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European Commission Consultation Paper on generation adequacy, capacity mechanisms and the internal market in electricity

Danish Energy Association finds the consultation document and questions on generation adequacy, capacity mechanisms and the internal market very relevant as a follow up on the Internal Energy Market Communication. Our assessment is that the EU internal energy market is now standing at a cross-road, where the functionality of the internal market is to stand its tests. More and more countries are starting the discussion on capacity mechanisms, and several are already using them. National measures are endangering the functionality of the internal energy market, but at the same time, there are reasons for concerns on the security of supply when the energy mix is changing in the pace we are witnessing at the moment.

The discussion on security of supply and lack of capacity arises as European power plants, amongst them also Danish plants, are not able to cover fixed costs through the energy markets. Hence, it is necessary to discuss how to address the integration of renewable energy on market terms, while not jeopardizing the evolvement of one European energy market and the security of supply.

Following, Danish Energy Association would like to stress the need for a transparent discussion of, how security of supply is maintained under consideration of the internal energy market and increasing shares of renewable energy. The new element in the evaluation of security of supply is to include decisions made in neighboring countries, and how these affect national security of supply and the competition across countries. E.g., integration and improvement of existing markets and extension of cross boarder markets for ancillary services.

To improve the internal energy market there are three main issues to address:

1. Exposing all actors to market prices in the energy and balancing markets (both producers and consumers) in order to improve demand flexibility and flexible power production.
2. Efficient and non-discriminatory utilization of the European transmission grid is a prerequisite for the development towards a true pan-European electricity market.

3. Increased investment in transmission lines, which allows Member States to pool and share generation resources, and thereby, reduces the need for purely national reserves.

Only if the above mentioned measures to allow the market to work and provide generation adequacy have been taken and proven not to be sufficient or to address temporary challenges in transition periods to for example more grid and more demand flexibility, the introduction of market based capacity mechanisms should be considered.

In that case, any capacity mechanism must be carefully evaluated so that it interferes as little as possible with a functioning market. In addition, the capacity remuneration mechanisms (CRMs) must be designed in a coordinated way between the member states to avoid effects on competition. From the internal market point of view it is not useful to design CRMs solely from the point of view of one member state. In addition a sunset clause and review mechanism should be included in the CRM from the start.

Reply to selected questions in the consultation (1+3+5+7+8+10+11):

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

The current prices are not able to generate investments in new capacity. This central question is if no investments are needed (signaled by low power prices) or if investments are needed (power prices are not reflecting scarcity). Danish Energy Association finds that prices are currently not able to reflect the right need, due to political uncertainty and large volumes of subsidized power.

Today's distorted market and the increasing political risks and red tape for generation investment other than subsidized is not promoting new investments - other than those based on subsidies. Only a minor share of new investments today is market based. Market prices cannot deliver in an overly complex environment with multiple overlapping policies and steering mechanisms, so the first step should be to make RES subsidies market compatible and create a stable regulatory environment to allow markets to work.

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

Yes, market integration on all timeframes considerably improves security of supply, as resources from the whole area can be automatically used to cover a deficit in one of the areas. Generation and demand trading them into balance close to real time in the day ahead and intraday markets support balancing carried out in the real time market. The integration of balancing markets requires the TSOs to share resources from a common merit order will advance, which will reduce cost and increase real time security of supply.

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

Member States should work for the full implementation of the 3rd energy package in their respective countries. The 3rd package incorporates important measures such as the removal

of regulated prices and price caps, but also the roll out of smart meters which would enable wider demand response. Making the internal market work (infrastructure development, market coupling, regional cooperation etc.) is to the large extent a question of political will and commitment from the Member States.

Member States could make another contribution by speeding up the permission process for both generation and transmission. Currently unpredictable permission and concession processes increase the cost, delay and even prevent investment in new generation and grid capacity, needed to increase generation adequacy.

Existing capacity remuneration mechanisms should be phased out through more reliance on cross-border trade and on market-based demand response, or at least existing capacity remuneration mechanisms effects on neighboring countries should be analyzed and reduced to a minimum as capacity mechanisms in one country can endanger generation adequacy for neighboring Member States.

(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:

Generation adequacy must be measured against the level of system security that is decided upon legally or by regulators in each area. As such, a first action could be to develop benchmarks of these system security requirements. However, the current European regulatory framework, mainly based on national schemes and some coordination at European level, results in the situation when Member States are concerned predominantly about ensuring national generation adequacy. It is even more legitimate taking into account the fact that political impact of power shortages remains largely national.

Overall, Danish Energy Association supports that there is a need for more in depth generation adequacy review especially taking into account contribution of cross border connections. This requires a firm commitment between involved countries by sharing interconnection resources, avoiding cuts of interconnection in case of scarcity, and so respecting trade agreements.

Based on electrical infrastructures, there are no systematic reasons to differ between national and regional levels, as cross border capacity needs to be accounted for. However, considering the diversity of situations of Member States' regulatory framework, political orientations, and considering that the current transport system is based on historical national approach, this scale is usually the most pertinent to assess generation adequacy, while taking into account the contribution of interconnections by reducing or increasing each Member State capacity needs.

Following this, all Member States should include evaluation of interconnectors and status in neighboring countries in the security of supply evaluation, taking historical availability of the lines and power plants into consideration.

(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?

Overall, more transparency is needed. Any assessment should transparently show the amount of balancing reserves contracted by the TSOs, and on how these resources are used, and some trends for the future. In general flexibility can be provided by most power plants and the capacity structure is in principle a result of an economic optimization.

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

Again, more transparency is needed. Common rules and methodology for Member States to do their assessments could enhance transparency. Furthermore, assessments should take into account the impact of the integrated market. The assessments should be detailed and should also include different scenarios – risk assessment of transmission lines, thermal capacity, flexibility etc.

(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?

Danish Energy Association believes that risk assessment is a good tool to enhance the level of security of supply, but at the same time recognizes that the existing non-binding TYNDP performed by ENTSO-E already addresses the concept of security of supply (Regulation 714/2009). Instead of introducing new reports it would therefore be preferable to build the risk assessment on the TYNDP, enhance the transparency in terms of regional planning and focus on the flexibility of the system and its ability to integrate intermittent resources.

The emphasis must be in improving market functioning, not in creating new mechanisms or administrative procedures. However, if capacity mechanism criteria are introduced, there should be an obligation for the country planning to implement a CRM to produce clear evidence on the justification of such mechanism and a risk assessment, which must take into account cross-border trade and availability of generation capacity and demand response in neighboring countries, should be part of that.

Summing up, Danish Energy Association would like to see that, if capacity mechanisms are used, they are designed on market terms and in consideration of equal and fair competition for all actors in the market independent of nationality and type of generation.

Yours sincerely,

Danish Energy Association



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