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ELECTRICITY FOR EUROPE

EUROPEAN ENERGY AT A DECISIVE CROSSROADS

Statement addressed to Heads of State and Government

European Council
Brussels, 4 February 2011

EURELECTRIC welcomes the increased focus accorded to energy and climate policy in recent years. EURELECTRIC is particularly supportive of the initiative to organise, on 4 February 2011, a first-ever "thematic" European Council focused exclusively on energy. As input to the EU Summit, EURELECTRIC has highlighted in the paragraphs below a number of concerns about Europe's energy future, together with four key recommendations. EURELECTRIC is available to discuss any of the issues raised in its paper in further detail.

Europe is at an unprecedented energy crossroads, facing an urgent need for sizeable power investments in the coming two decades. Total investments up to 2030 (generation and infrastructure) are estimated at one trillion euro, implying a substantial boost from the current investment levels of today. Given the crucial importance of achieving a sustainable, competitively-priced and low-carbon economy, it is time for a broader vision of the role and importance of electricity as well as for greater regulatory coherence and stability.

Electricity is key to a secure, sustainable and competitive future. With its potential for carbon neutrality, the electricity sector is determined to play its part in the decarbonisation of society.

In this context, it is important that carbon and electricity markets are allowed to function properly and that the right price signals are provided to customers. The industry needs to be able to plan and deliver investments in a timely and efficient manner. As price signals are the main drivers for efficient investments in low-carbon technologies, it is important that these are not artificially distorted.

Additional renewable energy generation capacities will require timely investments in grid expansion and refurbishment, so that there is an urgent need to address transmission and distribution infrastructures.

Ensuring security of supply, encouraging energy efficiency and boosting R&D spending on energy projects are equally important parts of the low-carbon equation. Provided that strong and consistent political action is taken to ensure the right investment framework, both industry and the economy stand to benefit in the long-run.

Given the right policy framework, the members of EURELECTRIC are optimistic that a carbon-neutral electricity sector can be achieved by 2050.

1. The main political and economic initiative of the EU over the past decades for a deeper and sustainable integration of Europe has been the Euro, as Europe's common currency. Similarly, the Emissions Trading Scheme (ETS), as one of the main sectoral initiatives of the internal market, is a clear driving force for climate and sustainable development policy, also impacting deeply on the energy sector. However, both policies are visibly under pressure and need urgent decisive support actions from the European Commission and the Member States. The lack of a joint support policy across Europe and the absence of strong political leadership are the factors that could jeopardize these common projects today.

2. The current development around the Euro and the substantial political fissures to which this has given rise can be explained with prevailing national interests. These in turn have required enormous joint efforts to prevent the collapse of this common currency and avoid undermining the goal of a common monetary union.

For the founders of the European Union the decisive question was: What is the price for non-implementation of the internal market? In other words, what would be the welfare losses in the case of separate closed national markets?

Today, the internal market for goods and services is a self-evident reality in most areas of economic activity and produces huge welfare benefits for its citizens across Europe. But for the electricity industry the common market is still mainly an aspiration.

3. We fear that in energy and climate change policies we are seeing a replay of comparable developments that today endanger the Euro.

ETS was designed as an efficient market tool to drive a coordinated policy towards a low carbon, competitive European economy. But in the absence of a deeper coordination of energy policies and in the face of conflicting national initiatives, the ETS may fail and also the dream of an integrated European energy market.

The current situation of the European energy sector is unsatisfactory. In this sector the internal market largely remains an empty shell. Many national markets are still closed to a significant extent with governments focusing on national energy policy interests supported by purely national instruments.

It is therefore high time to ask the question: What is the price for non-implementation of a real common market in energy? What kind of losses in terms of social welfare and efficiency are suffered due to the continuation of fragmented markets and the use of uncoordinated instruments?

4. While it cannot be denied that significant progress has been made in several specific areas in recent years, alarming deficits in the common energy policy that undermine the investment climate are still prevalent:

a) Renewables Growth

- The current European Renewable policy translates into national subsidy schemes for RES-E, which has led, in some cases, to an expensive system of rigid feed-in schemes (e.g. PV in Germany, Czech Republic, Spain), representing a redistribution of wealth on account of the national end customers and the competitiveness of those economies at large.
- Competition between national governments to attract investors in renewables takes place on the basis of highest subsidies, instead of optimal location and technology options.
- The European internal energy market is being turned into separate closed markets by this development with increasing shares of 'ring-fenced' generation with market risk free feed-in tariffs.
- These elements lead to regionally overheated situations, with governments adjusting subsidy schemes accordingly.
- This trend is resulting in a system with high cost for RES growth due to inefficiency and high uncertainty among investors and as a consequence decreasing support of RES from society.

b) Infrastructure

- Investments in grid expansion and modernisation and reinforcement of interconnections are crucial for the development of an integrated market. The predominantly national view of regulators and grid operators in this regard results in uncoordinated expansion of infrastructure for the connection of RES generation leading to the misallocation of funds. Peripheral regions are often not sufficiently considered. In addition, a lack of public acceptance inhibits investments in important transmission grid infrastructure and generating plant, jeopardizing competitiveness and the efficient allocation of resources.
- This leads to national system inadequacies (concentration of intermittent RES surrounded by grid bottlenecks), that would not necessarily occur in a market with higher integration and better supervision and coordination.

c) Market regulation

- Market functioning is no longer assured in the medium term as a consequence of continued treatment of renewables in isolation from the market and other low-carbon technologies.
- Several Member States are discussing adjustments of national market design e.g. to change from energy-only markets to capacity markets – however, these discussions are purely national, leading to a further disconnect between the energy markets across Europe.
- Every change in a national market will influence all connected neighbouring countries and will damage the idea of European market integration, if these changes do not converge.
- Countries introducing Robin-Hood-taxes, price-caps or other fiscal instruments, or regulating wholesale or retail prices, eat into the capital available for the urgently needed investments.

d) Climate Policy

- The EU is keen to act as a global leader on climate policy but fails to recognise that not many countries are following the European approach to reach a low carbon society.
- The cornerstone of EU climate policy should be the EU emissions trading scheme as a harmonised market-oriented system to reach politically set reduction targets. However, lack of progress on an international agreement brings increasing uncertainty as to its long-term survival.
- In addition, the ETS targets and timescales fail to align with the long pay-back timescales for remunerating low carbon investments.
- Given the fact that many of our non-European competitors do not follow this track, energy-intensive production is jeopardized in the EU even with the complicated special treatment in the ETS.

- Within Europe, full integration of Switzerland as a non-EU country in the ETS market is vital.
- Furthermore there are ongoing discussions in several Member States on the introduction of a carbon floor price contradicting the principles of ETS.
- As a consequence of mandatory targets for renewable energy and its treatment in isolation from the market, new coal fired power stations, CCS technology and nuclear energy, are not treated in a technologically neutral way with respect to the ETS with the result that the scheme may not deliver reductions cost-effectively.
- Furthermore, there is no common understanding of the interaction between the ETS and national subsidies for energy efficiency and renewable energy to deliver cost effective emissions reduction.

e) Energy Efficiency

- One of the most important issues for the transformation of the energy system is enhancing energy efficiency. A critical and immediate task for policymakers is to develop the necessary regulatory, fiscal and informational tools to overcome the current obstacles to mass investment in demand-side measures, bearing in mind the unique role of energy companies (electrification of road transport, efficient electro-technologies for heating and cooling, cogeneration and district heating etc).

f) Security of Supply

- For some years the European Commission and Parliament have been pleading for a common external energy policy and "speaking with one voice". On the other hand, few concrete actions have been taken and several Member States appear to have little real interest in a shared approach to this topic.
- Member States with strong integration with neighbouring non-EU-markets face different energy market challenges and constraints in relation to security of supply compared to other EU Member States. The EU should have a coherent internal and external energy policy.
- Energy storage on a large scale is needed to integrate the higher share of intermittent renewables in Europe; however the Member States try to find optimal national solutions.
- Proposals for measures such as emissions performance standards (EPS) applied in some Member States run counter to fuel diversity and undermine the EU ETS.
- Gas and electricity are tightly connected commodities and both are vital for the security of supply in Europe as a whole.

5. All six areas mentioned above highlight a significant tendency towards national solutions, which are not only suboptimal but also contradict the European vision of a harmonized and integrated energy market. If these developments continue, the projected significant increase of renewable electricity production will severely undermine the idea of a European internal market for electricity:

- Markets will stay or become more and more national – and regional integration will be weakened.
- National policy intervention will distort markets and therefore hinder the ability to find efficient solutions.
- System inadequacies will similarly be tackled on a national level, since the regulators are mainly concerned with national jurisdictions and have little real interest in regional problems.
- All investment decisions in Europe will face a higher risk and reduced chances of success.
- National solutions for infrastructure development and RES schemes will lead to suboptimal solutions, which will hence increase the cost of electricity - which in turn will endanger the target of the Lisbon agenda to make Europe "the most competitive economy". (According to EWI, the Institute of Energy Economics at the University of Cologne, a Europe-wide-harmonisation of renewable support schemes would save costs of up to € 174 bn in the period to 2020, if compared to a continuation of national feed-in systems).

6. If Europe wants to be the front runner in climate change policies and take the international lead as a low-carbon society, it is imperative to tackle these issues now and look for solutions that are cost effective, more efficient and enable competitiveness for this continent.

In other words: we will have to invest in renewables in locations where the cost is lowest and not where subsidies are highest; storage for electricity will need to be built where it can be used most cost-effectively; we will have to opt for the most efficient technologies and not those most popular with public opinion; and we will have to choose those measures where carbon abatement costs are the lowest for the whole of Europe.

7. Numerous studies have proven that efficiency gains are greatest when decisions are left to the market in one common framework at European level. A harmonised framework for RES development, an EU wide coordinated approach for infrastructure development and a fully integrated energy market, would ensure the 20/20/20 targets are achieved as economically as possible, offering benefits for the whole European society:

- Larger markets offer better opportunities for competition. Cost-reflective pricing systems promote current, state-of-the-art technologies.
- We should have integrated market rules. Rules are the crucial part of defining where the grid should be developed or what kind of new power station should be built.
- High regional concentrations and inflexible feed-in schemes have considerable impact on networks. In the first instance, a gradual harmonisation of renewable support schemes supported by increasing market integration of national production systems through strengthened cross-border transmission capacity is required. Given the need for a stable generation mix, adequate remuneration of back-up capacity to cover intermittency of generation could be considered at EU level. In the medium term, all support schemes should be progressively withdrawn and be substituted by a strong carbon price signal – this will enable an economically efficient level playing field for all low-carbon generation.
- Speaking with one voice to other world regions will have positive effects for the procurement of energy sources (gas, coal, uranium). This will also result in a competitive landscape at EU borders for electricity produced in EU and non-EU countries.
- A well-balanced, market oriented approach on emission reduction efforts across all sectors, with the ETS as the main instrument without political interference, will deliver cost-effective reduction and create a stable environment for long-term investments.
- An EU wide view (instead of a national view) on the electricity system i.e. a consistent and coherent view of grid expansion and generation needs in line with market instruments will lead to higher security for investments in conventional and renewable generation assets and grid. Investments are thus allocated most efficiently in a regional market e.g. renewables production at sites with the highest wind speeds, the highest solar influx etc. and grid investments, where the most pressing bottlenecks exist.
- Consequently investment would be reduced to the minimum necessary, leading to lower energy prices for the consumers.

Recommendations

We call upon Heads of State and Government at this first thematic European Council, to take up the energy challenge together with the European Commission and Parliament, to make it visible to the public, and provide answers within the term of the current Commission, ending 2014. The Commission should also challenge national initiatives that jeopardize the common goal until necessary common answers are tabled.

We urge Heads of State and Government to dramatically shorten the process to obtain licences to build energy infrastructure, including new transmission lines. Without such a change the RES targets will stand much less chance of being met and security of supply will be impaired.

We recommend in particular that direct action be taken within four specific areas:

- Ensure full implementation of existing internal Energy market legislation (for gas and electricity) in all Member States, legally as well as in practice. Tougher enforcement and "policing" of national regulatory decisions are imperative in this respect in order to safeguard that no national elements are introduced which endanger the competitiveness of the European internal market. Market coupling should be applied between all regions at the latest by 2015. There is also an urgent need for new high voltage network capacity within the EU, especially the North-South axis to integrate the huge RES potential in the North and South to high consumption centres in Central Europe.

- Progress climate targets and measures in a structured and well-signalled manner in line with best scientific advice. The EU Emissions Trading Scheme (ETS) should become the essential driver in the change towards a low-carbon economy. However, the system requires further improvement, longer-term clarity and development in terms of efficiency, transparency and effectiveness before it can provide the right price signals for long-term investments. It is very important to manage, through the ETS system, the transformation to the low carbon economy, without compromising the European economy. EURELECTRIC is willing to constructively enter into such a dialogue with that purpose.

- Discuss ways to harmonise the different national subsidies for RES at EU level possibly by replacing the electricity share of the 20% goal with an obligation on industry to deliver 30-35% renewable energy of all electricity sold through markets/ exchanges. The transition should be smooth and completed by 2020 without losing momentum in the RES deployment. RES support mechanisms should then be progressively phased out by 2030 and replaced with a strong carbon price signal. There will be a need to analyse the impact of changing the present national solutions. In the short-term it is important to make operational the cooperation mechanisms available to Member States under the renewables Directive. Fossil fuel subsidies should be phased out after 2018 and, in addition, there should be no national taxes on the use of fossil fuels for power generation.

- Radically refocus and substantially increase European and national R&D spending on a new intelligent energy economy. Energy R&D should receive priority in overall R&D budgets. Support should focus only on technologies which have a reasonable chance of reaching market viability anticipated under carbon reduction regimes. Priority should thus be given to technologies which can result in the highest carbon reductions e.g. nuclear, CCS, RES, smart grids and electric transport. Funds should be distributed in a transparent way, ensuring benefits for the whole of society.

  The Europe-wide need to increase education in the energy field should be tackled in order to guarantee availability of experts in the energy field.

  Actions to decarbonise the heating and transport sectors through electrification should be given further attention.

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The Union of the Electricity Industry - EURELECTRIC is the sector association representing the common interests of the electricity industry at pan-European level, plus its affiliates and associates on several other continents.

EURELECTRIC's mission is to contribute to the development and competitiveness of the electricity industry and to promote the role of electricity in the advancement of society.

EURELECTRIC's Full Member structure is based on national representation, via the national electricity association, where such a body exists, or the leading electricity enterprise in each country. Currently there are 33 Full Members, including all 27 EU Member States, current applicants negotiating to join the European Union, plus other European OECD countries.

Membership is enriched by European and International Affiliate Members representing the electricity industry across the rest of Europe, in the Mediterranean basin and on other continents, and by Business Associate Members from other sectors with stakeholder links to or interest in the electricity industry.

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