Making the internal energy market work

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PURPOSE: to set out an Action Plan on making the internal energy market work.

CONTENT: this communication recalls the benefits of integrated European energy markets and sets out ways to ensure that the market fulfils its potential as soon as possible and satisfies the needs and expectations of the EU's citizens and businesses. This initiative has been identified as one of the 12 priority actions under the Communication "Single Market Act II – Together for new growth. In spite of the progress made in the last few years in the functioning of the market, further efforts are needed to integrate the markets, improve competition and deal with new challenges.

As underlined by the Commission's Energy Roadmap 2050, **Europe's energy networks and systems and opening up energy markets further** are essential in making the transition to a low-carbon economy and maintaining secure supplies at the lowest possible cost. It stressed the need to:

- invest urgently in generation, transmission and distribution infrastructure, as well as storage. Existing energy systems need to be modernised, at a cost estimated at EUR 1000 billion);
- encourage more efficiency measures, stimulate fair competition, and empower consumers to take an active role and fully exercise their rights and choices.

Accordingly, the **European Heads of State or Government set a clear deadline of 2014 for completion of the internal energy market.**

By 2014 the existing legislation needs to be implemented in full. Cross-border markets for gas and electricity must be up and running in all parts of the EU and the implementation of plans to complete, modernise and smarten EU grids must be well under way. **Today the EU is not on track to meet this deadline:**

- the generation market is still highly concentrated. In eight Member States more than 80% of power generation is still controlled by the historic incumbent;
- energy markets in general are perceived not to be transparent or sufficiently open for newcomers, including demand-side service providers;
- economically rational investments in energy efficiency are not being made – or at least not enough;
- consumer satisfaction is low even in Member States that today have fairly competitive energy markets.

Challenges to be met: although the benefits of a well-functioning internal energy market are becoming progressively visible, there are challenges that need to be tackled urgently in order to complete the internal energy market by 2014.

(1) Implement internal market legislation and actively enforce competition rules: the architecture for the internal energy market is laid out in the Third energy package. The building blocks are there but they must be implemented effectively for the internal energy market to work.

The Commission is pursuing, as a matter of priority, infringement procedures against those Member States that have not yet fully transposed the Third energy package Directives or have failed to do so correctly. It intends to provide regular updates on the state of implementation of internal energy market legislation in individual Member States and on the infringement procedures.

Furthermore, the Commission:

- will enforce competition rules to ensure that all companies in the market are treated equally and that a level playing field is established and maintained;
- will press public authorities ensuring that concessions (e.g. for hydro power generation facilities, storage facilities or the operation of distribution grids), are awarded in full compliance with Treaty principles and EU legislation;
- will promote regional initiatives to help set up additional regional gas hubs and power exchanges, and reach the target of full market coupling in electricity across the EU as soon as possible.

Member States, for their part, must **stimulate competition by developing infrastructure**, in particular in support of cross-border activity, and eliminating market entry barriers.

(2) Help consumers take advantage of opportunities afforded by the internal market: currently, SMEs and households are more passive than large industrial customers and are therefore losing out as available price differentials remain unexploited.

In this area, the challenges are: i) enabling the **delivery of diverse and innovative services** to consumers; ii) ensuring targeted assistance to give vulnerable consumers better protection.

The Commission feels that timely deployment of **smart meters** as set out in the EU acquis can trigger demand-response and other innovative and smart services.

However, at present, **price regulation in many Member States prevents suppliers from offering attractive services** and tailor-made and dynamic pricing schemes. It discourages new entrants that could challenge the incumbents. In some Member States prices are even regulated by the State for some or all customer groups at levels below market costs. It is clear that such a situation is not conducive to the development of a competitive market and is economically unsustainable.

A recent European Court of Justice ruling states that price regulation can be compatible with EU law only under strictly defined circumstances.

In these circumstances, the Commission intends:

- to insist on **phase-out timetables for regulated prices** being part of Member States' structural reforms;
- to promote market-based price formation in retail markets, including through infringement cases against those Member States maintaining price regulation that is not meeting the conditions laid down by EU law;
- to support Member States in defining what is meant by and what causes energy consumers' vulnerability by providing guidance and facilitating the exchange of best practice.

(3) Making Europe's energy systems fit for the future: energy systems are in the early phase of a major transition. Significant investments are needed to replace the EU's ageing systems, decarbonize them and make them energy-efficient and increase security of supply. The internal energy market can help the EU make the transition. However, **the system change cannot take place without a properly integrated, modern infrastructure.** The Commission will act on several issues:

- ***Wholesale markets:*** the Commission considers that properly functioning long-term and short-term wholesale markets, which reflect the economic value of power at each point in time in each area can steer investments to where they are most efficient.

The Commission will ensure the **further development of well-functioning, cross-border, wholesale markets in all timeframes** by developing network codes. These codes will establish common rules to enable network operators, generators, suppliers and consumers to operate more effectively within the market.

- *Security of supply in electricity:* some Member States have introduced or plan to introduce separate payments for the market availability of generation capacity, as they are concerned that the 'energy only' market will not deliver sufficient investment in generation to ensure security of supply in the longer term.

The Commission is of the view that if capacity mechanisms are not well designed and/or are introduced prematurely or without proper co-ordination at EU level, they risk being counterproductive, since they will tend to distort investment signals. Accordingly, before introducing such mechanisms, Member States should: (i) **carry out a full analysis of whether there is a lack of investment in generation, and why;** (ii) seek cross-border solutions to any problems they find before planning to intervene.

- *Steering the energy mix to low carbon*: currently, Member States use various forms of direct or indirect state support and/or surcharges on consumers' bills for a range of energy sources. Assuming further progress in completing the internal energy market, falling production costs, and evolution in the carbon market, all forms of support mechanisms need to be regularly reviewed.

The Commission will **issue guidance on best practice and experience gained in renewable energy support schemes and on support scheme reform**.

- *More integration, faster modernisation and better use of grids*: serious investment in energy networks is needed to enable certain areas of the EU to emerge from isolation and to achieve our Europe 2020 targets. In October 2011, the Commission tabled a proposal for a Regulation on "Guidelines for trans-European energy infrastructure." The adoption and swift implementation of the energy infrastructure packet is essentia as acknowledged by the European Council on 9 December 2011.

Lastly, with the growing need for flexibility and energy efficiency and to accommodate distributed generation and demand-side participation, co-ordinated action is needed with a view to the **deployment of smart grids at European, regional and municipal levels.**

The Commission intends to: (i) further support R&D and innovation to facilitate the deployment of smart grids; (ii) promote pro-competitive co-operation between the energy and the ICT sector, including innovative service providers for advancing the modernisation of grids and accelerating innovation in the energy sector.