group hopes and believes that the current market malfunctioning can and will be addressed (this means the EU ETS reform, real implementation of 3rd liberalization package in all MS and RES being responsible for balancing), this prospect does not address the failure of the current market place to support the investments needed to ensure security of supply and achieve decarbonisation targets. Support mechanism may therefore be required today even if they would turn out no longer to be necessary by the time that the new capacity is built because absent such mechanism the project will not go forward. It is important that the Commission takes this time dimension into account when assessing whether improvements in market functioning eliminate the need for support mechanisms. The Commission must distinguish improvements that can be achieved in the short term and those that will materialize only in a longer time frame. The latter are unlikely to address current investment impediments because investors want to see the improvements before they factor them into their investment decisions.

**13) Under what circumstances would you consider market functioning to be insufficient:**

- a) to ensure that new flexible resources are delivered?**
- b) to ensure sufficient capacity is available to meet demand on the system at times of highest system stress?**

The market is capable of covering demand/consumption including peak consumption by itself if not being distorted by different forms of RES support. CEZ Group takes the view that schemes that remunerate flexibility are on the same footing as other schemes that distort markets. Flexibility should be delivered by market participant adapting their generation portfolios to market needs.



**14) In relation to strategic reserves:**

**a) Do you consider that the introduction of a strategic reserve can support the transition from a fossil fuel based electricity system or during a nuclear phase out?**

Such an introduction during a nuclear phase out would further distort the ability of markets to deliver necessary sources by itself; furthermore, in CEZ Group's view nuclear phase out would hamper the EU's ability to achieve its low carbon goals for 2030 and 2050. It is not realistic to achieve these targets without nuclear generation.

**b) What risks, if any, to effective competition and the functioning of the internal market do you consider being associated with the introduction of strategic reserves?**

As already mentioned – the risk is further distortion of markets that as a result are unable to deliver the right price signals and thus deliver new investments.

**15) In relation to capacity markets and/or payments:**

**a) Which models of capacity market and/or payments do you consider to be most and least distortionary and most compatible with the effective competition and the functioning of the internal market, and why?**

The least distortive model is one that is technologically neutral covering only new power plants. It leaves all technologies on an equal footing, increasing the likelihood that the outcome is fit for purpose while reducing the distortive effects. When the technology is not dictated, the market will deliver the economically most attractive result. Moreover, by limiting the scheme to new plants, distortions are limited to what is strictly needed to deliver new investments. When existing capacity is included, there are wider distortive effects. If the model is extended to existing capacity, there must be clear evidence that the capacity would otherwise exit the market on a permanent basis.

**b) Which models of capacity market and /or payments do you consider to be most compatible with ensuring flexibility in a low carbon electricity system?**

Idem.

**c) Are there any models of capacity mechanism the introduction of which would be irreversible, or reversible only with great difficulty?**

Every model of CM supporting current generation sources is irreversible in the sense that it distorts market functioning for the period of time in which it operates.

**16) Which models of capacity mechanisms do you consider to have the least impact on costs for final consumers?**

Temporary models supporting new and technologically neutral generation capacity needed for ensuring security of supply until phase out of feed-in-tariffs for RES is completed and proper functioning of EU ETS is restored.

There should be a clear predefined timeline/procedure for the phase-out of the FITs, so that the support has a clear end.

**17) To what extent do you consider capacity mechanisms could build on balancing market regimes to encourage flexibility in all its forms?**

CEZ Group does not support artificial flexibility support as stated in the answer to question 13.



**18) Should the Commission set out to provide the blueprint for an EU-wide capacity mechanism?**

Any capacity mechanisms for existing power plants should be coordinated at the EU level. However, as regards capacity mechanisms for new power plants, Member States should remain responsible for introducing temporarily such mechanisms as a short term solution.

**19) Do you consider that the European Commission should develop detailed criteria to assess the compatibility of capacity mechanisms with the internal energy market?**

Yes, the European Commission has to ensure full compatibility between different existing capacity mechanisms and the internal energy market.

**20) Do you consider the detailed criteria set out above to be appropriate?**

Criteria developed by the European Commission seem appropriate; however, they should be explained more in detail and put into the state aid guidelines context.

**a) Should any criteria be added to this list?**

No, the list of criteria seems to be complete.

**b) Which, if any, criteria should be given most weight?**

N/A.