Internal market for electricity: safeguard security of supplies, infrastructure investment

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COMMISSION'S IMPACT ASSESSMENT

1. PROBLEM IDENTIFICATION

Currently, there are a number of undesirable and unsustainable trends emerging in European electricity markets which jeopardise the Commission's objectives to ensure sustainability, enhance security and supply and improve competitiveness. It is vital to ensure that different Community policies, targeted on the above-mentioned three objectives, are compatible and that the configuration of the physical characteristics of the network, market structure and technology are in place to deliver these objectives. Of particular concern is the need for measures relating to infrastructure development and relating to security of supply.

For more information regarding the context of this problem, please refer to the complementary summaries of Communications COM(2003)0743 and COM(2003)0740.

2. OBJECTIVE

This paper is intended to address some key outstanding issues which, in particular, relate to the need for additional transmission investment, to include environmental considerations in network investment decisions, as well as the need for a clearly policy statement to be made by Member States concerning the market for electricity generation and ensuring a balance between supply and demand. Security of electricity supply is important since the use of electricity is central to the functioning and well-being of society. New interconnections are required at EU level to support the internal market and to allow for competition between the existing electricity companies in Europe. Without this happening, and in the absence of measures by Member States to reduce the dominant position of the largest companies, the possibility of choosing between different suppliers will remain an illusion for many customers.

The proposal addresses **the need for Member States to have a stable regulatory framework for maintaining the supply-demand balance**.

3. POLICY OPTIONS AND IMPACTS

3.1 – "Do nothing" approach: this leaves the Member States to find a solution on an individual basis with only ad-hoc bilateral co-operation as considered necessary. On the issue of **transmission**, this would leave decisions on infrastructure up to Member States and more specifically transmission system operators (TSOs). **This was rejected** because, firstly, a number of TSOs are vertically integrated and, secondly, in some Member States, regulatory practice is not conducive to new infrastructure investments and this

creates problems when considering the issue at European level. A further variation of the 'do-nothing' approach would be for the Commission to stop in its efforts to accelerate cross border interconnection. Such an approach would rely on new investment in the generation market to deliver the competition goals of the Community.

In relation to the issue of **balancing supply and demand,** there are also some key choices to be made. This approach would mean that the only obligations on Member States would be those contained in the new Electricity Directive (2003/54). This already obliges Member States to monitor the supply-demand balance and report to the Commission.

The '**do nothing' option** would probably mean **negative consequences from the environmental point of view**. Offshore wind farm would, for example, have a more limited impact on the internal market. Similar criticisms apply to a "**weaker version"** of the proposal to the extent that this would mean slower progress with the projects under discussion.

Moreover, this option would **reduce the one-off investment costs but this would damage the functioning of the competitive market** and mean that the ongoing benefits of competition would be forgone. The main effect of the proposal is to accelerate the effectiveness of introducing competition as discussed in the section above. On the other hand, this approach might be the **preferred option for consumers** since they are familiar with the current framework and may not welcome being asked to think more about their consumption decisions.

3.2 - "Light" approach: the Commission can choose to play a co-ordinating role by encouraging the Member States to co-operate more generally in formulating their policies but without any obligations.

A lighter version of the proposal requiring, for example, more voluntary coordination, would risk realising only part of the benefits. Since the above analysis suggests the benefits of the investments being covered outweigh the costs, this is also rejected. There is also the problem of asymmetric implementation of, for example, the requirement to publish a supply-demand policy which would risk problems of market distortion and free-riding. This approach would be to merely strengthen the existing co-operative approach through, for example, the Florence Forum and the existing co-operation between the Commission and national regulators. This approach **was also rejected since these discussions are a voluntary arrangement and experience has shown that it is difficult to get many difficult concrete issues resolved through such arrangements without binding rules.** Since part of the objective is to remove regulatory risk, a voluntary approach might even be a disincentive to investment.

3.3 - "A more interventionist approach": is one where the Commission seeks to place obligations on Member States to fulfil certain requirements in how they organise their policy on the issue concerned and how they interact with each other. The most extreme intervention is where the Commission would propose a Community-level solution to the problem being considered. **More interventionist possibilities**, such as the introduction of a common standard for reserve capacity or a common EU approach to the generation market **were rejected due to subsidiarity reasons and the recognition that the reality of the electricity market still amounts to national or regional markets that are not very well interconnected**.

CONCLUSION: for the current proposal relating to **infrastructure**, the approach taken is mainly in terms of coordination of practice in existing Member States with some obligation to provide a framework compatible with regulated third party access and some reporting obligations on projects of European Interest. **The proposed approach is therefore relatively "light".**

Concerning **security of supply**, the approach is **more prescriptive** in that is requires Member States to have a clearly defined policy for this subject. It does, however, leave a considerable amount of choice available to Member States as to the approach to be taken.

5. FOLLOW-UP

Relating to infrastructure, the TEN guidelines envisage that, **every two years**, the Commission shall draw up a report on the implementation of the projects of common interest as listed in the TEN-E Guidelines. Regarding **supply and demand**, there is already an obligation in the existing Electricity Directive on Member States and the Commission to co-operate in producing a regular report monitoring the position. This will be extended somewhat by the new proposal since the Commission will also be required to monitor the coherence of the different approaches in Member States and seek to minimise any distortions that might arise.