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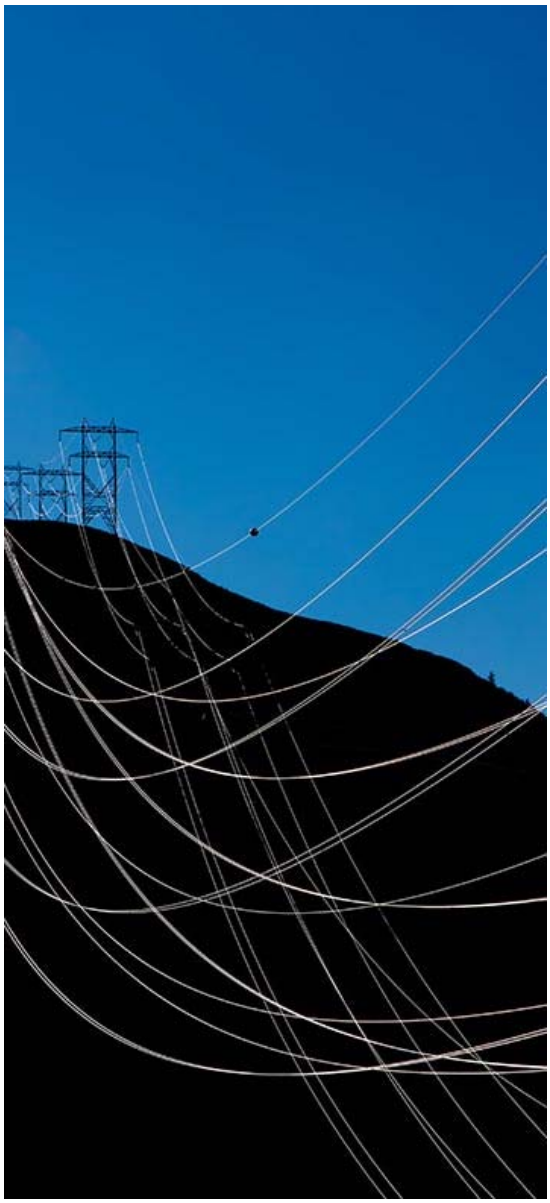
ENERGY
AND INFRASTRUCTURE

Key points: reform of European electricity market design: Regulation (EU) 2024/1747

On July 16, 2024, Regulation (EU) 2024/1747 of the European Parliament and of the Council of June 13 came into force.

European Union - Legal flash

July 2024



Key aspects

- Aiming to achieve affordable and competitive electricity prices for all national customers and the Union's industries
- Striving to stabilize markets and long-term prices by promoting power purchase agreements ("PPAs")
- Promoting financial investments in low-carbon power-generating facilities with direct support schemes by means of two-way contracts for difference ("CFDs") or equivalent schemes
- Promoting use of peak-shaving products
- Promoting non-fossil flexibility support schemes consisting of payments for the available capacity of non-fossil flexibility
- Adapting intraday markets to the participation of renewable energy technologies
- Accelerating the implementation of energy infrastructures from renewable energy sources to meet the Union's 2050 climate neutrality objective

On July 16, 2024, Regulation (EU) 2024/1747 of the European Parliament and of the Council of June 13 (the "**Regulation**") came into force, amending Regulations (EU) 2019/942 and (EU) 2019/943 regarding improving the Union's electricity market design.

In a complex context, the Regulation establishes the guidelines for the reform of the Union's electricity market design, to reduce its fluctuations and protect consumers from price variations, while also ensuring security of supply and accelerating renewable energy deployment.

Why reform the electricity market design?

The Regulation is a response to (i) the increase in fossil fuel prices (particularly gas) —drawn out over time—, and (ii) the uncertainty regarding the supply of raw materials used by power-generating facilities, which has been exacerbated by the war in Ukraine.

Its objective in the long-term is—in addition to mitigating the short-term impact of the situation—to achieve affordable and competitive electricity prices, both for national consumers and industrial clients.

Therefore, a series of guidelines have been established to reform the electricity market's design, with the ultimate aim of separating electricity prices from fossil fuel prices, acting on several fronts and seeking to guarantee the following:

- **Better end-consumer protection:** less volatile prices, flexibility of access to fixed-price and fixed-term contracts, greater transparency when accessing information, adjustment of production to consumption using smart meters.
- **Greater stability for companies**: more stable prices thanks to long-term contracts, more stable revenue by structuring new investments in low-carbon power-generating facilities in the form of two-way CFDs.
- **Greater renewable energy deployment into the electricity market**: better access to the grid, reinforced mechanisms for coordinating, exchanging and supplying information between transmission system operators, study of measures to increase the share of renewable electricity consumed.

How to achieve stabilized markets and prices

- By reforming the electricity market design, focusing on developing renewable energy and reducing the need to generate electricity from fossil fuels.
- **By reforming the long-term market**, enabling participants to hedge price risks. There are two essential mechanisms for long-term investment in renewable energy production: PPAs and CFDs.

- By enabling market operators to develop **forward hedging products and long-term forward hedging products,** to provide market participants—including owners of power-generating facilities using renewable energy sources—with appropriate possibilities for hedging financial risks against price fluctuations.

- **By promoting non-fossil flexibility,** *i.e.*, developing flexibility solutions that ensure integration of renewable energy into the grid, enabling the electricity system and grid to adjust to the variability of electricity generation and consumption across different time horizons (including the possibility for states to apply non-fossil flexibility support schemes through capacity payment schemes).

- By providing for the purchase of **peak-shaving products** in limited regional or Union-wide electricity price crisis situations.

Promoting PPAs

- PPAs are **bilateral purchase agreements** between electricity producers and buyers that are concluded on a voluntary basis and are based on market price conditions without regulatory interventions in price-setting.

- The allocation of long-term transmission rights enables market participants to hedge volatile price risks. This happens on a regular basis, in a transparent, market-based and non-discriminatory manner, through a **single allocation platform** established in line with Commission Regulation (EU) 2016/1719. The single allocation platform should act as an entity offering allocation and facilitating the trading of financial long-term transmission rights on behalf of the transmission system operators, between the different bidding zones and, where relevant, the regional virtual hubs.

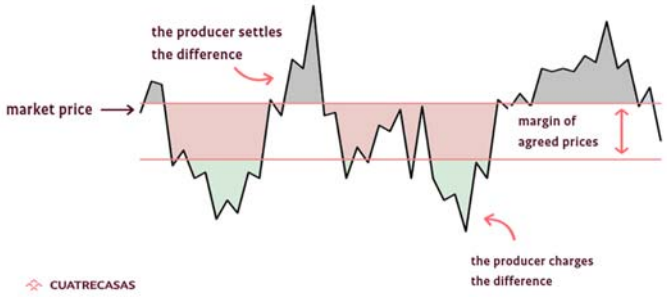
- The Member States will promote the uptake of PPAs, by **removing unjustified barriers and disproportionate or discriminatory charges**, so as to provide **price predictability and reach the objectives of decarbonization**, while preserving competitive and liquid electricity markets and crossborder trade.

- The Member States will ensure, in a coordinated manner, that **instruments for reducing the financial risks associated with the default of payment in the framework of PPAs are in place and accessible to clients that face entry barriers to the PPA market and that are not in financial difficulty.** Member States should be able to determine the categories of clients that are targeted by those instruments.

More stable revenue through CFDs

- The **support that Member States have from public funds for investment in new electricity-generating facilities using renewable resources** (wind, solar, geothermal, hydropower without reservoir and nuclear energy) will be provided through two-way **CFDs** or equivalent schemes with the same effects.

- CFDs are contracts between **power-generating facility operators** and a **counterpart**—usually a **public entity**—that provide both **minimum remuneration (floor) and a limit on excess remuneration (cap).** The producer sells the electricity in the market but then settles the difference between the market price and the strike price agreed in advance with the public entity.



- The Regulation states that the **participation** of market participants in direct price support schemes in the form of CFDs or equivalent schemes should be **voluntary.**

- The direct price support schemes in the form of CFDs or equivalent schemes must be orientated to efficient functioning in the electricity markets, avoiding any undue distortion to the market and to the competition. Remuneration amounts must be determined through an **open, transparent and non-discriminatory competitive bidding process.** The scheme ensures that the **level of the minimum remuneration protection** and of the upward limit to excess remuneration are **aligned with the cost of the new investment and the market revenues**, to guarantee the long-term economic viability of the power-generating facility while avoiding overcompensation.

- **Revenues of direct price support schemes** in the form of CFDs or equivalent schemes **should ultimately be passed on to final customers**, without prejudice to a certain flexibility granted to national authorities. They can also be used to **finance the costs of direct price support systems or investments, to reduce electricity costs for final customers.**

Support systems for non-fossil flexibility "payments for available capacity"

- The Regulation enables Member States to apply non-fossil flexibility support schemes consisting of **payments for the available capacity of non-fossil flexibility**, where **flexibility needs are not being addressed** enough to achieve the indicative national objective.

- These support schemes must respect the principle of **proportionality** and **avoid undue distortions** to the efficient functioning of the electricity markets.

- Providers must be selected using **competitive, non-discriminatory and cost-effective processes.**

Day-ahead and intraday market

- All products are negotiated in a **single coupling**.
- The **intraday cross-zonal gate closure time is shortened to 30 minutes ahead of real time**, so market participants can trade energy as close to real time as possible to better adapt to the participation of demand response and facilitate deployment of variable renewable energy sources and energy storage.
- The **minimum bid size of products provided by nominated electricity market operators (NEMO) is reduced** in the day-ahead and intraday market from 500kW or less to 100kW.
- The Regulation promotes **fixed-price grid tariffs** that foster market integration, the integration of renewable energy and security of supply; and supports the use of flexibility services, promoting efficient and timely investments.
- It recognizes the obstacles to the widespread and efficient deployment of **offshore renewable energy sources** and encourages using **instruments to reduce investment risks for offshore project developers (through PPAs or CFDs).** To reduce the risks associated with the unique topographical situation related to access to the offshore sources market, the transmission system operators who have not made available the capacity agreed in the connection agreements on the interconnector or have not made available the capacity on the critical network elements, should **compensate the developers**. The compensation should be paid from congestion income.
- **The mechanisms for coordinating, exchanging and supplying information between transmission system operators** are reinforced, as are **transparency obligations**. Transmission and distribution system operators must publish **clear information on the capacity available for new connections in their areas of operation** with high spatial granularity, as well as provide in a transparent manner, clear information to system users about the status and treatment of their connection requests.

For additional information, please contact our *Knowledge and Innovation Group* lawyers or your regular contact person at Cuatrecasas.