



European Commission
Directorate-General for Competition
Unit for State aid Energy and Environment

Ref.: "HT 359 - Consultation on Community Guidelines on State Aid for Environmental Protection"

February 2014

Consultation on DG Competition's draft Guidelines on environmental and energy aid for 2014-2020

E3G response

Registration number 07783117686-61

We thank the European Commission for the opportunity to express our view on the draft environmental and energy aid (EEAG). This document will be an important tool for managing Member State interventions and guiding the transition towards a competitive and highly resource efficient economy.

Key points

The transformation to a low carbon and resource efficient economy will involve major increases in investment, rapid innovation and new markets creation across Europe in the next decade. An effective state aid framework will be critical for creating the conditions for efficient transformation by removing support to inefficient and polluting industries, and opening markets to competition, innovation, new entrants and disruptive business models. In this context we encourage the Commission to:

- Increase the level of aid intensity to energy efficiency measures. The proposed level is currently too low to incentivise the necessary investment to ensure European competitiveness, energy security and reduce emissions.
- Secure a level playing field between demand and supply resources in capacity mechanisms. Currently, capacity mechanisms risk further reinforcing the dominant market position of incumbents and, in some cases, prolonging harmful subsidies to fossil fuel fired plant.
- Prevent subsidies to the most inefficient fossil fuel plant while addressing adequacy concerns through the introduction of an emissions performance standard.
- Include demand-side management in the scope of these guidelines to enable Member States to grow their demand-side resources.
- Increase the threshold for small renewables installation to allow for further development of community scale renewables and participation of new entrants.

1. General / Scope of the guidelines

We very much welcome the extension of the environmental aid guidelines to cover energy aid. The European energy policy objectives of security, sustainability, affordability are strongly intertwined and therefore better addressed collectively, rather than in isolation.

We however think that the current draft creates undue uncertainty regarding specific tools and instruments available to Member States. Our main recommendation regarding the scope of the EEAG is:

- Clarify the place of demand management in the guidelines

Demand side management does not currently fit in the scope of these guidelines. Demand response for instance does not fall within the definition of energy efficiency, infrastructure, or even eco-innovation. We propose that the definition of energy efficiency and/or infrastructure is expanded in the final EEAG, or that a specific definition and section for measures is added that allows for the development of demand-side management.

2. Energy efficiency

The current draft presents energy efficiency as a purely environmental measure. It does not take into account the important benefits to energy security, affordability (reducing energy costs) and competitiveness. If the full range of benefits and market barriers were included, it would justify greater support and a higher priority status. Our main recommendations regarding energy efficiency are:

- Present energy efficiency measures as benefiting the internal market as well as the environment.
- Increase the aid intensity to energy efficiency measures to 100% of eligible costs.
- Make investment in energy efficiency as a pre-condition for tax exemptions.

Present energy efficiency measures as benefiting the internal market as well as the environment.

Energy efficiency is widely recognised for its contribution to all major objectives of EU climate and energy policies. Most recently, the European Commission praised it for improving competitiveness, security of supply, sustainability, and enabling the transition to a low carbon economy in its communication on the 2030 climate and energy package. The Internal Energy Agency also considers investments in energy efficiency to cut energy bills, improve health, increase competitiveness and improve consumer welfare.

This however is not reflected in the EEAG. We thus propose the following changes:

- Explicitly address energy efficiency's potential contributions to the objectives of common interest that are security of supply, functioning of the internal energy market and affordability in articles (139) and (141).

(139) By way of derogation from section 5.1.1, in order to ensure that aid contributes to a higher level of environmental protection and/or to a stronger internal energy market, etc.

(141) To demonstrate the contribution of an individually notified aid to an increased level of environmental protection and/or to a stronger internal energy market, etc.

- Expand on the 'need for state aid' for energy efficiency. The current text narrowly defines state aid for energy efficiency as necessary only when counting towards meeting the energy efficiency target, reducing emission reductions, or overcoming problems of split incentives between building owners and tenants. Market failures to energy efficiency are multiple and systemic, and not at all reflected in article (142).

(142) Energy-efficiency measures target negative externalities as set out in point (42) by creating individual incentives to attain ~~environmental~~ targets for energy-efficiency, ~~and for the reduction of greenhouse gas emissions, or for the strengthening of the internal energy market~~. ~~One particular market failure which may arise in the field of energy-efficiency measures concerns energy-efficiency measures in buildings. When renovation works in buildings are considered, the benefits of energy efficiency measures do typically not accrue with the building owner which generally bears the renovation costs, but with the tenant. The Commission therefore considers that State~~

aid may be needed to promote investments in energy-efficiency in order to meet the targets of the EED.

Increase the aid intensity to energy efficiency measures to 100% of eligible costs. Proposed aid intensities of 20-40% are currently too low to incentivise investments in energy efficiency.

- The greatest barrier to implementing energy efficiency measures is the upfront costs. An aid intensity of 20-40% will not be enough to help overcome these market barriers. It must be increased to 100% to significantly reduce the cost of the total investment. .
- The proposed levels for aid intensity to energy efficiency are the lowest of all environmental and energy aid intensities. This poorly reflects the fact that energy efficiency is the EU's most effective lever to strengthen the block's energy security and economic resilience while reducing greenhouse gas emissions.
- Competitive bidding procedures are most appropriate for sectors or industries that: 1) are somehow "harmonised" in terms of technologies (in order for the tender to be effective and allowing an easy comparison of the bids); 2) have somehow proved their « marketness ». The energy efficiency sector is very heterogeneous and many energy efficiency technologies are still under development. This makes the energy efficiency sector a poor candidate for competitive bidding procedures.
- Competitive bidding procedures are in essence discriminatory to smaller players given the burden of participation (resource and time intensive process to prepare a project proposal) without any guarantee that the proposed projects will be successful in the auction.

Make investment in energy efficiency a pre-condition for tax exemptions. The European Commission's Staff Working Document 'Energy Economic Developments in Europe' released on 22 January showed that energy efficiency has allowed the European industry to maintain its lead in the export of energy intensive products despite the widening gap in energy costs between Europe and its trading partners.

We thus propose that sections 5.6 and 5.7 on 'aid in the form of reductions in or exemptions from environmental taxes' and 'aid in the form of reductions in funding support for electricity from renewable sources' build on this conclusion. Both sections could include the condition that aid will only be considered proportionate where member states can demonstrate that the recipient of the aid has taken all reasonable measures to improve efficiency of energy consumption.

3. Capacity mechanisms

We welcome the European Commission's efforts in managing Member States' interventions and attempts to secure a level playing field and overcome market failures. In particular, we fully support the explicit mention of interconnections and demand response in paragraphs (205) and (209) of section 5.9, and paragraph (212) stressing the fact that any measure should not in principle reward investments in generation from fossil fuel plants. We however think that a few amendments to the rest of the document could go a long way in ensuring the demand side of electricity markets actually do compete on a level playing field with the supply side. Our main recommendations regarding capacity mechanisms are:

- Change all terminology giving bias to supply over demand.
- Ensure that supply and demand compete on a level-playing field, and that all mechanisms are open for participation by operators from other Member States.
- Include an emissions performance standard to prevent harmful fossil fuel subsidies.

Change all terminology reflecting the historical bias towards generation. Albeit a few mentions of demand response and interconnections, the document is very much written to assess aid to generators, leaving little room for alternatives. This needs to be updated. Simple changes could allow a real level playing field, mainly through the removal of all mentions of "generation adequacy" throughout the document. Notably:

- Paragraph (18) (ii). We propose “generation adequacy” is renamed “resource adequacy”, or “system adequacy”.

Resource adequacy means there are sufficient capacity resources that are planned to be available on the power system to ensure that a prescribed reliability standard is met. A reliability standard is a probabilistic measure of the likelihood that sufficient capacity resources will be available in real time to balance supply and demand without enforced disconnection or voltage reduction, defined by organisations recognised by EU institutions as performing an essential role in the creation of a single market in electricity, such as ENTSO-E.

- Paragraph (18) (jj). We propose “generation operator” is replaced by “market operator”.

A market operator is an undertaking which can produce, consume, or deliver electrical power.

- Paragraph (18) (kk).

Capacity mechanism means a mechanism aimed at ensuring that certain resource adequacy standards are met at a defined level (usually national or regional).

- Replace ‘generation adequacy’ by ‘resource adequacy’ in various mentions throughout the text – for instance article (201), (203), (204), etc.

Ensure that supply and demand compete on a level-playing field, and that all mechanisms are open to participation for operators from other Member States. This could be done by redrafting section 5.9 while keeping in mind both demand and supply side resources and enforcing some requirements already present in the text. Notably

- Enforce article (205) by requesting Member States to demonstrate their efforts in developing alternative ways of achieving adequacy.

“Member States shall therefore primarily consider alternative ways of achieving resource adequacy which do not negatively impact on the objective of phasing out environmentally harmful subsidies, such as facilitating demand side management and increasing interconnection capacity and should be required to explain their efforts in this regard.”

- Amend article (210) into “the aid should remunerate solely the service of pure availability provided by the market operator”.

- Enforce article (212) by explicitly requiring consideration of demand-side options and assessment of energy savings and demand management potential as part of the appropriateness test for capacity mechanisms. This could be done through the addition of the following paragraph

“Member States shall primarily consider alternative ways of achieving resource adequacy, such as facilitating demand side management and increasing interconnection capacity. Member States must demonstrate their ongoing efforts in pursuing the development of these alternatives.”

- Strengthen the wording of article (218) on avoidance of negative effects

“(a) The mechanism shall be open to potential aggregation of both demand and supply, as well as participation by operators from other Member States where such participation is physically possible.”

~~(a)~~ *(a) The participation by operators using different technologies offering measures with equivalent technical performance. The restriction on participation can only be justified based on insufficient technical performance required to address the resource adequacy problem; however the inability of operators to reflect power plant operating characteristics should not be considered as a basis for insufficient technical performance in addressing resource adequacy problems.”*

Include an emissions performance standard to prevent harmful fossil fuel subsidies. As highlighted in the draft, there is a risk that measures addressing adequacy concerns may end up supporting the use of fossil fuels, which goes against the European objective of phasing out environmental harmful subsidies. The most effective way to minimise this risk is to include an emissions performance standard in the EEAG.

The provisions for the Emissions Performance Standard (EPS) could be included in section 5.9.3 on appropriateness of aid to adequacy measures. The threshold shall reflect existing EU and national commitments to limit carbon emissions; it must be reviewed on a regular basis to remain in line with future commitments. For instance:

(212) The measure should in principle not reward new investments in or extensions from fossil fuel plants unless it can be shown that a less harmful alternative to achieve generation adequacy does not exist. To this purpose, the aid should solely remunerate operators whose

- (a) Carbon emissions fall below a set threshold;*
- (b) The threshold shall reflect existing EU and national commitments to limit carbon emissions;*
- (c) The threshold must be reviewed every three years to remain in line with new commitments.*

4. Infrastructure

While we welcome the addition of a specific section on aid to energy infrastructure, we are concerned that the scope of the text is currently too narrow to allow the necessary investment in European infrastructure. Our recommendations are as follows:

- Explicitly extend the scope of guidelines beyond Projects of Common Interests and projects in assisted areas.
- Ensure aid to infrastructure is aligned with general objective of phasing out harmful fossil fuel subsidies.
- Amend text to cover smart grids and storage in section 5.8.

Explicitly extend the scope of guidelines beyond Projects of Common Interests and projects in assisted areas. Article (191) states that aid may be granted to projects of common interest (PCI) and infrastructure investments in assisted regions. Whether the scope of section 5.8 currently expands beyond the PCIs and projects in assisted regions is currently unclear. This needs to be rectified: such limitation could exclude early stage innovative projects in need of support, or create undue uncertainty for projects applying for PCI status.

Ensure aid to infrastructure is aligned with general objective of phasing out harmful fossil fuel subsidies. The development of further oil and gas infrastructure may further incentivise fossil fuel use in Europe. State aid should only be allowed if it contributes to economic growth in a positive and sustainable manner. We propose that section 5.8 explicitly forbids the granting of aid to projects incompatible with EU and national commitments to limit GHG emissions.

Amend text to cover smart grids and storage in section 5.8. Whilst the definition of energy infrastructure in article (18) (ff) does include electricity storage and equipment or installation aiming at two-way digital communication, the text of section 5.8 seems to mainly address interconnection, transmission or distribution projects. For instance statements such as “*competition is generally limited as [such] infrastructure often constitutes a natural monopoly*” (189) or “*the Commission considers that tariffs are the appropriate primary means to fund energy infrastructure*” (194) would not necessarily apply to storage or smart grid projects, which offer wider opportunities for financing and competition.

Further smart grids and electricity storage development will be needed in Europe this decade. It would be beneficial to clarify what aid could be considered acceptable.

5. Renewables

We are concerned that the current draft is too prescriptive when it comes to support to renewables, and as such would hinder further decarbonisation of the European energy sector. The current text does not allow any flexibility for national circumstances and favours incumbent players. Our main recommendations to reduce these impacts are as follows

- Increase the threshold for small-scale renewables to 10MW.
- Allow any transition schemes providing it covers a short period, and that the enduring scheme is compliant.
- Allow flexibility for the definition of deployed vs non-deployed technologies.

Increase the threshold for small installations to 10MW. The current draft risks favouring incumbents and discriminating against community-scale renewables and small players.

- Standard balancing responsibilities will be prescriptive for new entrants and small players.
- Competitive bidding processes are by nature discriminatory to smaller players given the burden of participation (resource and time intensive process to prepare a project proposal) without any guarantee that the proposed projects will be successful in the auctions. In addition, incumbents are advantaged in the bidding process due to their experience and lower financing costs.
- Increasing the threshold to 10MW would allow smaller players to qualify for feed-in-tariffs.

Allow any transition scheme providing it covers a short period, and that the enduring scheme is compliant. Any changes in existing RES schemes to transition towards new arrangements should not, in themselves, be considered a change that needs to be compliant with the new guidelines, provided the transitional period is short and the enduring scheme is compliant.

Allow flexibility for the definition of deployed vs non-deployed technologies. The European Commission should consider alternative definitions.

- The current definition of deployed renewable technologies is unclear: when would a non-deployed technology move to the 'deployed' category? Would national schemes need to be amended as a result?
- The fact a technology is deployed at the European level does not necessarily mean that the relevant supply chain is available in all countries. Developing that supply chain may require additional support on a temporary basis.

Main contact

Manon Dufour
E3G - Third Generation Environmentalism
manon.dufour@e3g.org
M: +32 (0)477 76 78 01
T: +32 (0)2 893 9212

Rue de la Science 23
1040 Bruxelles
Belgium

About E3G

E3G is an independent, non-profit European organisation operating in the public interest to accelerate the global transition to sustainable development.

E3G builds cross-sectoral coalitions to achieve carefully defined outcomes, chosen for their capacity to leverage change.

E3G works closely with like-minded partners in government, politics, business, civil society, science, the media, public interest foundations and elsewhere.

More information is available at www.e3g.org